From: George Kirrin
To: Asbcomment Letters;
Subject: The Financial Reporting of Pensions (A PAAinE Discussion Paper)
Date: 12 July 2008 11:04:09

You have invited comments on any aspect of the above paper by 14 July 2008. I offer comments as a trustee and members' representative:

Q1 Liabilities to pay benefits based on expectations of employees' pensionable pay when they leave service should be recognised by trustees for funding purposes.

For scheme accounting purposes, future liabilities should not be recognised on grounds that members and their representatives are more interested in individual benefit statements, and are also anxious that costs incurred by schemes, such as the very considerable costs of annual actuarial estimates and auditing,
should be based on a cost/benefit assessment of value for money. In my experience, members have no requirements for such liabilities to be included in scheme accounts, which are not "general purpose" financial statements, in the sense that I think I understand you mean for accounting by corporates or other
public interest bodies.

For scheme sponsor (employer) accounting purposes, I would support a liability to pay benefits that is recognised on current pensionable pay, including non-discretionary increases if material. That is because I believe such accounting, in most cases, will be based on going concern and surely should give a true
and fair view of the liabilities which the scheme sponsor has to pay. This falls short of "full (buy-out)" liabilities because [a] these do not seem to me, or to pensions lawyers with whom I have spoken, to be constructive or likely liabilities to be borne by shareholders, and [b] scheme sponsors continue to
demonstrate their ability to manage the potential scale of future liabilities by measures such as capping, "risk-sharing", partial or complete buy-in/buy-out at lower than "full" accounting estimates.

Q2 Liabilities are owed to individual employees and other beneficiaries, not to the workforce as a whole. Increasingly, I see workforces where there are a range of individual involvements - some still have defined final pay benefits, others have defined contribution (money purchase) benefits, others have no benefits at all
(other than State benefits or personal savings or inheritance). For funding purposes, I do not agree that the focus should shift from mechanisms that spread pension costs over expected service lives to the "principle" of reflecting (and thereby introducing a reporting bias in favour of fully funding or otherwise

matching) present obligations, including non-discretionary increases. In reading your discussion paper, I am struck by the fact that there is a chapter (number 2) on Liabilities to pay benefits, but no equivalent chapter on Investments to pay benefits.

Q3 No, for the reason stated in Q2 above. I would urge ASB and EFRAG to think again about investment to pay benefits.

Q4 To the extent that you mean where the employer has control of the plan, yes. But I detect elsewhere in the paper (eg 3.51 on page 88) a presumption that employers do not control plans here in the UK. I would again urge ASB, in particular, to do more work in this area, particularly where plans use corporate trustees, which are either subsidiaries of the sponsor for VAT planning and other reasons, and where the employer in effect controls the trustee's constitution through means of appointment and selection. You will be aware that many UK schemes have been reluctant to appoint up to 50% member-nominated trustees and/or independent trustees. This seems to me to suggest that sponsors still "control" plans in more cases than may be thought. Substance over form.

Q5 I note the concerns of Dutch representatives and others about removing the use of "corridor" approaches. My limited understanding of their plans is that the sponsors' obligations may not be the same as under other jurisdictions, such as the US and arguably the UK. I would again urge ASB and EFRAG to do more work with legal input on this. For scheme accounting, where the focus is on both historic stewardship and future funding (and the latter is better dealt with outside the scheme accounts through business plans and funding plans, where commercially sensitive issues about the employer covenant may be addressed in a more appropriate way), I disagree fundamentally that immediate market changes should be recognised. For sponsor/employer accounting, the focus may be different, but the knock-on impact for plans should be assessed and re-considered before moving to immediate recognition. I also did not see "immediate" recognition, for example, by banks and other financial institutions when the so-called "credit crunch" began to bite last year. I find it strange (but perhaps we are viewed as a soft target) that pensions accounting should be "leading" when other accounting remains less "immediate".

Q6 Regulatory measures are leading the way in the UK at this time. If ASB/IASB do not plan to implement aspects of the discussion paper before 2011 or later, as I have heard, then I think you will find that trustees and UK sponsors will be more interested in regulatory measures, certainly for business planning purposes.

I do not understand what is meant by a "risk-free" rate, but suspect you mean in a UK context the return on index-linked gilts. By "return", I also suspect you mean spot yield, not total return or term-adjusted yield curves. Again, I would urge ASB and EFRAG to do more work on this as an investment proposition before selecting it as a basis for accounting discounting.

On disclosure of riskiness, recent honesty from banks such as UBS would suggest that conventional disclosure and monitoring based on VaR95 has been flawed. Again, I would urge ASB and EFRAG to do more research in this area.

Expenses of administering plan benefits should be reflected in funding the liabilities. With accounting by schemes, I refer you to my earlier comments about an emphasis on historic stewardship. With accounting by employers, I would ask you to consider whether the proposed treatment is consistent with other future expenses, such as corporate governance (or Board overheads). These seem to me to be more like annual costs than future costs to be discounted and accrued immediately.

Q7 Funding plans reflect the (prudent) probabilities of different outcomes, so I would expect any accounting to follow similar principles. I would, however, urge ASB and EFRAG to do more work on the difference between "prudent" estimates for funding purposes and "best" estimates for accounting purposes. Best estimates, I am informed, are to be based on a 50% likelihood, whereas prudent estimates tend to be based on two-thirds or more, less only where the sponsor covenant is a particularly strong one, and even then (for example, UK local government pension schemes) the covenant strength may often be ignored and greater prudence adopted. I have also heard legal advisers warn trustees against "excessive prudence".

Q8 See my comments at Q2 above, that I do not think ASB and EFRAG have considered investment to pay benefits sufficiently at this stage to be able to finalise a position on whether or not to book assets at current values. I would certainly support disclosure of assets at current values, but also urge ASB and EFRAG to look again at the limitations of so-called "current values". In my experience as a trustee, less liquid assets appear less volatile because of limited trading, and some of that trading is "secondary" in nature, which may be more artificial than full realisation. Supposedly more liquid assets tend to be valued at the latest trade, which may be misleading either on grounds of scale (both within the security concerned and also the relevant market volume as a

whole). Realisation of asset portfolios typically takes time and involves selling costs, particularly if proceeds are reinvested rather than cashed to pay benefits.

Q9 See my earlier comments about the notion of control at Q4 above. Booking of net pensions surpluses or deficits in employer/sponsor accounting seem to me to be flawed. Legal obligations may differ in different jurisdictions, as may the time profile of cash and non-cash (eg underwriting) commitments. Disclosure would be another matter, but again more context could be added regarding the time scale and likely (prudent|) investment returns which may or may not accrue. Trustees in the UK already get an estimate of direct buy-out as part of the regulatory basis of assessing funding requirements.

Q10 Certainly as trustees we would wish to use decomposition and sensitivity analyses. I would have thought the same principles would appeal to sophisticated users of financial statements such as security analysts and public interest regulators.

Q11 Actual returns should be disclosed alongside expected returns. This is certainly the case within some trustees' business and funding plans and performance monitoring.

Q12 I am in support of more disclosure generally. In the 21st century, we have tools such as hypertext linking and search facilities to access much larger information databases. I would urge ASB and EFRAG to do more work generally to encourage "general purpose" reports to adopt a pyramid structure, from a so-called "executive" summary at the top to every level of detail at the bottom and in-between. While financial statements may appear longer to many, their accessibility is frankly much poorer than the shorter-form financial statements I recall reading and using in the latter half of the 20th century. Alongside accounting standards on issue-based matters, I would hope any framework methodology looks beyond the narrow confines of public accounting to look at leading-edge information technology. I keep reading that accountants are just the messenger. Well, in that case they should look to the technology used (and the many opportunities to date which have been wasted) to communicate better.

Q13 Yes. I'm sure ASB (or PRAG?) could look at practice in the UK's multi-employer schemes in local government, industries such as railways post 1993, the motor trade, the coal industry post 1994, etc.

Q14 No, for the reasons mentioned at the very outset in Q1 above. In a UK

context, the ASB should revisit the work done recently by DWP and The Pensions Regulator. Plan financial statements in the UK (and probably elsewhere too) are less of a priority than improving plan business planning, including funding

planning and monitoring. When trustees have limited time and budgets, it would seem to me to be a better investment to make a step change in business planning and budgetary control than to waste money on financial statements which very few request or use for decision-making.

Q15 I think ASB and EFRAG need to do more work here. While I can see how the employer covenant can be confidentially addressed by plan trustees and their professional advisers in a planning and monitoring context, I am less clear on how easy (and cost-effective and whether or not counter-productive) this would

be in plan financial statements. I'm reminded that PRAG seemed to back off here when finalising the last SORP revision in May 2007. They must have had good reasons to do so.

Q16 Developments in pensions buy-outs need further work, particularly for the so-called "buy-in" solutions on offer. This seems to me that employer covenant risk is being replaced by solution provider risk, but standards here seem to be either non-existent or "lite". I'm also not clear where, in a UK context, local

government and other public sector pensions lie in all this. It seems unfair that standards in private sector pensions seem to develop at a different rate to public sector pensions. Surely one of the ways to defuse some of the emotions around this whole area and attempt to reconcile politicians with their

electorates would be to adopt similar standards to all benefits, particularly post-employment benefits. I also question whether executive pension arrangements, which tend no longer to feature among closed UK schemes, are fully described, particularly in terms of discretions and pre-retirement settlements.

Q17 I would be interested to know what contact ASB and/or EFRAG have had with trades unions, as members' representatives. Brendan Barber recently in another UK pensions context (Myners Principles) questioned the inclusiveness of consultations and task forces set up to progress changes. ASB may wish to

consider the composition of its Pensions Advisory Panel, if it continues, in appearing to lack trade union representation. Cost-benefit analysis in other areas usually means some sort of market impact assessment (such as trustees should do before and after deciding to sell assets to pay benefits or to reinvest for

future benefits). I didn't see one of these in the discussion paper, but would have thought one could be built up for each EU country jurisdiction?

I close by thanking you for this opportunity to comment. I shall be happy for

these personal views to be published on your website or in any similar form. I look forward to reading the views of DWP and others who have said they will comment. I do hope that your comments will include some from trades unions too.

Yours faithfully, George Kirrin

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