The Actuarial Profession
making financial sense of the future

Pensions, benefits and social security colloquium 2011

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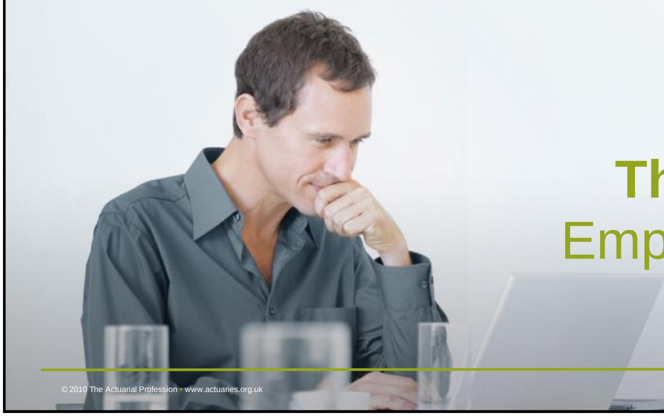

The new IAS 19
Employee Benefits

25-27 September 2011

The road to IAS 19 2011

2006	- Added to agenda
March 2008	- Discussion paper published
April 2010	- Exposure draft published
June 2011	- Revised IAS 19 published
January 2013	- Effective date

- Retrospective application
- Early adoption permitted
- Transition relief for sensitivity analysis

Why did the IASB revise IAS 19?

- Option to defer the recognition of gains and losses, known as the ‘corridor method’ allowing companies to ‘smooth’ results.
- Recognised amounts presented in different ways.
  - eg gains and losses can appear in different positions
- Disclosure requirements that lack information about the risks related to defined benefit plans.

How will the amendments help?

- Elimination of the option to defer recognition; immediate recognition will provide a clearer picture of the entity’s performance
- New approach to present gains and losses through clear categories without options will improve comparability and will be more understandible
- Enhanced disclosures including information about the risks arising from defined benefit plans

Main changes

- Immediate recognition of changes in net
- Interest on net balance sheet asset/liability to replace interest on liability, expected return on assets
- Service cost and net interest in P&L; remeasurements in OCI
- Termination benefits
- Disclosures
- Other amendments

Disaggregation and Presentation

- Profit & Loss (P&L)
  - Current service cost
  - Past service cost
    - Curtailments and plan amendments
  - Settlements
  - Net interest
- Other Comprehensive Income (OCI)
  - Actuarial gains and losses
  - Asset returns (except bit in net interest)
  - Effect of the asset ceiling (except bit in net interest)

Disclosures

- Focused on disclosure objectives
  - Explain characteristics of the entity's defined benefit plans and risks arising from them
  - Identify and explain amounts in financial statements resulting from defined benefit plans
  - Describe how defined benefit plans affects the amount, timing and variability of future cash flows.
- New disclosures
  - Risk exposures and asset-liability management
  - Sensitivity on defined benefit obilgation
  - Duration of liability

Future review of IAS 19

- Agenda consultation
- Possible scope of future project
  - Contribution based promises (were within scope of 2008 DP)
  - Measurement
- Other projects
  - Insurance
  - IAS 37

Overview: Changes to IAS 19 * - what we read

Comprehensive Income (P&L + OCI)	Immediate recognition of all changes in funded position
Financing Cost	Interest cost and expected return on plan assets replaced with net interest on net DB liability/asset
Clarification of Measurement Issues	Explicit assumptions regarding taxes payable by plan on contributions and benefit payments; plans with risk-sharing features
Financial Reporting & Disclosure	Disaggregate cost into employment, financing, and remeasurement effects Disclosures to provide more insight on plan risks

* No change to accounting for other long-term benefits.

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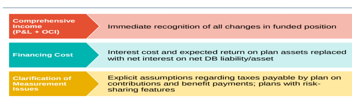
Overview: Changes to IAS 19 – what was meant



Financial Reporting & Disclosure	Disclosures to provide more insight on plan characteristics, risks

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What a preparer should prepare for

- **Understanding**
  - What the Statement does not state
  - What the Statement does state
  - What alternatives are available
- **Deciding**
  - What risk managment (governance) strategy to follow
  - What disclosure strategy to follow
- **Implementing**
- **Monitoring**

What the Statement does not state (and intentionally so)

- **. . . how contribution based plans are to be treated**
- **. . . that current measurement principles are here to stay**
  - what is a liability
  - what is the appropriate discount rate
  - . . .
- **. . . that current recognition principles are here to stay**
  - Is non-recycling always the reasonable approach
  - Do we really understand attribution (risk sharing / employee contributions)
  - . . .

Message: We are in transition

What the Statement does state (apart from the already well-known)

- **... that current disclosures are inadequate and perhaps obfuscating**
  - (The current disclosure rules) "… do not enable users …to understand the financial effect of liabilities and assets arising from defined benefit plans on the financial statements as a whole" and by virtue of "the volume of disclosures … risked reducing understandability and usefulness by obscuring important information)
- **... that disclosures áre to meet the following objectives**
  - Explain characteristics of and risks associated with plans
  - Identify and explain amounts in financial statements
  - Describe how plans affect the entity's future cash flows (amount / timing / uncertainty)

The preparer is charged with forming his own view on what framework he wishes to measure his plans against. IAS 19 does not prescribe this framework!

The new principles for disclosures (paradigm shift)

- **IAS 19.135 states the objectives preparers are to meet**
  - To meet those objectives, the preparer is encouraged to prepare for himself a (holistic) assessment of the opportunities and risks inherent in his DB plans
  - This will typically be spelled out in the enterprise's risk management (or governance) strategy will set out its (own) opinion of these risks
  - Part of this strategy will be a framework to set the basis for assessing risk.

    The content of this risk management strategy and the framework are not in any way prescribed in IAS 19. The onus is on the preparer!
  - Every enterprise is thus called upon to form an opinion on what it considers to be the most reasonable measurement framework for its obligations and plan assets, i.e. what guiding framework it considers most suitable in assessing progress in achieving its goal of fulfilling its constructive obligations
  - The Statement further expects the preparer to explain the result

The Framework 1/2

A view is to be reached - from the preparer's perspective – what the most appropriate benchmark for obligations and plan assets is. Some examples:

A. Obligations

- Assumptions to be used in estimating future payment obligations (e.g. best estimate)
- Actuarial valuation method (e.g. PuC)
- Determination of the Discount Rate (e.g.):
  - Risk free (or realistic minimum risk) rate
  - IAS 19 principles (high quality or government bond yields)
  - Expected return on the basis of investment strategy
  - Rate required by one or more supervisory authorities
  - Buyout basis

The Framework 2/2

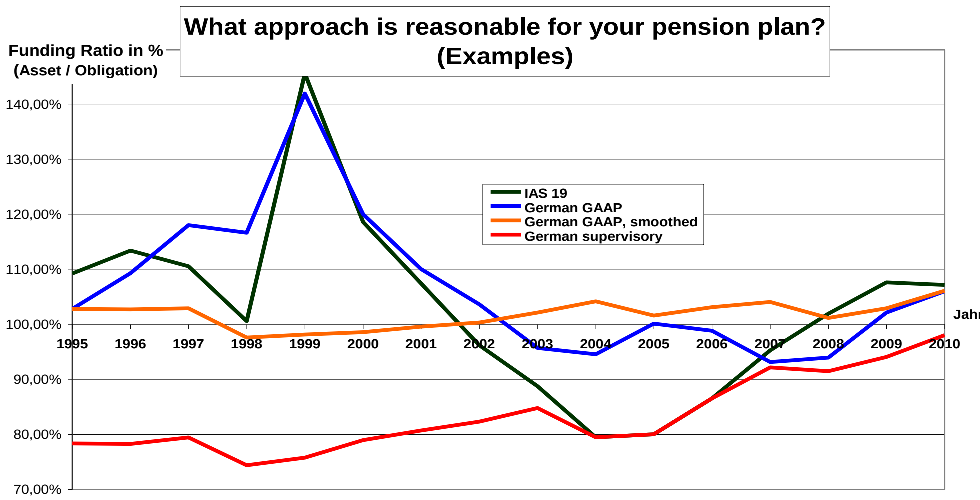
B. Plan Assets

- Determination of appropriate value (e.g.):
  - Market value as currently prescribed by IAS 19
  - Discounted Cashflow (using a rate consistent with the discount rate chosen)
  - Modified market value (using a method consistent with the discount rate chosen)
  - Book value

C. Assessment of "solvency"

- Comparison of expected cashflows
  – these should be fairly constant from year to year
- Funding Ratio determined under the framework
  – compared with the Funding Ratio as determined under IAS 19

What view is “reality“ from the preparer‘s point of view? - what “colour“ does my pension plan have -



Actuarial “Roadmap“ up to full first time Implementation

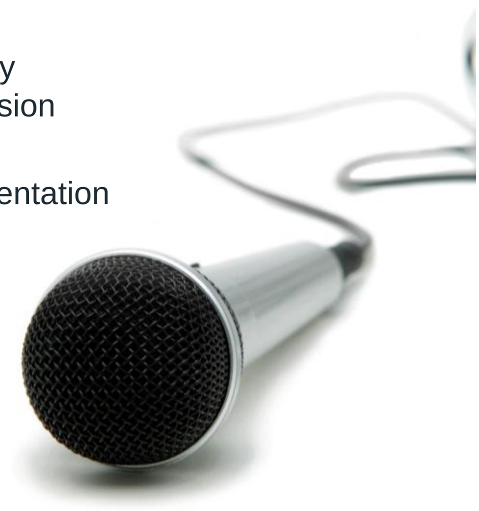
Assume: Financial year = calendar year, First time implementation for FY 2013

	Old IAS 19	New IAS 19
31.12.2011	• Disclosure 2011 • Expense 2012 **Support now**	• **Possibly new determination of DBO as at 31.12.2011 and Service Cost 2012 due to „clarifications“** • **Determination of the amount to be booked against equity / deferred taxes** • **Expense 2012** ➔ **Required for the Financial Statements 2013 for comparative purposes**
31.12.2012	• Disclosure 2012 (last time)	• Possibly new determination of DBO as at 31.12.2012 and Service Cost 2013 due to „clarifications“ • Disclosure 2012, but without sensitivities • Expense 2013 ➔ Required for the Financial Statements 2013 for comparative purposes
31.12.2013		• Full Disclosure 2013, incl. sensitivities only for the year end 2013 • Expense 2014

Questions or comments?

Expressions of individual views by members of The Actuarial Profession and its staff are encouraged.

The views expressed in this presentation are those of the presenters.



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