ACA Members' Conference 2016 – Current Accounting Issues (C27)

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The session takes a look at the main changes to pensions accounting over the past year and looks forward to some possible future developments.

Asset Ceilings

1. IAS 19

- IFRIC 14 sets out how to apply the asset ceiling under IAS 19, including the circumstances in which an additional liability needs to be recognised.
- There are two ways to justify an asset under IAS 19: refunds or reductions in future contributions. Both have been subject to change – or consultation about change – in the past year.

- On refunds, the June 2015 IAS 19 / IFRIC 14 exposure draft seeks to clarify what is meant by the unconditional right to a refund. For schemes where thirs parties (such as trustees) can "spend" surplus without the company's consent – such as by winding-up the plan or augmenting members' benefits – then the Company will not have an unconditional right to a refund under the terms of IFRIC 14.
- Not having an unconditional right to a refund can be significant, since any "minimum funding requirement" for past service that would lead to an IAS 19 surplus needs to be recognised as an additional liability on the company's balance sheet.
- The FRC is of the view that agreed deficit contributions under the UK funding regime constitutes a "minimum funding requirement". It is asking companies to disclose their approach to applying IFRIC 14 and how the exposure draft may affect this.
- However, as drafted, the changes to IFRIC 14 contain a number of areas of uncertainty.
- The consultation period on the exposure draft ended in October 2015 – a number of concerns were raised about the proposals, including by the ACA Accounting Standards Committee. However, we do not expect to know the direction that IASB will take until sometime in Q2 of 2016.

- On the reduction in future service contributions, there was an IFRC Interpretations Committee agenda decision in July 2015 that may affect the asset ceiling. Typically this will only be of interest where a company does not have an unconditional right to a refund at some point in the future.
- The agenda decision explains that – when calculating the asset ceiling as the difference between service cost and agreed future contributions – those future service contributions should be estimated beyond the end of the end of the schedule of contributions by following the statement of funding principles agreed with the trustees.
- The potentially reduces the asset ceiling as, currently, the asset ceiling is often calculated on the assumption that all future service contributions will cease at the end of the agreed schedule of contributions.

2. FRS 102

- Proposals made in FRED 55 were adopted by the FRC last February and are effective from the implementation of FRS 102
- This introduces a difference between FRS 102 and IAS 19 – as under FRS 102 it will not be necessary to show a larger liability than the FRS 102 deficit even if funding to a higher target with no prospect of a refund (an exception to this is for multi-employer schemes where the balance sheet liability is based on the agreed past service contributions).
- The FRC also made it clear in FRS 102 that funding policy disclosure requires a statement of the amount and timing of agreed deficit contributions.

Remeasurements

1. IAS 19 exposure draft

- The June 2015 exposure draft mentioned earlier also deals with how to calculate pension cost for the part-period after a plan amendment, curtailment or settlement takes place.
- For that part-period the assumptions applying at the date of the special event will apply, rather than the start of year assumptions.
- This would be a departure from usual practice under IAS 19, but in line with the ASC 715 approach.
- This creates uncertainty about the impact on P&L of a planned special event. It also raises a question about materiality – is a small plan amendment material if there has been a large enough change in financial conditions or the IAS 19 funded status since the start of the year?

2. Pensions flexibility

- Increased levels of transfer activity raises questions about if and when to make an assumption about the probability that members will transfer out.
- The implications of higher levels of transfer – whether assumed or actual – need to be considered carefully. In some cases they should be treated as a settlement, in other cases as an experience item. ASC 715 is relatively clear with the concept of the settlement threshold, compared to both IAS 19 and FRS 102.

Discount rates

1. Disaggregation

- Following guidance from SEC staff there is a lot of interest in using a "disaggregated" approach to discount rates under ASC 715.
- By applying the full yield curve to scheme cashflows a lower interest and service cost can be disclosed, provided that the corporate bond yield curve is upward sloping.
- The impact is less pronounced for interest cost under IAS 19 and FRS 102 since there is no separate expected return on assets assumption. Therefore the interest cost is based on the surplus/deficit rather than the whole obligation.

2. IASB research project

- The IASB's staff's review of the use of discount rates in IFRS highlights inconsistencies in the way that discount rates are derived and used in different accounting standards.
- With IAS 19 there is no stated objective for the use of discounting, leading to a rules-based approach to setting discount rates.
- As this is a research project there are no firm proposals for change at this stage.

Comprehensive review of IAS 19

- IASB is returning to an old problem to how satisfactorily account for schemes have some DB and some DC features.
- Various models are begin discussed – some old, some new – but at the moment there is no clear favourite.

Pension scheme accounts

- The introduction of FRS 102 affects the accounts of pension schemes themselves, but in a way different way to how companies account for their pension obligations.
- The key points of interest for actuaries will be around valuing scheme annuities, disclosure of investment risks and the allocation of investments to a three/four-level hierarchy.
- The FRC has taken on board comments that the hierarchy does not match the existing hierarchy in IFRS 13. It has proposed – in FRED 62 – to make this consistent with IFRS 13. There is the possibility of being able to early-adopt the proposed hierarchy for 31 December 2015 scheme year-ends provided that the FRC moves quickly enough to make the proposed changes to FRS 102.