

Research on Pensions: Hybrid Plans

Presented on behalf of a group of national standard-setters in Canada, Germany, Japan, the U.K. and the U.S.

Linda Mezon, FCPA, FCA, CPA (MI)
Chair, Accounting Standards Board

The views expressed in this presentation are those of the presenter, not necessarily those of the Accounting Standards Board.

Why the research and why now?

- Hybrid pension plans becoming more prevalent in multiple jurisdictions
- Issues arise in accounting for these plans under both IFRS[®] Standards and several local GAAPs
- Financial statement users need relevant information about plan sponsor's obligation
- Further accounting guidance may be needed to better reflect economic characteristics of hybrid plans
 - Actuarial guidance meant to fill in gaps could result in diversity

What we mean by "hybrid pension plans"

- Can mean different things to different people
- For purposes of our research
 - New types of pension plans that are neither defined contribution plans (DC plans) nor defined benefit plans (DB plans)
 - Contain elements of both traditional DC plans and traditional DB plans
 - Evolved in order to reduce plan sponsors' risk

Our research focus

- Focused on how to account for hybrid plans by determining similarities and differences
 - Considered a range of plans
 - From traditional DB to traditional DC and 4 example plans in between
 - Two shared-risk plans
 - Cash balance plan
 - Security-linked plan

Some key features of our example plans

Shared-risk Plan #1	Shared-risk Plan #2	Cash Balance Plan	Security-linked Plan
<p>Targeted benefits established pursuant to a formula, but not guaranteed by plan sponsor</p>	<p>Based on traditional DB plan, with modifications to benefit formula such as adjustments based on funded status. Targeted benefits not guaranteed by plan sponsor.</p>	<p>Benefits established pursuant to a formula that is a function of salary-based principal credits and a crediting rate based on those principal credits</p>	<p>Plan sponsor guarantees a minimum return (of at least 0% but usually higher) on the invested contributions</p>
<p>Plan sponsor and plan members participate equally in funding the plan with benefits managed through a funding policy</p>	<p>Risk-sharing contributions to be made by plan sponsor and agreed to by both parties at plan inception</p>	<p>Plan sponsor makes contributions that can accumulate to the actuarial PV of benefit due at time of distribution to each participant pursuant to plan's terms</p>	<p>Plan sponsor makes contributions to plan members' accounts with these contributions invested in a specified securities portfolio generating returns</p>

Extent of our research

- Consulted audit and benefit consulting firms in each jurisdiction about example plans
- Gathered views and observations:
 - **Domestic pension experience** such as extent to which the four example plans, or similar plans, exist in each jurisdiction
 - **IFRS[®] Standards and Local GAAP experience**
 - **Areas for improvement**

Where our example plans are found

Example Plan Existence

Shared-risk plan #1 found only in Canada; rare in private sector in Canada, but emerging; awaiting enabling regulation

Other three example plans exist in >1 of our jurisdictions

Security-linked plan common only in Germany and on the rise

Cash balance plan common in 3 of our jurisdictions

Similar Plan Existence

Germany has a growing interest in establishing plans like shared-risk plan #1

Canada, the U.K. and the U.S. have similar plans to the security-linked plan

Canada and the U.S. have similar plans to shared-risk plan #2

Shared-risk plans and security-linked plan all contain a risk-sharing element

Accounting challenges – Classification

- Found diversity in expected classification across our jurisdictions and within specific jurisdictions
 - Security-linked plan – DC account with DB guarantee, DB only; DC or DB depending on whether concept in IFRIC D9 applies
 - Shared-risk plan #2 – DC or DB
- Consistent classification for shared-risk plan and cash balance plan as DB plans across our jurisdictions

Accounting challenges – Measurement

- How to measure the obligation? E.g.,
 - Shared-risk plan #1
 - How to determine the portion of risks and costs retained by the plan sponsor?
 - What assumptions to use? e.g., which benefits are guaranteed and to what extent?
 - Shared-risk plan #2 — how to measure benefits that vary according to funded status?
 - Security-linked plan — how to determine the present value of the obligation, i.e., what discount rate?

Ideas to explore

- Identified possible avenues to explore to resolve the issues
- No clear cut winner
- Reviewed IASB's work done on post-employment benefits as well as feedback from IFASS participants
- IFASS participants agreed that some ideas show promise

Suggest developing principles-based guidance with flexibility to better reflect economics of hybrid plans

What we propose

- Propose IASB consider research performed to date
 - Add it as another dimension to the feasibility study on pensions in its research pipeline, or
 - Take on a project to address hybrid pension plans
- Stand ready to assist the IASB

Furthering our research

- Make our research more globally inclusive by hearing from other jurisdictions
 - Asked IFASS members to complete a questionnaire
- Hear from other stakeholders within our jurisdictions
 - Financial statement users
 - Academics
- Continue to monitor related activities

Questions for ASAF members

Q1 – Are there recent developments in your jurisdiction that reflect the ongoing evolution of hybrid pension plans? (¶s 17-18)

Q2 – Do you think our research on hybrid pension plans has merit? If not, why not? (¶s 17- 63)

Q3 – Do you agree with our proposal? (¶s 68-70)

Q4 – Do you agree with the next steps? (¶ 71) Do you have additional activities to suggest?



For more information, visit www.frascanada.ca

Contacts

Nancy Estey, CPA, CA

Principal, Accounting Standards Board

Phone: +1 (416) 204-3271

Email: nestey@acsbcanada.ca

Karen Jones, CPA, CA

Senior Principal, Accounting Standards Board

Phone: +1 (416) 204-3463

Email: kjones@acsbcanada.ca