



AUSTRALASIAN
COUNCIL OF
AUDITORS-GENERAL

9 August 2010

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

Dear Mr Stevenson,

ED 195 DEFINED BENEFITS PLANS

Please find attached the Australasian Council of Auditors-General (ACAG) response to the Exposure Draft referred to above.

I have also attached ACAG's comments to the International Accounting Standards Board on related IASB ED/2010/3.

The views expressed in this submission represent those of all Australian members of ACAG except the Auditors-General of the Northern Territory and the Australian Capital Territory.

The opportunity to comment is appreciated and I trust you will find the attached comments useful.

Yours sincerely

A handwritten signature in black ink, appearing to read 'S O'Neill', is written over a horizontal line.

Simon O'Neill
Chairman
ACAG Financial Reporting and Auditing Committee

ACAG RESPONSE TO AASB SPECIFIC MATTERS FOR COMMENT

1. The Preface to AASB 1049 Whole of Government and General Government Sector Financial Reporting notes that, as a result of potential amendments to the requirements in other Australian Accounting Standards, differences between Generally Accepted Accounting Principles (GAAP) and Government Finance Statistics (GFS) not contemplated in AASB 1049 may eventuate. Consistent with the AASB's comments in the Preface to AASB 1049 addressing this matter, the AASB will have regard to the implications for whole of government and GGS financial reporting in deciding whether to amend the proposals in this ED or the requirements in AASB 1049 to either avoid or confirm the existence of a difference. In that regard, do you think the proposed changes to the treatment of:

- (a) past service cost;**
 - (b) gains and losses arising from curtailments;**
 - (c) net interest on the net defined benefit liability (asset); or**
 - (d) remeasurements of the net defined benefit liability (asset);**
- would have implications for GAAP/GFS harmonisation and, if so, how do you think those implications should be dealt with in the context of the principles in AASB 1049?**

ACAG believes that the proposed changes to the accounting for defined benefit superannuation plans would align AASB 119 to the accounting treatments required under GFS, particularly by eliminating the option to not recognise certain portions of a defined benefit liability (the 'corridor' approach). Therefore ACAG does not believe any action is necessary in the context of GAAP-GFS harmonisation.

2. Do you agree that the proposed amendments to the definition of 'return on plan assets' and paragraph 73(b)(iv) of IASB's ED/2010/3 Defined Benefit Plans clarify the treatment of superannuation contributions tax in accounting for defined benefit obligations? If not, please explain why.

Some government defined benefit plans in Australia are subject to superannuation contributions tax. ACAG agrees that the proposed amendments are reasonable.

3. The AASB would particularly value comments on whether:

- (a) in addition to the issues raised in relation to Question 1 above, 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:
 - (i) not-for-profit entities; and**
 - (ii) public sector entities;****
- (b) overall, the proposals would result in financial statements that would be useful to users; and**
- (c) the proposals are in the best interests of the Australian and New Zealand economies.**

ACAG draws the AASB's attention to the ACAG response to Question 16 of IASB ED/2010/3. Specifically, ACAG is concerned about the cost that some entities will incur as a result of the accounting requirements for defined benefit plans being extended to other long-term liabilities such as long-service leave.

ACAG does not envisage any other issues that may affect the implementation of the proposals by public sector entities. With the exceptions set out in ACAG's comments to the IASB on ED/2010/3, ACAG believes the proposals would result in financial statements that are useful to users.



AUSTRALASIAN
COUNCIL OF
AUDITORS-GENERAL

9 August 2010

Sir David Tweedie
Chairman
International Accounting Standards Board
1st Floor 30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir David,

EXPOSURE DRAFT ED/2010/3 DEFINED BENEFIT PLANS

Please find attached the Australasian Council of Auditors-General (ACAG) response to the Exposure Draft referred to above.

The views expressed in this submission represent those of all Australian members of ACAG except the Auditors-General of the Northern Territory and the Australian Capital Territory.

The opportunity to comment is appreciated and I trust you will find the attached comments useful.

Yours sincerely

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Simon O'Neill
Chairman
ACAG Financial Reporting and Auditing Committee

cc: Mr Kevin Stevenson, Chairman, Australian Accounting Standards Board

**COMMENTS BY THE AUSTRALASIAN COUNCIL OF AUDITORS-
GENERAL ON IASB ED/2010/3 DEFINED BENEFIT PLANS PROPOSED
AMENDMENTS TO IAS 19**

Recognition

Question 1

The exposure draft proposes that entities should recognise all changes in the present value of the defined benefit obligation and in the fair value of plan assets when they occur. (Paragraphs 54, 61 and BC9–BC12) Do you agree? Why or why not?

Yes. ACAG agrees with the proposal for entities to immediately recognise employee benefit costs in the period in which they occur. The amount recognised in the balance sheet may be confusing and misleading if entities do not recognise gains and losses when they arise.

Question 2

Should entities recognise unvested past service cost when the related plan amendment occurs? (Paragraphs 54, 61 and BC13) Why or why not?

Yes, because the amendment of the plan in such circumstances gives rise to a liability in the period of amendment.

Disaggregation

Question 3

Should entities disaggregate defined benefit cost into three components: service cost, finance cost and remeasurements? (Paragraphs 119A and BC14–BC18) Why or why not?

Yes. It is particularly important that remeasurements should be separated out because they have different predictive values. For example, a change in the rate used to discount long-term benefits can have a major impact on the measurement of a defined benefit liability, but does not provide information about future cash flows.

Defining the service cost component

Question 4

Should the service cost component exclude changes in the defined benefit obligation resulting from changes in demographic assumptions? (Paragraphs 7 and BC19–BC23) Why or why not?

Yes, because changes in demographic assumptions will have a different predictive value from the actual service cost.

Defining the finance cost component

Question 5

The exposure draft proposes that the finance cost component should comprise net interest on the net defined benefit liability (asset) determined by applying the discount rate specified in paragraph 78 to the net defined benefit liability (asset). As a consequence, it eliminates from IAS 19 the requirement to present an expected return on plan assets in profit or loss.

Should net interest on the net defined benefit liability (asset) be determined by applying the discount rate specified in paragraph 78 to the net defined benefit liability (asset)? Why or why not? If not, how would you define the finance cost component and why? (Paragraphs 7, 119B, 119C and BC23–BC32)

Yes, net interest should be determined by applying the discount rates specified in paragraph 78 to the net defined benefit liability (asset). This approach has the advantage of simplicity and reflects the reality that entities are financing a net liability (asset).

Presentation

Question 6

Should entities present:

(a) service cost in profit or loss?

(b) net interest on the net defined benefit liability (asset) as part of finance costs in profit or loss?

(c) remeasurements in other comprehensive income?

(Paragraphs 119A and BC35–BC45) Why or why not?

Yes. ACAG believes the proposals will improve the visibility of different types of gains and losses arising from defined benefit plans. Service cost and net interest should be presented in profit or loss. In the absence of guidance from the Framework on the nature of other comprehensive income, ACAG agrees with reporting remeasurements in other comprehensive income; this would prevent revisions of actuarial assumptions, which can result in large movements, from distorting profit and loss for the current period.

Settlements and curtailments

Question 7

(a) Do you agree that gains and losses on routine and non-routine settlement are actuarial gains and losses and should therefore be included in the remeasurement component? (Paragraphs 119D and BC47) Why or why not?

(b) Do you agree that curtailments should be treated in the same way as plan amendments, with gains and losses presented in profit or loss? (Paragraphs 98A, 119A(a) and BC48)

(c) Should entities disclose (i) a narrative description of any plan amendments, curtailments and non-routine settlements, and (ii) their effect on the statement of comprehensive income? (Paragraphs 125C(c), 125E, BC49 and BC78)

Why or why not?

- (a) Yes, the gain or loss on settlement should be included in the remeasurement component.
- (b) Yes.
- (c) Yes, because it is important for users to understand the nature and impact of adjustments arising from these transactions.

Disclosures

Defined benefit plans

Question 8

The exposure draft states that the objectives of disclosing information about an entity's defined benefit plans are:

- (a) to explain the characteristics of the entity's defined benefit plans;**
- (b) to identify and explain the amounts in the entity's financial statements arising from its defined benefit plans; and**
- (c) to describe how defined benefit plans affect the amount, timing and variability of the entity's future cash flows. (Paragraphs 125A and BC52–BC59). Are these objectives appropriate? Why or why not? If not, how would you amend the objectives and why?**

Yes, with one exception. ACAG does not believe that explaining the characteristics of the entity's defined benefit plans should be an objective in itself. Instead, it is a means to achieving other objectives, such as the aiding the reader to understand the effect on the entity's future cash flows.

ACAG suggests instead that objective (a) be deleted and the current wording of paragraph 125 be prefaced with "Where necessary to an understanding of the impact on the amount, timing and uncertainty of the entity's future cash flows...".

Question 9

To achieve the disclosure objectives, the exposure draft proposes new disclosure requirements, including:

- (a) information about risk, including sensitivity analyses (paragraphs 125C(b), 125I, BC60(a), BC62(a) and BC63–BC66);**
- (b) information about the process used to determine demographic actuarial assumptions (paragraphs 125G(b) and BC60(d) and (e));**
- (c) the present value of the defined benefit obligation, modified to exclude the effect of projected salary growth (paragraphs 125H and BC60(f));**
- (d) information about asset-liability matching strategies (paragraphs 125J and BC62(b)); and**
- (e) information about factors that could cause contributions to differ from service cost (paragraphs 125K and BC62(c)).**

**Are the proposed new disclosure requirements appropriate? Why or why not?
If not, what disclosures do you propose to achieve the disclosure objectives?**

Yes, with one exception. ACAG does not believe that entities should be required to disclose the present value of the defined benefit obligation modified to exclude the effect of projected salary growth. It is not clear to ACAG that this disclosure would be useful, and it could be argued that providing alternative measures of liabilities might suggest that the liability in the balance sheet was somehow incorrect.

The Basis for Conclusions suggests one reason for this disclosure is that it represents, in some circumstances, the amount that would be paid on termination of the plan. If information about the amount that would be paid on termination is considered important, ACAG suggests a specific requirement to this effect be included. This could be along the lines of “Where there is a non-remote possibility that a plan would be terminated within twelve months from the end of the reporting period, the entity shall disclose the amount that would be required to settle the net defined benefit obligation at the end of the reporting period”.

Multi-employer plans

Question 10

The exposure draft proposes additional disclosures about participation in multi-employer plans. Should the Board add to, amend or delete these requirements? (Paragraphs 33A and BC67–BC69) Why or why not?

No. ACAG believes the proposed disclosures are relevant and sufficient.

State plans and defined benefit plans that share risks between various entities under common control

Question 11

The exposure draft updates, without further reconsideration, the disclosure requirements for entities that participate in state plans or defined benefit plans that share risks between various entities under common control to make them consistent with the disclosures in paragraphs 125A–125K. Should the Board add to, amend or delete these requirements? (Paragraphs 34B, 36, 38 and BC70) Why or why not?

ACAG believes that the requirement in paragraph 34B(d) to disclose information about the plan as a whole is excessive, because it requires each participating entity in a group’s defined benefit plan to repeat disclosures already made by the entity that is the sponsoring employer. Instead, ACAG suggests that such entities include a reference to the disclosure in the publicly available financial statement of the sponsoring employer entity. Only if the sponsoring employer entity does not produce publicly available financial statements, should all participating entities in the group be required to provide information for the plan as a whole.

Other comments

Question 12

Do you have any other comments about the proposed disclosure requirements? (Paragraphs 125A–125K and BC50–BC70)

ACAG welcomes the proposals for sensitivity analysis whereby entities would be required to disclose the effect of reasonably possible changes to significant actuarial assumptions on the defined benefit obligation and service cost. These proposals will provide users with a greater understanding of the risks underlying amounts included in the financial statements.

In addition, ACAG notes that the proposals for sensitivity analysis are consistent with the requirements contained within IAS 1 *Presentation of Financial Statements* on the sources of estimation uncertainty.

Other issues

Question 13

The exposure draft also proposes to amend IAS 19 as summarised below:

- (a) The requirements in IFRIC 14 IAS 19—The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction, as amended in November 2009, are incorporated without substantive change. (Paragraphs 115A–115K and BC73)**
- (b) ‘Minimum funding requirement’ is defined as any enforceable requirement for the entity to make contributions to fund a post-employment or other long-term defined benefit plan. (Paragraphs 7 and BC80)**
- (c) Tax payable by the plan shall be included in the return on plan assets or in the measurement of the defined benefit obligation, depending on the nature of the tax. (Paragraphs 7, 73(b), BC82 and BC83)**
- (d) The return on plan assets shall be reduced by administration costs only if those costs relate to managing plan assets. (Paragraphs 7, 73(b), BC82 and BC84–BC86)**
- (e) Expected future salary increases shall be considered in determining whether a benefit formula expressed in terms of current salary allocates a materially higher level of benefits in later years. (Paragraphs 71A and BC87–BC90)**
- (f) The mortality assumptions used to determine the defined benefit obligation are current estimates of the expected mortality rates of plan members, both during and after employment. (Paragraphs 73(a)(i) and BC91)**
- (g) Risk-sharing and conditional indexation features shall be considered in determining the best estimate of the defined benefit obligation. (Paragraphs 64A, 85(c) and BC92–BC96). Do you agree with the proposed amendments? Why or why not? If not, what alternative(s) do you propose and why?**

ACAG agrees with the proposed amendments.

Multi-employer plans

Question 14

IAS 19 requires entities to account for a defined benefit multi-employer plan as a defined contribution plan if it exposes the participating entities to actuarial risks associated with the current and former employees of other entities, with the result that there is no consistent and reliable basis for allocating the obligation, plan assets and cost to individual entities participating in the plan. In the Board's view, this would apply to many plans that meet the definition of a defined benefit multiemployer plan. (Paragraphs 32(a) and BC75(b))

Please describe any situations in which a defined benefit multi-employer plan has a consistent and reliable basis for allocating the obligation, plan assets and cost to the individual entities participating in the plan. Should participants in such multi-employer plans apply defined benefit accounting? Why or why not?

ACAG is not aware of any such plans.

Transition

Question 15

Should entities apply the proposed amendments retrospectively? (Paragraphs 162 and BC97–BC101) Why or why not?

Yes. Although there will be an actuarial cost to recalculate comparative figures based on the proposals, ACAG does not believe that retrospective application would be unduly onerous.

Benefits and costs

Question 16

In the Board's assessment:

- (a) the main benefits of the proposals are:**
- (i) reporting changes in the carrying amount of defined benefit obligations and changes in the fair value of plan assets in a more understandable way.**
 - (ii) eliminating some presentation options currently allowed by IAS 19, thus improving comparability.**
 - (iii) clarifying requirements that have resulted in diverse practices.**
 - (iv) improving information about the risks arising from an entity's involvement in defined benefit plans.**
- (b) the costs of the proposal should be minimal, because entities are already required to obtain much of the information required to apply the proposed amendments when they apply the existing version of IAS 19.**

Do you agree with the Board's assessment? (Paragraphs BC103–BC107) Why or why not?

Overall, ACAG agrees with the Board's assessment. However, ACAG notes that increased costs will flow to entities that provide long-term benefits that are not currently 'post-employment' benefits, such as long service leave. Currently, movements in such benefits are recognised entirely in profit and loss and no specific disclosures are imposed by IAS 19. The proposed amendments would mean that all long-term benefits would be accounted for in the same way as post-employment benefits.

Many Australian entities are not currently gathering the information required to apply the proposed amendments in respect of long service leave. In particular, some groups engage actuaries to determine a basis for estimating the long service leave liability that can be used for all entities in the group. Breaking down the movement in the liability to the three areas of cost would be difficult to perform on an entity-by-entity basis. ACAG asks that the IASB take into account the implications of benefits such as long service leave being captured by the definition of ‘defined benefit plans’.

ACAG does not believe that applying the proposed disclosures to all long-term benefits can be justified on cost-benefit grounds. ACAG proposes that long-term benefits that are not post-employment benefits should be exempted from the disclosures proposed in paragraphs 125A to 125K.

Other comments

Question 17

Do you have any other comments on the proposals?

ACAG has some further comments regarding the definitions in the proposals.

Paragraph 4 of the ED states the following:

Employee benefits include:

(a)...

(b) long-term employee benefits such as...long service leave....

The definition of long-term employee benefits provided under paragraph 7 captures benefits expected to be due to be settled 12 months or more after the end of the reporting period in which the employee renders the related service (as well as post-employment benefits). ACAG recommends that the IASB amend the Scope section (paragraph 4) to indicate that long service leave may not always be a long-term employee benefit.

If the intention of the IASB is that long-service leave and similar liabilities are to be captured by the terms ‘defined benefit plans’ or ‘defined contribution plans’, this should be made clearer in the body of the standard, particularly as a natural reading of ‘defined benefit plan’ would not ordinarily lead to the conclusion that long-service leave liabilities would be captured.

ACAG also recommends that clause (b) of the definition of long-term employee benefits be amended to read “*on or* after the completion of employment”. This would remove the possibility that the definitions would not address an employee benefit expected to be due to be settled at the time of termination of the employee. For example, an employee might be entitled to be paid their accumulated leave liability on termination of employment.

Finally, ACAG is of the view that the objectives of comparability and understandability of financial statements will be improved as a result of the proposals, in particular, the removal of the ‘corridor approach’ option, whereby gains and losses from previous periods were allowed to be presented in the current period, therefore preventing a clear understanding of the gains and losses that arose in the current period.