Rådet för finansiell rapportering

The Swedish Financial Reporting Board

RFR-rs 2010:08

International Accounting Standards Board
30 Cannon Street
London EC4M 6 XH
United Kingdom

Dear Sirs,

Re: Exposure Draft ED/2010/03 Defined Benefit Plans Proposed amendments to IAS 19

The Swedish Financial Reporting Board is responding to your invitation to comment on the International Accounting Standard Board's Exposure Draft ED/2010/3 Defined Benefit Plans Proposed amendments to IAS 19.

We consider that a comprehensive approach should be taken as to the accounting for post retirement benefits. As a consequence, we do not support that IAS 19 is amended to bring about a short term solution to presentation matters before a comprehensive solution is achieved and consider that all the three presentation alternatives presently available can continue to be used until such a solution exists. If the IASB however chooses to implement the Exposure Draft we want to highlight some weaknesses in the proposal:

- We do not support the suggestion by the IASB to eliminate the requirement to present an expected return on plan assets in profit or loss. We believe this measure is more relevant than the discount rate for estimating the yield on plan assets, and we do not agree that IASB should implement accounting rules that provide less relevant information in order to avoid management judgement and subjectivity (anti-abuse measures).
- The guidance with regard to determination of the discount rate needs to be amended. As further explained below, the current rules lead to higher pension liabilities as well as pension costs in countries where the government bond rates should be used and the suggestion in the ED to use the discount rate also for estimating the yield on plan assets will further increase those differences.
- We do not support that a standard should prescribe where the different components of pension expense should be recognized in the income statement in advance of the finalization of the financial statement presentation project. Interim measures in this regard are not warranted at this time.
- Actuarial gains and losses recognised in other comprehensive income should later be recycled to the income statement.
- The pension liability should not be measured based on future salary increases but should only reflect benefits for which a present commitment exists.

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- The disclosure requirements are too extensive. We question if the increase in these is of such benefit to the users that it makes up for the added costs for the preparers.

Our detailed comments are as follows:

Elimination of the requirement to present an expected return on plan assets in profit or loss

We believe that such a measure is more relevant than the discount rate for estimating the yield on plan assets, and we do not agree that IASB should implement accounting rules that provide less relevant information in order to avoid management judgement and subjectivity (anti-abuse measures).

Plan assets are usually made up of many different types of investments, and using the return on high quality corporate bonds would be arbitrary and would not be a faithful representation of the return that investors require or expect from each type of asset. We believe that the return on plan assets recognized in the income statement must reflect the actual composition of plan assets into shares, property, corporate bonds and government bonds. If plan assets are mainly invested into shares, an entity would expect to receive a return of such investments that exceeds the corporate bond rate (government bond rate) significantly. It appears reasonable to assume that the return on a diversified share portfolio in the long run exceeds the risk free rate by at least 3 – 4 per cent. Accordingly, there will be a systematic underestimation of the expected return on plan assets, thus resulting in an increased pension expense and a systematic allocation of profits to other comprehensive income. We do not see that this provides a faithful representation of the underlying pension expense.

We agree that determining the expected return on plan assets requires judgement by management, but this does not mean that the expected return on plan assets is unreliable. We believe that estimating the expected return on plan assets require the same degree of judgement as do other estimates.

Lack of proper guidance in determining the discount rate

It is important to consider that there are several countries in the world that do not have deep markets in high quality corporate bonds. In such circumstances, the present standard requires entities to use government bond rates when determining their pension obligation. We strongly believe that under the current IAS 19 reporting rules, such entities are significantly disadvantaged compared to peer companies in the Euro zone, the UK and the US where deep markets in corporate bonds exist. This has resulted in equal pension obligations (equal future cash flows to pay pension benefits to retirees) for companies in such countries are valued at much higher amounts than in companies in the euro zone, UK and US due to the difference between corporate and government bond rates. We believe this situation is unacceptable. The risks involved with future cash flows (pension payments) are unaffected by if there is a deep market in corporate bonds or not. An example highlighting the enormous effect of what is described above would be a situation where one would have a government bond rate of 3,9% and a corporate bond rate in a country such as the US of 5,75 %, which would give a lower liability in the US of some 30% for an identical pension obligation.

This situation highlights the need to review the issue of determination of the discount rate expeditiously in order to create a level playing field between countries that do not have deep markets in corporate bonds and those countries that do have such deep markets.

The current proposal to change IAS 19 would put companies in countries that do not have deep markets in high quality corporate bonds in a further disadvantage. When determining the interest income on plan assets, such companies would have to look to government bond rates, thus having to show higher pension expenses than their competitors in the Euro zone, the UK and the US. A higher portion of the return would under the IASB´s proposal be allocated to other comprehensive. We cannot see any real justification for such companies being forced to show higher pension obligations and higher pension expenses than peer companies within the Euro zone, when the pension benefits are the same. The measurement model is flawed in respect of the determination of the discount rate to be used for discounting of the pension obligations and this has to be amended quickly by the IASB.

Presentation in the income statement should not be prescribed by the standard

We consider that each entity should be permitted to determine how to present the pension expense based on its business model and how they look at their pension obligations. Some companies believe that it would be consistent with the presentation of a single net defined benefit liability in the statement of financial position to present a charge as a single net amount. Some companies treat their net pension obligation as an interest bearing liability and some other companies are treating its net pension obligation as a working capital item. All this impacts the way the companies want to present the pension expense. As long as the components of the pension expense are disclosed in the notes, we do not believe it is necessary to prescribe where to present them in the income statement. In addition, it is not warranted at this time to implement an interim measure in advance of the finalization of the financial statement presentation standard that will cover all presentation issues.

Recycling of actuarial gains and losses to the income statement

We are of the view that all items that are recognised through other comprehensive income should later be recycled to the income statement. This is required in US GAAP, and we believe the recycling method used in US GAAP can be used also for IFRS purposes. This would make the "net income" number more meaningful as it would enable the pension expense shown in net income to equal the cash outflows from pensions in the long run. We do not see any justification for a situation where the total comprehensive income measure should represent the cash outflows from pensions but where the net income would not.

Measuring the pension liability based on future salary increases

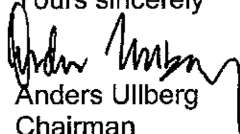
Another flaw in the measurement model relates to the issue of future salary increases. When pensions are linked to future salaries, we do not believe that the effect of future salary increases should be reflected in the measurement of the pension obligation. We believe that only pensions that the entity is presently committed to pay should be

reported as liabilities, not pensions that the entity might become committed to in the future which means that the pension liability shall be calculated using present salaries. We believe that the current approach is inconsistent with the treatment of expected increases in other elements of remuneration – such as salaries and bonuses – which are accounted for in the periods in which they occur.

If you have any questions concerning our comments please address our Executive member Carl-Eric Bohlin by e-mail to: carl-eric.bohlin@radetforfinansiellrapportering.se

Stockholm,7 September 2010

Yours sincerely



Anders Ullberg
Chairman