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CC:

IASB

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Discussion Paper Accounting for pension plans with an asset-return promise

Representing preparers' point of view, the Swedish Enterprise Accounting Group (SEAG) welcomes the opportunity to comment on the Discussion Paper (DP). We have added comments to the specific questions posed in the DP in the enclosed appendix.
Kind regards,

CONFEDERATION OF SWEDISH ENTERPRISE

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The Swedish Enterprise Accounting Group (SEAG) represents more than 40 international industrial and commercial groups, most of them listed. The largest SEAG companies are active through sales or production in more than 100 countries.

Appendix – Comments on the specific questions raised by EFRAG

Q1 SCOPE
The Discussion Paper addresses only those pension plans that have an asset-return based promise and hold the assets upon which the benefits are dependent. Do you think that the approaches could also be applied to those plans with an asset-return promise, where the plan does not hold the reference assets?

No, the plans are different in nature and risk. If the approaches would be applied to pension plans not holding the reference assets, this would require unfunded pension plans to change into funded plans. This would be a big effort with basically no return. This would also mean that shorter medical plans would be included.

Q2 ASSESSMENTS OF APPROACHES – ASPECTS TO CONSIDER
Do you agree with the aspects of qualitative characteristics considered in the assessment of the various approaches in Chapter 5? If not, which aspects do you think should/should not have been considered? Do you agree with the assessments of the various approaches made in Chapter 5?

Fulfilment value and fair value more or less lean towards fair valuation logic. To be able to approximate fair value such a long time in the future (the duration of the pension obligation can be very long, approximately 25 years) would require even more assessments, estimates and judgments than today and would add complexity. The measurement approach would be difficult to understand and it would be a challenge to explain the volatility of the pension obligation to the market. We fear that this will lead to an increased need to engage external consultants (actuaries and valuation experts) and thus be costly.

Regarding the fulfilment approach, the reporting entity has limited knowledge of the obligation in 25 years.

Q3 ASSESSMENT OF APPROACHES – ASSESSMENT OF COMPLEXITY
The assessment in Chapter 5 of the costs related to the various approaches presented in this Discussion Paper, only considers implementation costs. Do you think that the complexity related to preparing financial information in accordance with the approaches would differ significantly? If yes, which approaches would be the most complex and least complex to apply?

The fair value approach would be the most complex to apply since it is based on valuation techniques and models which would most probably be applied differently by different preparers.

For the fulfilment approach, the likelihood of being correct in the calculation is very low and there is a risk of divergent interpretations among preparers that might end up in application of fair value logic. This will impair comparability. Estimating outflow is particularly difficult

The least complex would be the capped asset approach.

One central aspect to take into consideration is the actuarial competence needed to apply these approaches and related cost, in comparison with the current situation. Another issue to consider is how the current OCI effect would be treated as part of the implementation.

Q4 CHOICE OF APPROACH
Which of the three alternative approaches, presented in this Discussion Paper, do you support? How should it be further developed?

During the last ten years, there has been several changes in IAS 19 such as the abandonment of the corridor method, introduction of OCI and the asset ceiling etc. While the aim of these amendments has been to achieve better accounting, the real issue with accounting for pension plans has not been addressed. In our opinion, the real issue is associated with the discount rate. According to IAS 19 "the discount rate shall be determined by reference to market yields at the end of the reporting period on high quality corporate bonds. For currencies for which there is no deep market in such high-quality corporate bonds, the market yields on government bonds denominated in that currency shall be used". The definition of what a deep market is shall be assessed on currency level and not a country/market level. This leads to difficulties for middle market countries and different assessments regarding what discount rate to use. The use of different rates causes loss of comparability of entities' pension obligations. In Sweden, the lack of guidance is causing significant uncertainty in relation to the size of the pension liabilities. In 2008, a number of large Swedish companies proposed a solution to this this issue, which resulted in an ED from the IASB with proposed amendments to IAS 19. The proposed amendments were, however, never adopted by the IASB. We believe that the proposal in the ED is still relevant and should be considered in a fundamental review of IAS 19. Ten years have passed and we believe that it is time for the IASB to address this matter. As most countries are "mid-size" guidance is definitely and urgently needed.

On these grounds, we generally believe that the proposals in the DP will not solve the real issue with accounting for pension plans. Thus, none of the approaches should be further developed.

Q5 PRESENTATION OF REMEASUREMENTS UNDER THE FAIR VALUE BASED APPROACH AND THE FULFILMENT VALUE APPROACH
This Discussion Paper assumes that remeasurements under the Fair Value Based approach and the Fulfilment Value approach are presented in profit or loss. Do you agree with this approach? If not, how would you present components of defined benefit costs other than service costs?

There are both pro's and con's with abandoning remeasurements in OCI and instead presenting them in profit and loss. The pension obligation has a duration of approximately 25 years, which is a long period. In addition, the obligation as such is difficult to measure. If remeasurements are included in profit and loss, this will affect the business performance as of today which *might not be fair since it is pure remeasurements based on estimates about the future, 25 years as from today. On the other hand, if it will be included in the profit and loss, it will provide a full picture of the costs as of today which are linked to the employees' performance and related revenues. However, in general, it will be very aggressive to include remeasurements in profit and loss. Therefore we believe that remeasurements shall be presented in OCI.*

Q6 RISK ADJUSTMENT FOR FULFILMENT VALUE APPROACH

As stated in paragraphs 4.56 to 4.57, this Discussion Paper proposes that a risk adjustment for non-financial risks is made when discounting the pension obligation under the Fulfilment Value approach. Do you agree? Which risks do you consider such an adjustment should cover?

We see a risk with introducing a non-financial risk adjustment since this is another area which includes estimates and judgments that affect comparability negatively. We also see a risk for introducing aspects similar to Solvency II in non-insurance companies.

If the methodology for accounting for defined benefit plans becomes even more complex than today, there is a risk that companies will close defined benefit plans and change the pension strategy to defined contribution plans. We see this trend already today. We would therefore prefer more guidance and a stronger methodology for retrieving the discount rate to be used.

Q7 DISCLOSURE

Do you think that additional disclosure requirements about pension plans, included in scope of this Discussion Paper, should be added to the requirements of IAS 19?

The disclosure requirements in IAS 19 are extensive and provide useful information, therefore we see no need of additional disclosure requirements.

Q8 ALTERNATIVE APPROACHES

Do you think there are other approaches to account for the pension plans within the scope of this Discussion Paper that should have been considered? If so, which approaches?

The approaches presented in this discussion paper will introduce more difficulties and reduce comparability when considering the extensive estimates and judgments that the approaches require. A stable model for calculating the pension obligation which allows for comparability would be more beneficial. Also, as mentioned under Q4, the real issue is the lack of guidance and methodology for the discount rate and the definition of what constitutes a "deep market".

Another approach, or rather aspect to consider, is that the present guidance in IAS 19 regarding discount rates was drafted when interest rates were significantly higher. Market rates are now low or zero e.g. in Sweden. The Swedish Riksbanken expect the rates to be continuously low for a long period of time. If the impact of discounting is very limited, then a more simplistic approach should be considered.