Deloitte.

Deloitte Touche Tohmatsu
2 New Street Square
London EC4A 3BZ
United Kingdom

Tel: +44 (0)20 7936 3000
Fax: +44 (0)20 7583 8517
www.deloitte.com

Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
London
United Kingdom
EC4M 6XH

Email: commentletters@iasb.org

27 July 2009

Dear Sir David,

Exposure Draft ED/2009/4 Prepayments of a Minimum Funding Requirement, Proposed amendments to IFRIC 14

Deloitte Touche Tohmatsu is pleased to respond to the International Accounting Standards Board's (the IASB's) *Exposure Draft ED/2009/4 Prepayments of a Minimum Funding Requirement, Proposed amendments to IFRIC 14* (referred to as the "exposure draft" or "ED").

We recognise that the application of the requirements of IFRIC 14 to prepayments of a minimum funding requirement ("MFR") results in some cases in an accounting treatment that does not reflect the substance of the transaction. We agree that this unintended result needs to be addressed and we believe that the solution proposed would address appropriately the issue that was brought to the attention of the Board (the so-called "Swiss plans" issue). However, we are concerned that the IASB is adopting a piecemeal approach to addressing this problem and that the amendments proposed will result in additional ambiguities in the application of IFRIC 14 and inconsistent accounting treatments. As a result, we do not support the proposed modifications to IFRIC 14. We offer alternatives for the Board's consideration in order to address the issues identified.

Concerns with the ED's proposals

Our concerns centre around the following two issues:

1. Definition of the term "prepayment"

   The ED proposes to apply a specific treatment to assets resulting from a prepayment of MFR, which, based on the explanation provided in proposed IFRIC14.20(a), appears to be an identifiable advanced payment made in respect of established MFR for specific years (i.e. the prepayments contemplated in the "Swiss plans"). However, the term "prepayment" is not defined in the context of IAS 19 or IFRIC 14 and it is unclear whether the proposals are aimed at addressing only prepayments as described above or prepayments defined more broadly. The ED does not explain the principle that justifies

treating differently certain amounts that result in lower MFR for future periods. For example, depending on the jurisdiction, the existence of a defined benefit asset (as measured under IAS 19) may affect the determination of MFR for future periods. It would be useful to understand whether or not proposed IFRIC 14.20(a) would permit recognition of an asset in such a circumstance. If the Board believes that proposed IFRIC 14.20(a) would not apply to such assets, it would be useful for the amendments to explain why it is relevant to make a distinction between a prepayment of MFR and the existence of an asset that affects the determination of MFR with respect to future periods.

Further, in some circumstances, prepayments of MFR may be made directly in the benefit fund (rather than in a separate account that is transferred to the fund when the contributions are actually due) and may be subject to fluctuations based on returns on plan assets. In such circumstances, it may be difficult, in subsequent periods, to identify separately the asset that results from a prepayment from other plan assets. Again, it would be useful to understand how the amount of prepayment contemplated in proposed IFRIC 14.20(a) is expected to be established where the contribution prepayments are not segregated from other assets.

2. Inconsistent treatment of assets resulting from prepayments vs. other plan assets

We believe that the proposed amendments further highlight the difficulties introduced by IFRIC 14 by requiring that MFR are considered in the determination of defined benefit assets and obligations.

IFRIC 14 has introduced funding considerations whereas IAS 19 purposely disregarded them. The broader issue is the extent to which funding requirements should be taken into consideration in determining the assets and liabilities that shall be recognised and whether any discrepancy should exist depending on whether it is an asset or a liability that shall be recognised. As explained in IAS 19.BC22, the Board has determined that IAS 19 should be based on the Projected Unit Credit Method rather than on a method that reflects funding costs. However, IFRIC 14 requires that MFR should be considered in determining the existence of an asset or of a liability. The complexities introduced are two-fold. Firstly, IFRIC 14 requires the determination of whether MFR relates to past or future services. This is particularly difficult to apply because MFR are often established on a basis that does not reflect the IAS 19 methodology. Secondly, by limiting the asset that may be recognised to the present value of the excess of future service cost over MFR for future services calculated over the expected life of the plan, in effect, IFRIC 14 reduces the asset that would otherwise arise from a plan surplus by a future obligation (the MFR for future services) that does not yet exist under IAS 19. This inconsistency is increased by the proposals in the ED: unlike for other plan assets, the ED would result in recognition of an asset if MFR for specific years are reduced by the prepayment as opposed to looking at the MFR over the expected life of the plan.

To understand better what appears to be a conceptual inconsistency between the treatment of an "asset" resulting in a prepayment of MFR and that of other plan assets, it may be useful to change the fact pattern presented in Example 3 of the implementation guidance to IFRIC 14. The situation addressed in the example is that of an entity that is required to make contribution in excess of future service cost and concerns the determination of the asset that would be recognised under proposed IFRIC 14.20(b). Suppose that if, instead of being in a situation where the early years show MFR in excess of service cost, the situation in IFRIC 14.IE 17 was the following:

Year	IAS 19 service cost (CU)	Minimum contributions required to cover future accrual (CU)	Amount available as contribution reduction (CU)
1	13	10	3
2	13	12	1
3	13	15	-2
4+	13	15	-2

Ignoring the effect of discounting, the ED would suggest that because the entity is not in a situation of prepayment, it would look at proposed IFRIC 14.20(b) and conclude that the economic benefits available as a reduction of future contribution is nil (since sum of the present value of the amounts shown in the rightmost column is not more than zero). While a surplus existing at the onset of the scheme would be utilised in years 1 and 2, IFRIC 14 reduces this asset by the obligation that arises in year 3 and later, i.e. it reduces an existing asset by a liability that does not yet exist under IAS 19.

In reality, the MFR for year 1 and 2 may have been established under the applicable plan regulations at lower levels because of the existence of a plan surplus. For instance, if in the absence of a plan surplus, the MFR had been CU 15 for all years, would the entity recognise an asset of CU 8 (representing the difference between the MFR of CU 15 that would have been required in year 1 and 2 in the absence of a plan surplus and the amount actually required of CU 10 and CU 12, respectively, for those years)? In practice, it may be difficult to establish to what extent MFR with respect to future services are reduced by the existence of a plan surplus. Accordingly, it is important that a rationale be provided for what appears to be inconsistent consideration of future funding costs.

Alternative proposals

In order to address the issues identified above, we offer two alternatives for the IASB's consideration:

1. One alternative treatment that would reduce the need to distinguish the origin of plan assets may include a more fundamental amendment to IFRIC 14 to eliminate the consideration of MFR in the assessment of whether an asset should be recognised. Under this approach, IFRIC 14 would be more consistent with IAS 19 that is based on a methodology that does not reflect funding costs. The interaction of MFR on plan assets and liabilities could then be reconsidered as part of the overall review of IAS 19. In the above example, the maximum asset that the entity would be entitled to recognise as the economic benefit available as a reduction in future contribution would be the lower of the plan surplus, if any, and the sum of the present value of the future service costs of CU 13 for each of the remaining years of the life of the plan.

2. A second alternative treatment would be to retain the concept that the recovery of a plan asset is established based on the excess of service costs over MFR for future services. However, in order to avoid reducing today an asset for an obligation that arises later, an entity would establish the maximum asset that it will be able to recover on a cumulative basis year by year. For each year, the entity would determine the difference between the estimated service costs and the MFR for that year. The present value of that difference (positive or negative) for each year would be summed up by adding the years consecutively, year by year, starting in the current period. The maximum asset that would be recognised (provided a pension surplus of at least that amount is available) is determined as the maximum amount that can be determined on a cumulative basis for any future period starting from the current period. This maximum can never be less than zero.

In the example above, the entity would recognise an asset of CU 4 at the outset (to the extent that a plan surplus of at least this amount exists) which is the asset throughout years 1 and 2.

For greater clarity, we have provided examples of the application of these two treatments to various scenarios in appendix 1 to this letter.

If the Board decided to follow one of those two alternatives, there would be no need to distinguish a prepayment from other plan assets. However, should the Board decide to pursue the proposals in the ED and retain the concept of prepayment, it will need to define this term. We urge the Board to establish a definition of prepayment of MFR that is based on a stated principle that ensures that similar accounting treatment is applied to similar economic situations.

Additional comments

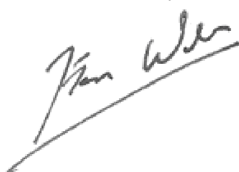
We note that certain changes were made to IFRIC 14, but that these changes are not explained in the basis for conclusions. An explanation would help in evaluating what, if anything, are the consequences of those changes on the previous application of IFRIC 14. In particular, we note that:

1. IFRIC 14.22 is being deleted and replaced by proposed IFRIC 14.20(b)(ii) with different wording. In particular, IFRIC 14.22 currently makes reference to "any given year" thereby indicating that the calculation must be done over the entire expected life of the plan, leading to the issue mentioned above that future obligations reduce assets that currently exist. Proposed IFRIC 14.20(b)(ii) does not include the reference to "any given year". By omitting these words, it is unclear whether the Board intended to change the computation method to a calculation akin to the one we described above as alternative 2. It would be useful if the Board clarified the intention behind the change in wording.
2. Throughout the text, references to "accrual of benefits" are being changed to "future service". It would be helpful if the Board explained the reason for the change and whether the change in terminology creates any change in application.

Finally, we note that IFRIC 14.IE16 starts with "in accordance with paragraph 20 of IFRIC 14...". As an editorial change, we suggest that the reference should be to paragraph 20(b)(ii) of IFRIC 14.

If you have any questions concerning our comments, please contact Ken Wild in London at +44 (0)20 7007 0907.

Yours sincerely,



Ken Wild
Global IFRS Leader

Appendix 1: Illustration of the alternative treatments proposed

The purpose of the following examples is to demonstrate the application of the alternative treatments proposed in our letter to various scenarios.

The alternative treatments proposed in our letter are as follows:

1. Alternative 1: eliminate the consideration of MFR in the assessment of whether an asset should be recognised.

2. Alternative 2: retain the concept that the recovery of a plan asset is established based on the excess of service costs over MFR for future services. However, in order to avoid reducing today an asset for an obligation that arises later, an entity would establish the maximum asset that it will be able to recover on a cumulative basis year by year. For each year, the entity would determine the difference between the estimated service costs and the MFR for that year. The present value of that difference (positive or negative) for each year would be summed up by adding the years consecutively, year by year, starting in the current period. The maximum asset that would be recognised (provided a pension surplus of at least that amount is available) is determined as the maximum amount that can be determined on a cumulative basis for any future period starting from the current period. This maximum can never be less than zero.

For simplicity sake, the examples assume that the plan has a remaining life of 6 years and ignore the effect of the time value of money. At the beginning of year 20X1, the IAS 19 calculation (before the application of the asset ceiling requirements) shows a plan surplus of CU 35. As noted in our letter, whether the plan surplus is the result of prepayment or not is not relevant in the application of the proposed alternative treatments.

Situation 1:

For the rest of the life of the plan, service costs and MFR (in CU) are expected to be as follows:

	20X1	20X2	20X3	20X4	20X5	20X6
Service costs	10	10	10	10	10	10
MFR	15	15	15	15	15	15
Net annual amount	(5)	(5)	(5)	(5)	(5)	(5)
Cumulative amount	(5)	(10)	(15)	(20)	(25)	(30)

Asset recognised at the beginning of the 20X1:

- Alternative 1: CU 35
- Alternative 2: nil

Situation 2:

For the rest of the life of the plan, service costs and MFR (in CU) are expected to be as follows:

	20X1	20X2	20X3	20X4	20X5	20X6
Service costs	10	10	10	10	10	10
MFR	0	0	15	15	15	15
Net annual amount	10	10	(5)	(5)	(5)	(5)
Cumulative amount	10	20	15	10	5	0

Asset recognised at the beginning of the 20X1:

- Alternative 1: CU 35
- Alternative 2: CU 20

Under alternative 2, the maximum amount recoverable is reached in 20X2 and represents the sum of the surplus to be recovered throughout years 20X1 and 20X2 (i.e. CU 10 + CU 10).

If 20X3 were added, the asset recoverable under alternative 2 would reduce to CU 15 and would reduce further as consecutive years are added. However, this latter consideration, which would result from the application of IFRIC 14, is excluded from our proposal under alternative 2.

Situation 3:

For the rest of the life of the plan, service costs and MFR (in CU) are expected to be as follows:

	20X1	20X2	20X3	20X4	20X5	20X6
Service costs	10	10	10	10	10	10
MFR	15	15	0	0	15	15
Net annual amount	(5)	(5)	10	10	(5)	(5)
Cumulative amount	(5)	(10)	0	10	5	0

Asset recognised at the beginning of the 20X1:

- Alternative 1: CU 35
- Alternative 2: CU 10

Under alternative 2, it is necessary to reduce the amount recoverable in years 20X3 and 20X4 by the obligation that will arise in 20X1 and 20X2. This reflects the fact that it would not be appropriate to consider that an asset may be recovered but to ignore the liabilities that must be assumed before being able to benefit from the asset. Accordingly, the maximum amount recoverable is reached in 20X4 and represents the sum of the surplus to be recovered throughout years 20X1 to 20X4 (CU (5) + CU (5) + CU 10 + CU 10).

If 20X5 were added, the asset recoverable under alternative 2 would reduce to CU 5 and would reduce further if 20X6 is added. However, this latter consideration, which would result from the application of IFRIC 14, is excluded from our proposal under alternative 2.