

XX September 2006

D19 Comment Letters
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
UK

DRAFT COMMENT LETTER

Comments should be sent to Commentletter@efrag.org by
24 October 2006

Dear Sir/Madam,

Re: IFRIC Draft Interpretation D19 *IAS 19-The Asset Ceiling: Availability of Economic Benefits and Minimum Funding Requirements*

On behalf of the European Financial Reporting Advisory Group (EFRAG) I am writing to comment on the IFRIC Draft Interpretation D 19 *IAS 19-The Asset Ceiling: Availability of Economic Benefits and Minimum Funding Requirements* (D19). This letter is submitted in EFRAG's capacity of contributing to IASB's due process and does not necessarily indicate the conclusions that would be reached in its capacity of advising the European Commission on endorsement of the definitive interpretations/amendments on the issues.

D19 clarifies when economic benefits in the form of a refund or reductions in future contributions to the plan may be considered 'available' under the asset ceiling test in IAS 19.58. It further provides guidance on the effect of minimum funding requirements on the measurement of the (net) defined benefit asset or liability.

We agree with IFRIC that these issues are widespread and that there is the potential for divergence in practice. Indeed, we note that the issue could become more widespread in Europe as a result of EC Directive 2003/41 on the activities and supervision of institutions for occupational retirement provision. We therefore welcome IFRIC's decision to develop an Interpretation on the subject.

D19 proposes that:

- it is *not* necessary for an economic benefit in the form of a refund of, or reductions in, future contributions to be *immediately* realisable at the balance sheet date for the economic benefit to be considered 'available' under IAS 19.58;

EFRAG draft letter on D19

- the measurement of 'available' economic benefits in form of reductions in future contributions shall be determined, for each year of the expected plan life, as the present value of the service cost to the entity less any future minimum funding contributions associated with the benefits accrued; and
- if the reporting entity has a statutory or contractual obligation to pay additional contributions into a plan in respect of employee services already received, those additional contributions need to be evaluated to determine whether they are 'available' (via refunds or reductions in contributions) to the entity. If (and to the extent that) they will not be available after they are paid into the plan:
 - the entity should reduce the (net) defined benefit asset or increase the defined benefit liability when the obligation arises such that no gain or loss is recognised from the (subsequent) calculation of the asset ceiling under IAS 19.58 when the contributions are paid; and
 - the adjustment should be taken to profit and loss or to equity (statement of recognised income and expense) in accordance with the current options under IAS 19.93-93C.

We broadly support these proposals and, therefore, D19. However, we wish to draw to your attention some detailed matters that if addressed we would believe result in the Interpretation being clearer and even more useful. Those matters are set out in the appendix to this letter.

If you would like further clarification of the points raised in this letter, Knut Tonne or I would be happy to discuss these further with you.

Yours sincerely,

Stig Enevoldsen
EFRAG, Chairman

Appendix

Areas of D19 that we believe could usefully be clarified or improved

Scope

- 1 Paragraph 5 of D19 states that the draft applies to "all long-term and post employment benefit plans that are within the scope of IAS 19". IAS 19 applies to employee benefits that do not fall within the scope of IFRS 2; and IAS 19.4 explains that 'employee benefits' include short-term employee benefits, post-employment benefits, other long-term employee benefits and termination benefits. A literal interpretation of the differences in these wordings would suggest that short-term employee benefits and termination benefits are within the scope of IAS 19 but outside the scope of D19. We understand that IFRIC wishes to exclude short-term employee benefits from D19's scope —because they are not long-term—but our understanding is that the intention was to include termination benefits.

We believe that, if the wish was to exclude only short-term employee benefits, IFRIC should use the same wording as in IAS 19.4 to avoid any misunderstandings. Whatever the intended scope, it needs to be very clear.

Consensus on the economic benefit available as a refund

- 2 The text in parenthesis in D19.9(a) refers to the possibility that the entity might have a contractual right to receive a refund. We are concerned that, although the purpose of this reference is just to make it clear that such rights should be taken into account for the subsequent measurement/application of the availability test in IAS 19.58, it might be misunderstood to have implications for what qualifies as a so called plan asset under IAS 19.7. For that reason it would be helpful to clarify exactly what the implications of this reference are. It would in particular be helpful to make it clear the contractual right to refund does not conflict with IAS 19.7's definition of plan assets.

We raise this concern because the question of what can be transferred back to the reporting entity (meaning what can be called or seen as 'sufficient' under IAS 19.7(b)(i)) has been a much debated issue among constituents recently.

Consensus on the economic benefit available as a contribution reduction

- 3 D19 proposes that the economic benefit available as a contribution reduction should be measured with reference to the amount of contributions that the entity would have had to pay if it had no surplus. It goes on to state that this is best represented by the cost to the entity of accruing benefits in the plan, so should be calculated by reference to the future IAS 19 service cost (see paragraph BC17).

However, we think that the method proposed in D19.13 for calculating this amount is not clear. For example, assume that an entity has already impaired its pension asset to zero (because there were no economic benefits available under the assumption of no unrecognised actuarial gains and losses) under IAS 19.58. Under D19.13 that entity might now have to account for a defined benefit liability because of the minimum funding requirements. Is that the intention?

This is illustrated in the example below.

Assume:

Net asset in accordance with IAS 19.54: 100

EFRAG draft letter on D19

| | |
|--------------------------------------|-----|
| Future service cost (13 (a) of D19): | 120 |
| Minimum funding requirements: | 150 |

The calculation under IAS 19.58 in connection with D19.13 would then turn the asset of 100 into a liability of 30 (120-150). This outcome seems appropriate by looking at the onerous contracts provisions in IAS 37. Indeed, it should probably have been the outcome also before D19 (ie under current IAS 19 which takes precedence over IAS 37, see IAS 19.1 and IAS 37.1(c)) as this requirement at least should qualify as a constructive obligation. This conclusion might also be reached by looking at D19.18 and an analogy to the second illustrative example.

However the above scenario of turning an asset into a liability is not specifically mentioned in D19. D19.IE2 covers the case where the minimum funding requirements are not fully available, but that already starts with a defined benefit liability (not an asset). One could argue that the last sentence of D19.16, which states that “the amount of the total asset available as a reduction in future contributions can never be less than zero”, implies that in the above example the outcome would be only to fully impair the asset, but not accounting for the 30 as liability. Another interpretation of this sentence could be that it applies only for the calculation of the asset ceiling under IAS19.58.

We think it would be useful if clarifying words (that also refer to the appropriate paragraphs in IAS 19 if a liability is assumed to be accounted for) were added to the draft interpretation or/and an example covering the issue were added.

Effective date and transitional arrangements

- 4 EFRAG believes that the general principle should be that all new Interpretations and new or revised IFRSs should apply retrospectively. For that reason, we support the proposal in D19 for full retrospective application.

Question for EFRAG's constituents

We have considered whether all the information would be available to enable the Interpretation to be retrospectively. We think this could arise only if neither the entity nor its actuaries have the necessary information concerning the expectation of future minimum funding requirements (as discussed in D19.14), which might conceivably be the case if there was no need for an asset ceiling test in accordance with IAS 19.58.

We would particularly welcome comments from respondents on this issue.

Illustrative examples

- 5 Finally we would like to share three observations in respect of the illustrative examples:
 - (a) In the examples 2 and 3 the contributions are discussed in the text, but have not been taken into account in the actual numbers. This should be correct as the contributions have not been paid yet; however, this might be made clearer at least in a footnote.
 - (b) As outlined above, the contribution in Example 2 is paid after the balance sheet date looked at and therefore not been taken into account. So Example 2 starts with a *deficit* of 100. The asset ceiling test only comes into effect when there is an *asset* (IAS 19.58 first sentence in connection with IAS 19.54). So the question is how example 2 can be an explanation of the requirements in this draft in connection with IAS 19.58.

EFRAG draft letter on D19

- (c) We recognise that the draft interpretation in general as well as the examples are not including any actuarial gains and losses and past service costs. We understand that this avoids introducing complexity where it is not needed. However we believe that it might be worth stating that probably the changes of expectations of future minimum funding requirements as described in paragraph 14 of D19 would fall under actuarial gains and losses (may be depending on IFRIC's view on the third issue above). In that case it might be worth clarifying by inserting some words in the draft interpretation or/and adding an example including actuarial gains and losses.