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Your ref

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Response to Exposure Draft of a Proposed Amendment to IAS 19, Employee Benefits: The Asset Ceiling

Dear Sir David,

We welcome the opportunity to comment on the *Exposure Draft of a Proposed Amendment to IAS 19, Employee Benefits: The Asset Ceiling.* The views expressed in this letter are those of KPMG International.

General comments

Overall we believe that the amendment proposed by the IASB achieves the desired mechanical outcome, e.g. not generating a current period income statement gain/loss as a result of an actuarial loss/gain.

We support the Board's efforts to address the unintended and inappropriate consequence of IAS 19, as it is drafted currently. We believe that the Board's proposed approach, to work within the "corridor" method, is appropriate for the very limited issue the Board is seeking to address. The complexity of the amendment and its application (as demonstrated in even the simplified examples) is unfortunate and illustrates a more basic problem of the complexity of IAS 19 because of the compromises introduced through, amongst other things, the mechanics of the smoothing mechanisms.

We note that the Board has signalled its intention to add a project on pension accounting to its agenda in the near future and we encourage the Board to use that broader project to simplify the approach to this area.

Question 1: Is the issue identified of sufficient importance to warrant a limited amendment to IAS 19?

Yes, we believe that it is. The IASC concluded, when it revised IAS 19 in 1998, that it was not appropriate to recognise assets that are not recoverable, based on conditions existing at the balance sheet date. This is why the IASC included an asset limitation cap in paragraph 58. For the same reasons, we believe it would be inappropriate to accept a mechanical application of IAS 19 as currently drafted and recognise a gain and asset while not recognising the related actuarial loss. Therefore, although the issue involved is limited and technical, we support the Board's efforts to address it rather than either accepting a flawed application of IAS 19 as drafted currently or indirectly encouraging preparers, auditors and regulators to override an existing requirement of the standard in order to achieve a fair presentation.

Question 2 - If so, does the proposed amendment to IAS 19 (paragraph 58A) appropriately address this issue? Does it create any anomalies? If the proposed amendment is inappropriate, can you suggest an alternative?

We agree that the proposed amendment to IAS 19 will address this issue.

Question 3 - Should the limited changes become effective for accounting periods ending on or after 31 March 2002, with earlier application encouraged?

Yes, they should.

Question 4 - Do you agree that there should be no specific transitional provisions for the limited changes proposed in this exposure draft? Consequently, IAS 8, Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies, will be applied to any changes in accounting policies that are made to comply with IAS 19 if amended as proposed.

We agree with this proposal.

Other comments and questions

1. We believe that the presentation of the amendment could be modified to provide greater detail in the examples of the interaction of proposed paragraph 58A with existing paragraph 58. We believe all examples, not just example 1, should present separately the initial computation under paragraph 58 and the effect of paragraph 58A.

2. We encourage the Board to state more clearly the reason for its intended modification. We acknowledge the explanation given in paragraphs 78C, D and E in the Basis for Conclusions, but would suggest a description that is easier to read and understand, perhaps along the following lines:

> The asset recognition limitation in paragraph 58(b) of IAS 19 is written so that an asset recognised for a net pension surplus is not limited to the amount recoverable from refunds or reductions in future contributions. Instead, IAS 19.5 8(b)(i) increases the asset recognised (up to but not in excess of the net surplus amount computed under IAS 19.54) to include an amount equal to unrecognised actuarial losses and past service costs. This inclusion of

unrecognised actuarial losses and past service costs is consistent with the Board's intention to provide a corridor to reduce the reported volatility of pension assets and obligations.

However, in some situations the usage of the asset ceiling results in the recognition of a gain/(loss) as a result of past service costs or actuarial losses/(gains). This amendment is required to ensure that changes in the asset recognised for a net pension surplus do not impact the net pension expense (income) reported in the income statement when those changes relate to changes in unrecognised actuarial gains/losses that otherwise are not required to be recognised. Having such an income statement impact would be inconsistent with the Board's intention of providing a corridor to reduce volatility reported in the income statement. This amendment therefore accelerates recognition of amounts that otherwise would be deferred within the corridor. The amount for which recognition is accelerated equals the amount by which the change in the asset computed under IAS 19.58 exceeds the change in the present value of future refunds or contribution reductions.

3. In paragraph 58A(a) it may be useful to indicate that it is the net actuarial losses and past service costs ***for the current year*** that should be considered for immediate recognition. This recommendation applies also to paragraph 58A(b). The examples in appendix C illustrate this point.

4. In an introduction to the examples in appendix C, it may be useful to indicate that the periodic amortisation of unrecognised gains and losses has been ignored for simplicity.

5. IAS 19.58 refers to the "present value of any economic benefits available to the enterprise..." Simplistically, the present value of the economic benefits will increase each year, as a result of the unwinding of any discount. Should the "unwinding" of the discount be considered when assessing the portion of actuarial gains that will be recognised immediately in accordance with the proposed paragraph 58A?

Please contact Mark Vaessen at 020 7694 8089 or Mary Tokar at 020 7694 8288 if you wish to discuss any of the issues raised.

Yours faithfully

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