From: Edward Beale
To: UKFRS
Subject: FRED 55
Date: 21 August 2014 10:56:47

Dear Jenny

I am responding to the consultation FRED 55, both as director of a small investment company and as chairman and member of the audit committees of two AIM companies with defined benefit pension plans. The comments below are from the perspective of an informed investor, rather than as a preparer of accounts.

My response to both the questions is **No**.

That this consultation is considered necessary serves only as proof that the FRC has overcomplicated the requirements for accounting for defined benefit pension plans.

The FRC should be considering how its standards can encourage the communication of useful information to investors. The absence of clear and concise standards only serves to hinder clear and concise reporting.

Relevant and reliable information

Most of the numbers that the FRC currently requires to be put into the accounts in relation to defined benefit pension plans are not only not understandable and highly unreliable due to volatility, they are also in many cases irrelevant. They do not communicate anything about the magnitude and timing of future cash flows of either the company or the DB pension plan.

The net present value of a defined benefit liability (or even asset) is of negligible relevance to me as a user. These are highly volatile numbers which display massive movements as a result of small changes to underlying model assumptions. And it is not even as if many of the underlying assumptions are consistent with the life of the schemes. Schemes typically have lives in excess of 20 years, but standards require that assumptions on interest rates and inflation are based on current measures not long term averages.

This is an example of spurious accuracy in accounts that has the potential to mislead users who are not experts, i.e. most users.

The only information content in an accounting valuation is whether the plan is definitely in a large surplus or deficit position or somewhere inbetween. This information can be obtained from a funding valuation without the additional cost of having to prepare a valuation just for accounting purposes.

As a user of accounts the information that I would like to see in relation to DB pension plans is:

- Where a scheme is still open, the employer and employee cash cost in respect of benefits accruing in the period, and an indication of future cash costs
- The magnitude and timing of the company's expected and/or agreed payments to eliminate any funding deficit, and when this is next due for renegotiation
- The size of the PPF levy
- The magnitude and timing of payments out of the fund to pay pensions (probably best

shown graphically), the key assumptions underlying the calculation of those payments and sensitivities surrounding them.
- The investment policy of the fund, the value of assets by type, the returns achieved (over, say, the last 3 years) and projected by asset type.

In my opinion this information can be best communicated by recognising in the statement of financial position a liability for the company's commitment to eliminate any funding deficit, and not by consolidating the DB pension plan. The other information above can then be provided in the notes to the accounts.

Comparability

Comparability is best served by highlighting the cash payments that need to be made by the company to the DB pension plan, rather than a highly volatile and unreliable net present value.

Consolidation of DB Pension Plans

As an aside, if DB pension plans were considered for consolidation following the rules for consolidation of SPEs, most would probably not be consolidated because of lack of the necessary degree of control (FRS 102 9.4). Consolidation of DB pension plans is an exception to the rules in FRS 102 for consolidation of SPEs and this exception has never been justified by the FRC. The conditions in paragraph 9.11 of FRS 102 are factors that might indicate control, not an extension of the requirement for control, and the UK statutory regime is such that companies should not be able to control their DB pension plans.

Influence of IFRICs

FRS 102 is clear that if an accounting treatment is not specified in the standard, preparers should look to develop an appropriate treatment based on other FRS, SORPS or on the concepts and pervasive principles underlying the standard (see FRS 102 10.4-5). While IFRIC pronouncements may be useful they are not binding (10.6). Changing FRS 102 just because an IFRIC has the potential to cause confusion is an unnecessary over-reaction. There is no justification for the FRC to make such changes outside of a normal review schedule. If the FRC is concerned that IFRIC 14 might cause confusion, then a more proportionate solution would be to issue a press notice to this effect and emphasising the importance of paragraphs 10.4-5 over 10.6.

By seeking to make changes because of IFRIC 14, the FRC is undermining the position that it took when it adopted FRS 102.

The FRC needs to consider the source of the demand for the proposed changes to FRS 102, their vested interests, and the weight to be put on the opinion of such constituents in future. FRS 102 as it stands does not require either the omission or double counting of liabilities and there is no need for a preparer to look at IFRIC 14, even if they knew of its existence and where to find it.

If you would like to discuss any of the above points further, please do not hesitate to contact me.

Kind regards
Edward Beale
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