EFRAG Secretariat: Sapna Heeralall/
Robert Stojek

~~EFRAG's Draft Letter to the European Commission Regarding Endorsement of Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)~~

Olivier Guersent
Director General, Financial Stability, Financial Services and Capital Markets Union
European Commission
1049 Brussels

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Dear Mr Guersent

Endorsement of Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)

Based on the requirements of the Regulation (EC) No 1606/2002 of the European Parliament and of the Council on the application of international accounting standards, EFRAG is pleased to provide its opinion on *Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)* ('the Amendments'), which were issued by the IASB on 7 February 2018. The Amendments in their draft form were issued in Exposure Draft ED/2015/5 *Remeasurement on a Plan Amendment, Curtailment or Settlement/Availability of a Refund from a Defined Benefit Plan (Proposed amendments to IAS 19 and IFRIC 14)* on 18 June 2015. EFRAG provided its comment letter on that Exposure Draft on 6 November 2015.

The Amendments require entities~~ to determine current service cost and net interest ~~, when ~~an~~a plan amendment, curtailment or settlement occurs to a defined benefit pension plan, to use updated actuarial assumptions to determine the current service cost and net interest for the remainder of the annual period after such plan event.

The Amendments apply prospectively for annual periods beginning on or after 1 January 2019, with earlier application permitted. If entities apply the Amendments earlier, they shall disclose that fact. A description is included in Appendix 1 to this letter.

In order to provide our endorsement advice as you have requested, we have first assessed whether the Amendments would meet the technical criteria for endorsement, in other words whether the Amendments would provide relevant, reliable, comparable and understandable information required to support economic decisions and the assessment of stewardship, lead to prudent accounting and are not contrary to the true and fair view principle. We have then assessed whether the Amendments would be conducive to the European public good. We provide our conclusions below.

Do the Amendments meet the IAS Regulation technical endorsement criteria?

EFRAG has concluded that the Amendments meet the qualitative characteristics of relevance, reliability, comparability and understandability required to support economic decisions and the assessment of stewardship and raise no issues regarding prudent accounting. EFRAG has also assessed that the Amendments do not create any distortion in their interaction with other IFRS Standards and that all necessary disclosures are required. Therefore, EFRAG has concluded that the Amendments are not contrary to the true and fair view principle. EFRAG's reasoning is explained in Appendix 2 to this letter.

Are the Amendments conducive to the European public good?

EFRAG has assessed that the Amendments would improve financial reporting and would reach an acceptable cost-benefit trade-off. EFRAG has not identified that the Amendments could have any adverse effect on the European economy, including financial stability and economic growth. Accordingly, EFRAG assesses that endorsing the Amendments are conducive to the European public good. EFRAG's reasoning is explained in Appendix 3 to this letter.

Our advice to the European Commission

As explained above, we have concluded that the Amendments meet the qualitative characteristics of relevance, reliability, comparability and understandability required to support economic decisions and the assessment of stewardship, raise no issues regarding prudent accounting, and that they are not contrary to the true and fair view principle. We have also concluded that the Amendments are conducive to the European public good. Therefore, we recommend the Amendments for endorsement.

On behalf of EFRAG, I would be happy to discuss our advice with you, other officials of the European Commission or the Accounting Regulatory Committee as you may wish.

Yours sincerely,

Jean-Paul Gauzès

President of the EFRAG Board

Appendix 1: Understanding the changes brought about by the Amendments

Background to the Amendments

1 The IASB received a submission via the IFRS Interpretations Committee questioning the requirements for calculation of current service cost and net interest when a plan amendment, curtailment or settlement occurs, and an entity remeasures the net defined benefit liability or asset in accordance with paragraph 99 of IAS 19 *Employee Benefits*.

2 The IASB published *Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)* (henceforth referred to as 'the Amendments') on 7 February 2018.

The issue(s) and how it has been addressed

3 When a plan amendment, curtailment or settlement ~~takes place~~occurs for defined benefit plans, entities need to determine past service cost or settlement gain or loss. Paragraph 99 of IAS 19 ~~required~~requires that entities ~~to~~ first:

(a) remeasure the net defined benefit liability (asset~~) ('DBL'~~) using the current fair value of plan assets and current actuarial assumptions, including current market interest rates and other current market prices~~, and reflecting the benefits offered under the plan before the plan amendment, curtailment or settlement.~~; and

(b) ~~However, although~~reflect the benefits offered under the plan before the change in the terms.

~~3~~4 In relation to the calculation of the interest cost, paragraph 123 of IAS 19 ~~required~~requires entities to take account of changes in the net ~~DBL~~defined benefit liability (asset) as a result of contribution and benefit payments, but it did not require ~~entities~~ to take account of changes in the net ~~DBL~~defined benefit liability (asset) as a result of the remeasurement required by paragraph 99 of IAS 19. ~~As a result, the amounts recognised in profit or loss for the remainder of the reporting period after the amendment, settlement or curtailment might not fully reflect the effects of those events. Moreover, it resulted in diversity in accounting when a plan amendment, curtailment or settlement occurred.~~

~~4~~5 Consequently, the IASB decided to amend the relevant requirements of IAS 19.

~~5~~6 The Amendments now specify that an entity should use the updated assumptions from remeasurement of its net defined benefit liability (asset) in order to determine current service cost and net interest for the remainder of the reporting period after the change to the plan. The Amendments result in a different allocation of the total comprehensive income between service cost, interest and other comprehensive income.

When do the Amendments become effective?

~~6~~7 The Amendments apply prospectively to plan amendments, curtailments or settlements occurring on or after the beginning of the first annual reporting period that begins on or after 1 January 2019. Earlier application is permitted.

Appendix 2: EFRAG's technical assessment on the Amendments against the endorsement criteria

~~**Notes to Constituents:**~~

~~This appendix sets out the basis for the conclusions reached, and for the recommendation made, by EFRAG on the Amendments. In it, EFRAG assesses how the Amendments satisfy the technical criteria set out in the Regulation (EC) No 1606/2002 for the adoption of international accounting standards. It provides a detailed evaluation for the criteria of relevance, reliability, comparability and understandability, so that financial information is appropriate for economic decisions and the assessment of stewardship. It evaluates separately whether the Amendments lead to prudent accounting and finally considers whether the Amendments would not be contrary to the true and fair view principle.~~

~~In its comment letters to the IASB, EFRAG points out that such letters are submitted in EFRAG's capacity of contributing to the IASB's due process. They do not necessarily indicate the conclusions that would be reached by EFRAG in its capacity of advising the European Commission on endorsement of the definitive IFRS Standards in the European Union and European Economic Area.~~

~~In the latter capacity, EFRAG's role is to make a recommendation about endorsement based on its assessment of the final IFRS Standard or Interpretation against the technical criteria for European endorsement, as currently defined. These are explicit criteria which have been designed specifically for application in the endorsement process, and therefore the conclusions reached on endorsement may be different from those arrived at by EFRAG in developing its comments on proposed IFRS Standards or Interpretations. Another reason for a difference is that EFRAG's thinking may evolve.~~

Does the accounting that results from the application of the Amendments meet the technical criteria for endorsement in the European Union?

1 EFRAG has considered whether the Amendments meet the technical requirements of the European Parliament and of the Council on the application of international accounting standards, as set out in Regulation (EC) No 1606/2002 (The IAS Regulation), in other words that the Amendments:

(a) are not contrary to the principle set out in Article 4 (3) of Council Directive 2013/34/EU (The Accounting Directive); and

(b) meet the criteria of understandability, relevance, reliability, and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.

2 Article 4(3) of the Accounting Directive provides that:

The annual financial statements shall give a true and fair view of the undertaking's assets, liabilities, financial position and profit or loss. Where the application of this Directive would not be sufficient to give a true and fair view of the undertaking's assets, liabilities, financial position and profit or loss, such additional information as is necessary to comply with that requirement shall be given in the notes to the financial statements.

3 The IAS Regulation further clarifies that *'to adopt an international accounting standard for application in the Community, it is necessary firstly that it meets the basic requirement of the aforementioned Council Directives, that is to say that its application results in a true and fair view of the financial position and performance of an enterprise - this principle being considered in the light of the said Council*

Directives without implying a strict conformity with each and every provision of this Directive' (Recital 9 of the IAS Regulation).

4 EFRAG's assessment as to whether the Amendments would not be contrary to the true and fair view principle has been performed against the European legal background summarised above.

5 In its assessment, EFRAG has considered the Amendments from the perspectives of both usefulness for decision-making and assessing the stewardship of management. EFRAG has concluded that the information resulting from the application of the Amendments is appropriate both for making decisions and assessing the stewardship of management.

6 EFRAG's assessment on whether the Amendments are not contrary to the true and fair view principle set out in Article 4(3) of Council Directive 2013/34/EU is based on the assessment of whether they meet all other technical criteria and whether they lead to prudent accounting. EFRAG's assessment also includes assessing whether the Amendments do not interact negatively with other IFRS Standards and whether all necessary disclosures are required. Detailed assessments are included in this appendix in the following paragraphs:

(a) relevance: paragraphs 7 to 10;

(b) reliability: paragraphs 11 to 15;

(c) comparability: paragraphs 16 to 21;

(d) understandability: paragraphs 22 to 26;

(e) whether, overall, they lead to prudent accounting: paragraphs 27 to 29; and

(f) whether they would not be contrary to the true and fair view principle: paragraphs 30 to 34.

Relevance

7 Information is relevant when it influences the economic decisions of users by helping them evaluate past, present or future events or by confirming or correcting their past evaluations. Information is also relevant when it assists in evaluating the stewardship of management.

8 EFRAG considered whether the Amendments would result in the provision of relevant information – in other words, information that has predictive value, confirmatory value or both – or whether they would result in the omission of relevant information.

9 EFRAG assesses that it is inappropriate to ignore the updated assumptions, related to a pension plan when determining current service cost and net interest for the remainder of the reporting period after a plan amendment, curtailment, or settlement. Therefore, applying the Amendments and using updated assumptions will result in providing more useful information to users of financial statements.

10 Consequently, EFRAG assesses that the Amendments will result in relevant information for users of financial statements.

Reliability

11 EFRAG also considered the reliability of the information that will be provided by applying the Amendments. Information has the quality of reliability when it is free from material error and bias and can be depended upon by users to represent faithfully what it either purports to represent, or could reasonably be expected to represent, and is complete within the bounds of materiality and cost.

12 There are a number of aspects to the notion of reliability: freedom from material error and bias, faithful representation, and completeness.

13 As mentioned in paragraph 9 above, applying the Amendments will result in using the updated information related to a pension plan when determining current service cost and net interest for the remainder of the annual reporting period after a plan amendment, curtailment or settlement.

14 Moreover, the Amendments do not introduce new concepts, principles or accounting models.

15 Consequently, EFRAG assesses that the Amendments raise no concerns about freedom from material error and bias, faithful representation, and completeness.

Comparability

16 The notion of comparability requires that like items and events are accounted for in a consistent way through time and by different entities, and that unlike items and events should be accounted for differently.

17 EFRAG has considered whether the Amendments result in transactions that are:

(a) economically similar being accounted for differently; or

(b) transactions that are economically different being accounted for as if they are similar.

18 EFRAG acknowledges that there will be a difference in accounting for pension plans among entities with and without a plan event, resulting from the new requirement to use the updated actuarial assumptions to remeasure service cost and net interest on the net defined liability (asset) for the periods after the plan event. However, EFRAG considers that this does not reduce comparability because these are two economically different events.

19 Furthermore, an entity would have to remeasure pension cost for the remaining year for all participants of a plan, including those not affected by the plan event because the requirements apply on a plan-by-plan basis. However, EFRAG considers that this is consistent with the general principle of IAS 19 paragraph 57 which requires entities to account for each material plan separately.

20 EFRAG also acknowledges that remeasured pension expense, including current service cost and net interest on defined benefit liability (asset), after the plan event has taken place, would differ from the pension expense before that plan event. However, such plan events are one-off events that impact comparability in general. In all cases, the calculation of the pension expense would be affected by the plan event in the following period. Moreover, EFRAG considers updating actuarial assumptions and recognising updated pension expense for the periods after plan event, to provide useful information for users of financial statements.

~~18~~21 Furthermore, EFRAG observes that the Amendments address diversity in the accounting for the effects of plan amendments, settlements and curtailments. Therefore, in EFRAG's opinion, the Amendments will bring consistency in accounting for current service cost and net interest for the remainder of the annual reporting period after a plan amendment, curtailment or settlement.

~~19~~22 Regarding the transition requirements, EFRAG notes that the Amendments apply prospectively to plan amendments, curtailments, or settlements beginning from the first application taking place on or after 1 January 2019 (note that earlier application is permitted).

~~20~~23 Generally, EFRAG considers retrospective application of new requirements appropriate. However, in the case of the Amendments, EFRAG agrees that the benefits from retrospective application are unlikely to exceed the cost of doing so, because:

(a) retrospective application would not provide useful trend information to users of financial statements because plan amendments, curtailments and settlements are discrete one-off events;

(b) the amendments may change whether and when an entity remeasures the net defined benefit liability (asset) in accordance with paragraph 99 of IAS 19. Accordingly, if the Amendments were applied retrospectively, entities would have to revisit plan amendments, curtailments and settlements that occurred previously ~~and~~, reassess materiality, and eventually remeasure the net defined benefit liability (asset) as of the date of the ~~changes resulting~~plan events. This would result in changes to the allocation within comprehensive income; and

(c) retrospective application would affect neither total comprehensive income nor the amounts recognised in the statement of financial position for the past periods.

~~21~~24 Therefore, EFRAG's overall assessment is that the Amendments satisfy the comparability criterion.

Understandability

~~22~~25 The notion of understandability requires that the financial information provided should be readily understandable by users with a reasonable knowledge of business and economic activity and accounting, and the willingness to study the information with reasonable diligence.

~~23~~26 Although there are a number of aspects related to the notion of 'understandability', EFRAG believes that most of the aspects are covered by the discussion above about relevance, reliability and comparability.

~~24~~27 As a result, EFRAG believes that the main additional issue it needs to consider, in assessing whether the information resulting from the application of the Amendments is understandable, is whether that information will be unduly complex.

~~25~~28 EFRAG observes that the Amendments do not introduce new concepts or principles.

~~26~~29 Overall, in EFRAG's view, the Amendments do not introduce any new complexities that may impair understandability. Therefore, EFRAG's overall assessment is that the Amendments satisfy the understandability criterion in all material respects.

Prudence

~~27~~30 For the purpose of this endorsement advice, prudence is defined as caution in conditions of uncertainty. In some circumstances, prudence requires asymmetry in recognition such that assets or income are not overstated, and liabilities or expenses are not understated.

~~28~~31 EFRAG ~~assesses~~notes that the application of the Amendments would affect neither total comprehensive income nor the total amounts recognised in the statement of financial position.

~~29~~32 EFRAG has therefore concluded that they raise no issues in relation to prudence as defined above.

True and Fair View Principle

~~30~~33 A Standard will not ~~impede~~prevent information from meeting the true and fair view principle when, on a stand-alone basis and in conjunction with other IFRS Standards, it:

(a) does not lead to unavoidable distortions or significant omissions in the representation of that entity's assets, liabilities, financial position and profit or loss; and

(b) includes all disclosures that are necessary to provide a complete and reliable depiction of an entity's assets, liabilities, financial position and profit or loss.

~~31~~34 EFRAG has assessed that, on a stand-alone basis, the Amendments provide relevant, reliable, comparable and understandable information and do not affect prudence.

~~32~~35 EFRAG has also assessed that the Amendments do not create any negative interactions with other IFRS. Accordingly, EFRAG has assessed that the Amendments do not lead to unavoidable distortions or significant omissions and therefore they do not impede financial statements from providing a true and fair view.

~~33~~36 EFRAG has concluded that no new disclosures are necessary to provide.

~~34~~37 As a result, EFRAG concludes that the application of the Amendments would not lead to information that would be contrary to the true and fair view principle.

Conclusion

~~35~~38 Accordingly, for the reasons set out above, EFRAG's assessment is that the Amendments meet the technical requirements for EU endorsement as set out in the IAS Regulation.

Appendix 3: Assessing whether the Amendments are conducive to the European public good

Introduction

1 EFRAG considered whether it would be conducive to the European public good to endorse the Amendments. In addition to its assessment included in Appendix 2, EFRAG has considered a number of issues in order to identify any potential negative effects for the European economy on the application of the Amendments. In doing this, EFRAG considered:

(a) whether the Amendments improve financial reporting. This requires a comparison of the Amendments with the existing requirements and how they fit into IFRS Standards as a whole;

(b) the costs and benefits associated with the Amendments; and

(c) whether the Amendments could have an adverse effect to the European economy, including financial stability and economic growth.

2 These assessments allow EFRAG to draw a conclusion as to whether the Amendments are likely to be conducive to the European public good. If the assessment concludes there is a net benefit, the Amendments will be conducive to the objectives of the IAS Regulation.

EFRAG's evaluation of whether the Amendments are likely to improve the quality of financial reporting

3 EFRAG notes that the Amendments require entities to ~~determine pension expenses when changes to a defined benefit pension plan occur. As a result, this increases consistent application of current accounting~~use updated actuarial assumptions to determine the current service cost and net interest for the remainder of the annual period after a plan event. As a result, entities will provide useful information based on actuarial assumptions updated at the date of the plan event.

4 EFRAG has therefore concluded that the Amendments are likely to improve the quality of financial reporting.

EFRAG's analysis of the costs and benefits of the Amendments

5 EFRAG first considered the extent of the work. For some Standards or Interpretations, it might be necessary to carry out some extensive work, in order to understand fully the cost and benefit implications of the Standard or Interpretation being assessed. However, in the case of the Amendments, EFRAG's view is that the cost and benefit implications can be assessed by carrying out a more modest amount of work.

Cost for preparers

6 EFRAG's assessment is that the Amendments would create a one-off cost for preparers in reading, understanding the Amendments and explaining to users of financial statements, but that cost is likely to be insignificant.

7 The Amendments would create ongoing costs for preparers relating to updating actuarial assumptions and valuations for current service cost and net interest after a change to the plan. Ongoing costs would depend on the frequency of ~~a change~~changes in ~~the~~a plan and ~~also~~ whether there would be a material effect from applying the requirements. However, such plan events are not expected to be frequent. Moreover, these costs are not likely to be significant because the existing IAS 19 requirements already require entities to remeasure the net defined benefit liability (asset) as of the date of a plan amendment, settlement or curtailment based on the updated actuarial assumptions for the purpose of determining any past service

cost~~.~~ and, therefore, entities are expected to have assessed the financial impact of the plan event including effect on current service cost and net interest on the net defined benefit liability (asset).

8 Overall based on the above, EFRAG's assessment is that the Amendments are likely to result in insignificant costs for preparers related to implementation of the Amendments and / or ongoing costs of complying with the Amendments.

Costs for users

9 EFRAG's assessment is that the Amendments would create a one-off cost for users in reading, understanding the Amendments and ongoing costs relating to updating their analyses specifically relating to the net benefit liability or asset, current service cost and net interest.

10 Overall, EFRAG's assessment is that the Amendments are likely to result in insignificant costs for users.

Benefits for users and preparers

11 EFRAG considers that the Amendments would reduce diversity. Therefore, in EFRAG's view, users will benefit from a more consistent application of the requirements thus improving the resulting financial information. In addition, the Amendments will provide a more useful basis for users' analyses as updated assumptions will be used to determine current service cost and net interest for the remainder of the reporting period.

12 Further, preparers are expected to benefit from reducing the effort required to determine how the requirements of IAS 19 should be interpreted.

13 Overall, EFRAG's initial assessment is that users and preparers are likely to benefit from the Amendments.

Conclusion on the costs and benefits of the Amendments

14 EFRAG's overall assessment is that the overall benefits resulting from clarity of the IAS 19 requirements arising from the Amendments are likely to outweigh any costs required to implement and continue to comply with the requirements of the Amendments.

Conclusion

15 EFRAG believes that the Amendments will generally bring improved financial reporting when compared to current guidance. As such, their endorsement is conducive to the European public good in that improved financial reporting improves transparency and assists in the assessment of management stewardship.

16 EFRAG has not identified the Amendments could have any adverse effect to the European economy, including financial stability and economic growth.

17 Furthermore, EFRAG has not identified any other factors that would mean endorsement is not conducive to the public good.

18 Having considered all relevant aspects, including the trade-off between the costs and benefits of implementing the Amendments, EFRAG assesses that endorsing the Amendments is conducive to the European public good.