# Basis for Conclusions

*This Basis for Conclusions accompanies, but is not part of, AASB 1056. The Basis for Conclusions was originally published with AASB 1056 as issued in June 2014.*

## Introduction

BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board's (AASB's) reasons for reaching the conclusions in AASB 1056 *Superannuation Entities*, which is the replacement Standard for AAS 25 *Financial Reporting by Superannuation Plans*. This includes the development of the proposals made in two Exposure Drafts (ED 179 *Superannuation Plans and Approved Deposit Funds* and ED 223 *Superannuation Entities*) and the AASB's re-deliberations of those proposals. Individual Board members gave greater weight to some factors than to others.

BC2 In the process of developing AASB 1056, the AASB also identified a number of topics that are beyond the scope of AASB 1056 or are linked to issues that would have an impact on a wide range of entities. These topics include issues around the measurement of liabilities using discounted cash flow techniques and the nature of the reporting entity in a superannuation context, which are likely to form the basis of future research by the AASB Research Centre. The outcomes of this research might impact on issues the AASB raises with the International Accounting Standards Board (IASB) or impact on the application of Australian Accounting Standards.

## Background

### Comprehensive review of general purpose financial reporting requirements for superannuation entities

BC3 When originally drafted, AAS 25 was intended to provide the main recognition, measurement and disclosure requirements applicable to superannuation plans. Accordingly, the Standard was intended to apply in the place of other Australian Accounting Standards on financial reporting issues that were considered most significant to superannuation plans. AAS 25 was also intended to address the financial reporting issues that superannuation plans were specifically dealing with at the time (the early 1990s).

BC4 However, in recent years, developments in the superannuation industry and the adoption of International Financial Reporting Standards (IFRS) mean there has been the need for a comprehensive review of the general purpose financial reporting requirements applicable to superannuation entities, particularly the requirements in AAS 25. For example, the increasing significance of superannuation entities that have both defined contribution members and defined benefit members (hybrid superannuation entities) highlights deficiencies in AAS 25, which had requirements that lead defined contribution and defined benefit superannuation plans to prepare their financial statements on different bases.

BC5 There were also deficiencies in AAS 25 when compared to the requirements in Australian Accounting Standards applied by other entities. These include AAS 25 permitting entities not to recognise member liabilities in respect of defined benefit members.

BC6 Only limited improvements were made to AAS 25 since its issue in 1993.[1]

### The AASB's policy on IFRS

BC7 In 2004, when the AASB was implementing the decision to adopt IFRS, it considered the merits of IAS 26 *Accounting and Reporting by Retirement Benefit Plans*, which was originally issued in 1987 and has changed little since that time. The AASB concluded that IAS 26 should not be adopted in Australia because its application by Australian superannuation entities would be unlikely to result in financial statements that meet

1 In late 2005, as a result of a process involving the issue of Invitation to Comment ITC 9 *Superannuation Plans – Financial Liabilities*, the AASB made two amendments to AAS 25 through AASB 2005-13 *Amendments to Australian Accounting Standards*. One amendment was to require a hedging instrument or derivative to be recognised at net market value, whether it has a debit or credit balance, with any changes recognised in profit or loss for the period. A second amendment confirmed that a superannuation plan holding a controlling interest in another entity would apply AASB 3 *Business Combinations* and AASB 127 *Consolidated and Separate Financial Statements*. AAS 25 was also amended in 2013 to remove references to the materiality Standard through AASB 2013-9 *Amendments to Australian Accounting Standards – Conceptual Framework, Materiality and Financial Instruments*.

users' information needs and would potentially reduce the quality of financial reporting by superannuation entities.

BC8 In particular, the AASB considered that IAS 26 would not result in useful information on the capacity of a superannuation entity to meet its member liabilities. For example, IAS 26:

(a) contemplates that a plan would invest in assets for which it is impossible to estimate fair value, and permits those assets to be measured at an amount other than fair value; and

(b) permits the actuarial present value of 'promised retirement benefits' to be based on either current or projected salary levels.

BC9 In contrast to IAS 26, AAS 25 required all assets held by a superannuation plan to be measured at a current value (consistent with Australian prudential measurement requirements). The AASB also considered other relevant IFRS being adopted in Australia and noted that the requirements of IAS 26 are highly dissimilar from the requirements of most other IFRS. For example, in contrast to IAS 26, IAS 19 *Employee Benefits* (AASB 119 *Employee Benefits*) requires plan assets attributable to defined benefit obligations to be measured at fair value in determining an employer-sponsor's net defined benefit obligations.

BC10 The AASB considers that the reasons identified for not adopting IAS 26 (and retaining AAS 25) remain valid in respect of AASB 1056.

BC11 The AASB also considered the implications of withdrawing AAS 25 and requiring superannuation entities to apply, where appropriate, Australian Accounting Standards. The AASB concluded that, while the financial reporting requirements for superannuation entities can, in many respects, be enhanced by being more closely aligned with corresponding requirements of other Standards, there remains a need for a specific Standard to help ensure the general purpose financial statements (GPFSs) of superannuation entities cater for the needs of users.

## Users of the general purpose financial statements of superannuation entities

BC12 The AASB concluded that the following are most prominent among the users of GPFSs of superannuation entities:

(a) current and potential members and beneficiaries;

(b) parties that act on behalf of members and beneficiaries, such as financial analysts, advisors and unions; and

(c) employer-sponsors.

BC13 This is because the primary responsibility of superannuation entities is to provide retirement benefits to their members, and both employees and employers contribute to those entities.

BC14 Financial analysts and advisors are generally servicing a wide variety of existing and potential superannuation entity members and may use superannuation entity financial statements in the course of their work.

BC15 The *Superannuation Guarantee (Administration) Act 1992* provides most superannuation members the right to choose the superannuation entity managing their entitlements, thereby reducing the incentives for employers to provide corporate superannuation arrangements. An employer without a plan of its own is required to identify an appropriate default plan for employees. Consequently, employers seeking a superannuation entity to meet their employees' superannuation needs might use the financial statements of an entity to gain assurances regarding its financial position and performance.

BC16 Employers that provide defined benefit entitlements, particularly through master trusts and other similar arrangements, are interested in a superannuation entity's financial statements in order to evaluate whether the arrangement is cost-beneficial and the capacity of the assets to fund entitlements as and when they fall due.

BC17 The AASB concluded that, for some items, the reporting requirements that would otherwise apply under Australian Accounting Standards would not necessarily give rise to relevant financial information for users of superannuation entity financial statements. This is particularly the case in relation to measuring assets, recognising member liabilities, measuring defined benefit member liabilities and disclosing information about the amount of, and the entity's capacity to meet, member liabilities. As a consequence, the AASB concluded there is a need to:

(a) require superannuation entities to depart from Australian Accounting Standards on some topics;

(b) limit the accounting treatments available to superannuation entities in other Australian Accounting Standards; and

(c) require superannuation entities to provide information about items and events specific to them.

## A replacement Standard for AAS 25

BC18 In May 2009, the AASB published ED 179 containing proposals for a replacement Standard for AAS 25. The AASB received 20 comment letters on ED 179 from a range of constituents, including superannuation plans, superannuation industry representative bodies, accounting firms, professional accounting and actuarial bodies and service providers to the superannuation industry. The AASB also held roundtable discussions on ED 179 with a range of constituents with an interest in the superannuation industry to enable them to discuss the proposals directly with AASB members.

BC19 Based on the responses to ED 179 and the AASB's redeliberations, in December 2011, the AASB published ED 223 containing revised proposals for a replacement Standard for AAS 25. The AASB received 17 comment letters on ED 223 from a range of constituents and also held roundtable discussions on ED 223. The feedback from both ED 179 and ED 223 and other forms of outreach that the AASB has performed between 2012 and 2014 have shaped AASB 1056.

BC20 The majority of respondents to both ED 179 and ED 223 expressed broad support for developing a replacement Standard that:

(a) provides greater transparency and consistency in reporting by superannuation entities; and

(b) substantially aligns the reporting practices of superannuation entities with other entities applying Australian Accounting Standards, thereby facilitating greater comparability.

BC21 Each of the respondents expressed concerns with one or more of the proposals in ED 179, particularly on cost-benefit grounds, which the AASB considered in developing ED 223. Further revisions have been made in developing AASB 1056 in response to issues raised by constituents on the revised proposals in ED 223. The revisions arising from the consultative process include matters relating to:

(a) presenting financial statements, including a statement of changes in member benefits;

(b) recognising defined benefit member liabilities;

(c) measuring both defined contribution member and defined benefit member liabilities;

(d) measuring assets;

(e) accounting for liabilities and assets that might arise from insurance arrangements provided to members;

(f) disclosing information about the nature, extent and management of credit, liquidity and market risks; and

(g) disclosing disaggregated information.

BC22 In the process of finalising AASB 1056, the AASB approved a Draft AASB 1056 for fatal-flaw review that was published in December 2013 for a 60-day comment period. The comments received during that process helped the AASB to refine its requirements before making AASB 1056.

# Application of the replacement Standard

## The reporting entity concept and superannuation entities

BC23 AAS 25 applies to the financial statements of each private or public sector superannuation plan that is a reporting entity or is not a reporting entity and prepares financial statements which purport to be GPFSs.

BC24 The AASB considered the advantages and disadvantages of the replacement Standard for AAS 25 applying to different types of superannuation entities, including superannuation plans, approved deposit funds, eligible rollover funds, pooled superannuation trusts, Small Australian Prudential Regulation Authority (APRA) Funds (SAFs) and self-managed superannuation funds (SMSFs).

BC25 The AASB proposed in ED 179 and ED 223 that the replacement Standard for AAS 25 should retain the reporting entity concept, particularly in view of the AASB's current research on the concept. Accordingly, the replacement Standard would apply to each reporting entity that is a defined contribution plan, defined benefit plan, 'hybrid' plan (comprising both defined contribution and defined benefit members), private sector plan, public sector plan, eligible rollover fund or approved deposit fund.

BC26 Whilst a number of respondents to ED 179 and ED 223 argued that some SMSFs would often be reporting entities, the AASB concluded that an entity such as a SMSF would not normally be a reporting entity because:

(a) each member is required to be a trustee (or a director of a corporate trustee) and to have access to the entity's financial information; and

(b) the primary external user is the Australian Taxation Office, which requires specific information for compliance and regulatory purposes.

BC27 During its deliberations, the AASB gave particular consideration to whether the replacement Standard for AAS 25 should apply to pooled superannuation trusts. The AASB noted pooled superannuation trusts and superannuation plans, particularly defined contribution superannuation plans, share a number of characteristics. For example, they are both required to comply with many of the same prudential requirements, are taxed at the same concessional tax rate and accept monies from other superannuation entities.

BC28 However, the AASB concluded pooled superannuation trusts are more in the nature of investment trusts, such as managed investment schemes, because they have unitholders rather than members, and there are no member-based restrictions over when they can distribute funds to a unitholder. Accordingly, to facilitate comparable financial reporting among investment-type trusts, the AASB concluded pooled superannuation trusts should apply Australian Accounting Standards in the same manner as managed investment schemes.

BC29 Respondents to ED 179 and ED 223 expressed general agreement with the proposed scope and the AASB concluded that the replacement Standard for AAS 25 should reflect those application proposals.

## Tiers of Australian Accounting Standards

BC30 Subsequent to issuing ED 179, the AASB promulgated AASB 1053 *Application of Tiers of Australian Accounting Standards*, which establishes a differential reporting framework consisting of two tiers of reporting requirements for preparing GPFSs:

(a) Tier 1: Australian Accounting Standards; and

(b) Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements (RDR).

BC31 In the process of developing AASB 1053, the AASB issued ED 192 *Differential Reporting Framework* (February 2010), which noted that:

"AAS 25 *Financial Reporting by Superannuation Plans* has been excluded from the RDR on the grounds that entities applying AAS 25 would be superannuation plans registered with the Australian Prudential Regulation Authority, which are regarded as publicly accountable in this Exposure Draft. Superannuation entities that apply AAS 25 and prepare general purpose financial statements are required, under the *Superannuation Industry* (*Supervision*) *Act 1993,* to hold assets in a fiduciary capacity for their members. In addition, most superannuation entities, particularly public offer superannuation plans and approved deposit funds, have a broad range of members who have no involvement in the day-to-day operations of the entity."

BC32 Some respondents to ED 192 questioned whether all APRA-regulated entities, particularly SAFs, should be considered to have 'public accountability'. They noted that, while SAFs lodge financial statements with APRA, they are not made publicly available, APRA does not mandate that SAFs prepare GPFSs and most, if not all, SAFs are similar in nature and size to SMSFs.

BC33 During its redeliberations on ED 179, the AASB noted SAFs are defined by APRA as superannuation plans with less than five members and have an Extended Public Offer Entity licence. As such, members of a SAF appoint a trustee with a Public Offer Entity licence to manage the plan on their behalf. While SAFs must lodge APRA returns that include information reported in their financial statements, this information is not publicly available for individual SAFs. In addition, the AASB noted SAFs would not be considered publicly accountable or reporting entities because they are small, have few members who have a close relationship with the trustee and SAFs normally prepare special purpose financial statements.

BC34 ED 223 included a question asking constituents whether there are any superannuation entities that would meet the criteria in AASB 1053 for applying Tier 2 disclosure requirements and the AASB also conducted targeted outreach on the issue, including in respect of so-called 'paragraph 66 plans'. Paragraph 66 of AAS 25 permits superannuation plans whose only assets (other than temporary deposits at call with a bank) are endowment, whole of life or other long-term insurance policies which match and fully guarantee the benefits to be paid to individual members to apply only a sub-set of its recognition, measurement and disclosure requirements, provided they report items such as: whether those policies have been fully maintained as directed by the insurer(s), the identity of the insurer(s), and amounts contributed by employers and members during the reporting period, and the expenses of the plan incurred by the trustees during the reporting period.

BC35 The AASB concluded superannuation entities are currently divided between Tier 1 entities (including industry plans, public sector plans, retail plans, eligible rollover funds, corporate plans and approved deposit funds) and non-reporting entities (including SAFs and SMSFs). Accordingly, in the context of AASB 1056, there are entities that prepare GPFSs by applying all the relevant Australian Accounting Standards and those that need not prepare GPFSs. Consistent with AASB 1053, there is no applicable second Tier of general purpose financial reporting requirements for superannuation entities.

## Definitions

### Superannuation entity

BC36 AAS 25 defines a superannuation plan as "an arrangement whereby it is agreed, between trustees, employers or self-employed persons, that benefits be provided upon retirement of plan members or upon their resignation, death, disablement or other specific event(s)." It also includes commentary that notes a superannuation plan may be constituted as either a separate entity or a number of separate entities established to administer aspects of the plan, such as when one entity manages contributions and another administers benefit payments. AAS 25 applies regardless of whether a separate pool of assets from which benefits are paid is created.

BC37 In recognition of the significant legislative and other changes that have occurred in a superannuation context, ED 179 and ED 223 proposed:

(a) a definition of 'superannuation entity'; and

(b) definitions for the terms 'superannuation plan' and 'approved deposit fund' (to form the basis for the 'superannuation entity' definition) that are consistent with the equivalent definitions in the *Superannuation Industry* (*Supervision*) *Act 1993* and accompanying Regulations.

BC38 The AASB noted that, given the extent of regulation about the forms superannuation arrangements can take, particularly in the private sector, the proposed definitions received general support from those responding to ED 179 and ED 223. However, the AASB also noted that some of the superannuation arrangements in the public sector are not as straight-forward.

BC39 The AASB concluded that the proposed definitions are appropriate for AASB 1056. However, the AASB also noted that entities, particularly in the public sector, would need to consider the nature of their activities and the boundaries of the entity to determine if they are superannuation entities or only custodial arrangements. For example, there may be cases in the public sector where an entity administers information about members and their benefits, but is not liable for paying benefits to members.

### Defined contribution member and defined benefit member

BC40 Due to the increasing significance of superannuation entities that have both defined contribution members and defined benefit members, AASB 1056 does not have definitions of 'defined benefit plan' and 'defined contribution plan' (as in AAS 25). The AASB instead developed definitions of 'defined benefit member' and 'defined contribution member'. These are based on the AASB 'plan' definitions and the relevant definitions in AASB 119. These definitions were generally supported in the comments received on ED 179 and ED 223.

BC41 In the context of the Draft AASB 1056 for fatal flaw review, some constituents commented that the AASB should consider using the definition of 'defined benefit member' in the prudential regulation. However, the AASB concluded that the regulatory definition might change in ways that would not necessarily suit the aims of AASB 1056. Nevertheless, in terms of the current definitions, the AASB does not expect there to be any difference between those members identified as being either defined benefit members or defined contribution members based on definitions in AASB 1056 and those members identified as being either defined benefit members or defined contribution members based on the defined benefit member definition under prudential regulation.

## Applying recognition and measurement requirements in Australian Accounting Standards

BC42 Under AAS 25, a superannuation plan applied other relevant Australian Accounting Standards with the key exceptions of some aspects of: financial statement presentation (defined benefit plans can present a statement of net assets and a statement of changes in net assets), asset measurement (net market value is required), and defined benefit member liability measurement (actuarial valuations performed on at least a triennial basis).

BC43 The AASB decided there are no compelling reasons for retaining this approach and concluded that a superannuation entity should apply the presentation, recognition and measurement requirements in other relevant Australian Accounting Standards, except in relation to:

(a) measuring most assets at fair value through profit or loss;[2]

2 This exception includes fair valuing acquired intangible assets each period, but would apply only when a superannuation entity is required to prepare consolidated financial statements in accordance with AASB 10, as amended by AASB 2013-5 *Amendments to Australian Accounting Standards – Investment Entities*.

(b) presenting a statement of changes in member benefits;

(c) measuring defined benefit member liabilities; and

(d) measuring liabilities and assets arising from insurance arrangements it might provide to its members.

## Measurement of assets at fair value

BC44 AAS 25 required a superannuation plan to measure its assets at market value less costs that would be expected to be incurred in realising the proceeds from their disposal. The AASB considered a number of alternative approaches, including measuring assets:

(a) in a manner consistent with the approach under AAS 25;

(b) in accordance with the various requirements of relevant Australian Accounting Standards; and

(c) in a manner consistent with AASB 1023 *General Insurance Contracts* and AASB 1038 *Life Insurance Contracts*, under which assets are required to be measured at fair value through profit or loss where that is required or permitted in other Australian Accounting Standards.

BC45 With respect to approaches (b) and (c), the AASB noted some Australian Accounting Standards currently provide a choice between alternative measurement methods, particularly cost and fair value through profit or loss, and some require cost or fair value through other comprehensive income, for particular types of assets. However, the AASB regards measurement of superannuation entity assets at cost or at fair value through other comprehensive income to be inconsistent with the needs of users in the investment performance of superannuation entities, and inconsistent with the prudential measurement requirements.

BC46 The AASB concluded the AAS 25 approach is an appropriate starting point, and that there are a number of compelling arguments in favour of requiring a superannuation entity to use fair value through profit or loss rather than net market value.

BC47 Both net market value measurements and fair value measurements provide useful information for users of the financial statements of a superannuation entity about:

(a) the capacity of a superannuation entity with defined contribution members to pay benefits as the information reflects the interests of members; and

(b) the financial position (solvency) of a superannuation entity with defined benefit members as the information reflects the capacity of the entity to meet member liabilities.

However, the approach for measuring assets under AAS 25 is inconsistent with the approach for measuring equivalent assets under other Australian Accounting Standards. In addition, fair value measurement is more comprehensively dealt with in the accounting literature, in particular, AASB 13 *Fair Value Measurement*. Accordingly, the AASB considers requiring fair value measurement would enhance the comparability of the financial statements of superannuation entities with other entities.

BC48 Both ED 179 and ED 223 proposed that superannuation entities measure their assets at fair value through profit or loss, with the exception of tax assets, and any assets arising from insurance arrangements the entity provides to its members.

BC49 Most of the respondents that specifically commented on the ED 179 and ED 223 asset measurement proposals expressed general agreement with them. One respondent expressed concern that assets be measured at 'bid' prices and liabilities be measured at 'ask' prices. However, the AASB noted that entities reporting under AAS 25 should, in principle, measure their assets at bid prices and liabilities other than member liabilities at ask prices because AAS 25 is based on an exit value model. The AASB also noted that, while some superannuation entities may be currently measuring assets at their 'mid' prices, this is presumably because any differences between the assets' bid and mid prices are not material.

BC50 In the interests of providing useful information on investment performance and in light of respondents' comments, the AASB concluded the replacement Standard for AAS 25 should require fair value through profit or loss measurement for most assets.

BC51 In coming to this conclusion, the AASB noted:

(a) a superannuation entity would apply AASB 13, which takes a principles-based approach to determining fair value measurement; and

(b) any implementation issues a superannuation entity might encounter in applying AASB 13 are unlikely to be unique and would potentially arise in the context of other investment-type entities, such as managed investment schemes.

Accordingly, the AASB concluded it is not necessary to include additional fair value measurement guidance in the replacement Standard for AAS 25.

## Transaction costs

BC52 Under AAS 25, a superannuation plan is required to measure its assets net of anticipated disposal costs. In developing ED 179, the AASB considered a number of different treatments for transaction costs, including:

(a) separate recognition as an expense when incurred; and

(b) as a reduction of the carrying amounts of assets.

BC53 The AASB concluded ED 179 should propose transaction costs be treated as a reduction in the carrying amounts of assets because:

(a) members and beneficiaries would regard information about assets net of transaction costs as useful as it might have a direct bearing on assessing a superannuation entity's capacity to pay benefits;

(b) it would facilitate alignment between financial reporting requirements and member reporting practices; and

(c) it is consistent with the treatment of assets under some Australian Accounting Standards, such as AASB 5 *Non-current Assets Held for Sale and Discontinued Operations* in respect of assets held for immediate sale.

BC54 Several respondents to ED 179 expressed disagreement with the proposal to adjust fair value amounts for transaction costs because:

(a) the treatment is inconsistent with the approach required under most Australian Accounting Standards, including AASB 139 *Financial Instruments*: *Recognition and Measurement*;[3] and

(b) transaction costs are generally an immaterial amount relative to a superannuation entity's net assets.

BC55 During its redeliberations on ED 179, the AASB also noted:

(a) AASB 13 requires that, while transaction costs be considered when determining the most advantageous market, the price used to measure the fair value of an asset (or liability) should, in principle, not be adjusted for such costs. As noted in paragraph 25 of AASB 13:

> "… Transaction costs are not a characteristic of an asset or a liability; rather, they are specific to a transaction and will differ depending on how an entity enters into a transaction for the asset or liability…"; and

(b) defined contribution members and beneficiaries would regard information about assets net of transaction costs as useful because it may help clarify whether all members and beneficiaries are being treated equitably, including different generations of members.[4] However, the AASB rejected the intergenerational equity argument, noting that it would be better facilitated by a superannuation entity determining crediting rates for defined contribution members on a basis that reflects anticipated transaction costs. The AASB also noted that these types of intergenerational equity issues are not as relevant in a defined benefit context because benefits are determined on the basis of a member's salary.

BC56 In light of respondents' comments, ED 223 proposed not permitting the carrying amounts of assets measured at fair value to be adjusted for transaction costs. The AASB also proposed that, to facilitate consistency across superannuation entities in relation to transaction costs, the application of AASB 5 should be prohibited.

BC57 There was general support from constituents commenting on the asset measurement proposals in ED 223 and the AASB concluded fair values should not be adjusted for transaction costs.

---

3 AASB 9 *Financial Instruments* had not yet been issued.

4 Intergenerational inequities can arise when exiting members do not 'pay' a share of the transaction costs because the superannuation entity has the capacity to pay departing member benefits out of cash on hand or else out of ongoing contributions and income. In such circumstances, members who remain in the entity may eventually incur transaction costs that would otherwise have been shared equally amongst all members if they had all exited the entity at the same time. In addition, members with relatively large account balances may be charged transaction costs as a consequence of their superannuation plan selling some of its assets whereas other members with relatively smaller balances may not be charged transaction costs if their entitlements are paid out of funds from other sources.

### Measurement of liabilities other than tax liabilities, member liabilities and liabilities arising from insurance arrangements provided to members

BC58 AAS 25 required a superannuation plan to measure its financial liabilities at net market value.

BC59 During its deliberations on the proposals in ED 179 and ED 223, the AASB considered the different ways in which a liability can be measured under Australian Accounting Standards, in particular:

(a) at fair value; and

(b) at amortised cost.

BC60 The AASB decided amortised cost is not an appropriate basis in a superannuation context because it would not result in useful information to users. Accordingly, the AASB proposed that a superannuation entity should measure its liabilities at fair value, with the exception of member liabilities, tax liabilities, and liabilities arising from insurance arrangements the entity might provide to its members. In addition, consistent with its decision in relation to the treatment of transaction costs in respect of assets, the AASB proposed in ED 223 that a superannuation entity should treat transaction costs attributable to each liability measured at fair value as an increase in its carrying amount.

BC61 Consistent with constituent comments on measuring assets, the majority of respondents agreed with the ED 223 measurement proposals for liabilities. The AASB concluded it should require fair value measurement for liabilities other than member liabilities, tax liabilities and liabilities arising from insurance arrangements. Consistent with its conclusions on transaction costs in relation to assets, the AASB also concluded it should require that:

(a) the carrying amount of liabilities measured at fair value not be adjusted for transaction costs; and

(b) costs attributable to issuing a liability be treated in accordance with the relevant Australian Accounting Standards.

## Presentation of financial statements

BC62 AAS 25 required a defined contribution plan, and permits a defined benefit plan, to present a statement of financial position, operating statement, and statement of cash flows. Alternatively, defined benefit plans can present a statement of net assets and a statement of changes in net assets.

BC63 In relation to ED 179 and ED 223, the AASB decided to propose that the existing AAS 25 approach should not be retained because financial statements may not be comparable between superannuation entities and the approach does not cater for (hybrid) entities that have both defined contribution members and defined benefit members.

BC64 The AASB considered the implications of superannuation entities applying AASB 101 *Presentation of Financial Statements* and decided to propose that they present:

(a) a statement of financial position, a statement of cash flows and, where relevant, a statement of changes in equity, in accordance with applicable Australian Accounting Standards;

(b) an income statement instead of a single statement of comprehensive income or a separate income statement and a statement of comprehensive income;

(c) a statement of changes in member benefits; and

(d) notes in accordance with other relevant Australian Accounting Standards except where the disclosure principles and requirements in other Australian Accounting Standards are not consistent with the measurement requirements or the disclosure principles for superannuation entities.

### Statement of financial position

BC65 The AASB noted a superannuation entity would recognise a difference between total assets and total liabilities (including members' accrued benefits and any obligations to employer-sponsors) in a number of circumstances, including when:

(a) it has an operational risk reserve; and

(b) the amount of net assets attributable to defined benefit members is greater or less than such members' accrued benefits.

BC66 The AASB noted the net assets attributable to defined benefit members would not exceed such members' accrued benefits if:

(a) the relevant trust deed terms or legislation required any surplus be applied for the benefit of members, in which case the entity would be presently obliged to such members;

(b) an employer-sponsor agreed to apply surplus assets to enhance defined benefit members' benefits in the past, and it is reasonable to assume that this practice would continue, in which case the employer-sponsor would arguably have a constructive obligation to meet the enhanced benefits; or

(c) the trustee agreed to pay surplus assets to an employer-sponsor and this meets the relevant prudential requirements, in which case the entity would be presently obliged to the employer-sponsor.

BC67 The AASB also noted that, where trust deeds or the relevant legislation is silent with respect to surplus assets, and there is no established practice, the entity would present a residual interest in the net assets as equity because the entity has no present obligation with respect to surplus assets.

BC68 Where net assets attributable to defined benefit members is less than defined benefit members' accrued benefits, the AASB noted in the Bases for Conclusions to ED 179 and ED 223, that unless there is a specific contractual arrangement between the entity and employer-sponsor, the deficit would not in itself give rise to a receivable controlled by the entity. (However, also see paragraphs BC138 to BC141.) This is because, in the absence of a contract, the payment of any future contributions by the employer-sponsor to address the deficit:

(a) would not meet the definition of a financial instrument under AASB 132 *Financial Instruments*: *Presentation*; and

(b) would not be virtually certain to be received, as required to recognise a 'reimbursement' under AASB 137 *Provisions, Contingent Liabilities and Contingent Assets*.

BC69 In relation to ED 179 and ED 223, the AASB decided, where the amount of a superannuation entity's total assets does not equal its total liabilities (including defined contribution members' vested benefits, defined benefit members' accrued benefits and any obligations to employer-sponsors), the residual is in the nature of equity in the context of Australian Accounting Standards. Accordingly, to ensure consistency with other entities, a superannuation entity should present any residual interest as equity in accordance with applicable Standards.

## Statement of changes in equity

BC70 Under AAS 25, a superannuation entity is not required to present a statement of changes in equity.

BC71 The AASB noted that, while superannuation entities have no equityholders as such, they often have equity, particularly in the form of reserves. The AASB also noted that an entity's reserving policy could have implications for the amounts credited to defined contribution members' accounts. Accordingly, ED 179 and ED 223 proposed that, when appropriate, a superannuation entity should present a statement of changes in equity in accordance with AASB 101.

## Responses to ED 179 and ED 223 proposals on statement of financial position and statement of changes in equity

BC72 Some respondents expressed concerns with presenting a difference between total assets and total liabilities in the statement of financial position. They suggested such presentation might be misleading to users where, for example:

(a) an entity has several groups of defined benefit members and the difference is attributable to only one or some of these groups;

(b) there is no specific contractual arrangement between the entity and relevant employer-sponsor(s) but it is probable the employer-sponsor(s) will make sufficient future contributions to eliminate any deficit; or

(c) there is an expectation any surplus (reserves) of the entity will be used for the future benefit of members.

BC73 The AASB noted these concerns, but concluded they are not sufficient to justify an entity not presenting a difference between assets and liabilities in its financial statements because:

(a) the extent of any surplus or deficit of net assets is useful information regarding the entity's capacity to pay defined contribution members' benefits and/or financial position (solvency) with respect to defined benefit members' entitlements;

(b) if an entity considers users of its financial statements might misunderstand the implications of any surplus or deficit, consistent with paragraph 55 of AASB 101, the entity would present additional line items by way of explanation, and/or make further note disclosures; and

(c) unless there is a present obligation at reporting date to pay reserves to a member and/or employer-sponsor, the reserve is equity in accordance with Australian Accounting Standards.

BC74 Several respondents were also concerned an entity might be permitted or required to present its liabilities for defined contribution and defined benefit members' benefits as a single line item under the ED 179 proposals. The AASB noted, because defined contribution member liabilities are different in nature and would be measured on a different basis from defined benefit member liabilities; consistent with the approach in paragraph 59 of AASB 101 and, when appropriate, the entity would present separately its liabilities for the two types of benefits.

BC75 Several respondents suggested that a statement of changes in equity would not provide sufficient useful information to users in a superannuation context to justify the cost of preparation and audit. They suggested the information that would otherwise be presented in a statement of changes in equity be included in:

(a) the statement of changes in member benefits because equity in a superannuation context is normally small (if not immaterial) and in most cases would comprise reserves that will ultimately be used for the benefit of members; or

(b) a note to the financial statements.

BC76 The AASB concluded it should require the recognition of the difference between total assets and total liabilities in the statement of financial position and require a statement of changes in equity. However, the AASB noted that there may be situations when a statement of changes in equity may not be material.

BC77 The AASB also concluded that, consistent with the sentiments in paragraphs 5 and 6 of AASB 101, superannuation entities should employ terminology that best suits their circumstances. Accordingly, superannuation entities might use a term such as 'reserve' rather than 'equity' in referring to line items or in naming statements.

## Income statement

BC78 The AASB considered whether superannuation entities should present a single statement of profit or loss and comprehensive income or a single statement of comprehensive income in accordance with AASB 101 and concluded neither would be appropriate in a superannuation context because:

(a) all remeasurement changes in assets and liabilities, other than tax items credited or charged directly to member benefits, should be recognised in an income statement in the period they occur; and

(b) 'comprehensive income' encompasses items that would not be recognised in equity in a superannuation context and, accordingly, requiring a statement of comprehensive income may be misleading.

### Income and expense items

BC79 Under AAS 25, superannuation entities recognise all income and expense items, including remeasurements of assets at net market value, in profit or loss when they occur.

BC80 The AASB considered the merits of retaining this approach and noted that defined contribution members may choose between superannuation entities based on investment returns. In addition, some employer-sponsors of entities with defined benefit members would rely on investment returns to minimise the likelihood of being required to make additional future contributions.

BC81 The AASB also noted that some Australian Accounting Standards require remeasurements of some types of assets to be debited or credited to comprehensive income. However, the AASB concluded all remeasurements, other than tax items, that are credited or charged directly to member benefits should be presented in the income statement when they occur to facilitate a clear presentation of a superannuation entity's financial performance. The AASB also noted this treatment is generally consistent with prudential reporting and to require otherwise may increase reporting costs.

## Presentation of contributions, rollovers, transfers and benefit payments

BC82 Under AAS 25, contributions, rollovers and other inwards transfers are treated as revenues, and benefits to members are treated as expenses.

BC83 The AASB decided this treatment should not be retained because:

(a) for defined contribution members, member contributions, transfers and rollovers and employer contributions fully vest in members and are payable to, or on behalf of, members upon demand (if they rollover their benefits to another superannuation entity or meet a condition of release) and therefore give rise to liabilities; and

(b) employer contributions on behalf of defined benefit members assist in funding the obligations to such members.

BC84 Accordingly, the AASB concluded these flows increase the liabilities of superannuation entities and benefit payments reduce those liabilities, and they are not in the nature of revenues and expenses.

## Net benefits allocated to defined contribution members' accounts

BC85 Under AAS 25, the difference between a defined contribution superannuation entity's revenues and expenses is presented in the operating statement as benefits accrued for members and their beneficiaries during the period.

BC86 The AASB noted this could be interpreted by some users to mean all revenues and expenses attributable to defined contribution members are allocated to their accounts and vest with them. However, this might not be the case where, for example, a trustee creates a reserve of unallocated assets. The AASB also noted:

(a) other Australian Accounting Standards that permit or require liabilities to be remeasured generally require recognition of remeasurement changes in profit or loss when they occur;[5] and

(b) it had concluded that most of a superannuation entity's assets and other liabilities should be measured at fair value, with remeasurement changes recognised in the income statement when they occur.

BC87 The AASB concluded that a superannuation entity should present the net benefits allocated to defined contribution members' accounts for a period as an allocation of operating profit or loss in the income statement for that period. This is in the interests of having information that provides users with an understanding of net benefits allocated to defined contribution members' accounts.

## Net changes in defined benefit member liabilities

BC88 Under AAS 25, a defined benefit superannuation plan that measures members' accrued benefits at the end of each period is permitted (but not required) to recognise the remeasurement change for the period as an expense in the operating statement. In contrast, an entity that does not measure those benefits at the end of each period would disclose in the notes the amounts of members' accrued benefits at the most recent measurement date and at the previous measurement date.

BC89 The AASB noted that:

(a) the AAS 25 requirements do not facilitate the provision of comparable information useful for users in a superannuation context because defined benefit superannuation entities that are similar in all significant respects could prepare their financial statements on different bases;

(b) it has concluded, in the interests of providing users with useful information on a timely basis, and consistent with the treatment of similar types of liabilities, such as insurance contract liabilities, a superannuation plan should recognise defined benefit members' accrued benefits as a liability and measure them as at the end of each period;

(c) other Australian Accounting Standards that permit or require liabilities to be remeasured generally require remeasurement changes to be recognised in profit or loss in the period they occur; and

(d) it has concluded most of a superannuation entity's assets and other liabilities should be measured at fair value, with remeasurement changes recognised in profit or loss in the period they occur.

BC90 However, the AASB also noted, unlike many other types of liabilities, defined benefit member liabilities are funded, at least in part, by contributions from members' employers and the members themselves. Consequently, the 'cost' to a superannuation entity of providing defined benefit entitlements for a reporting period is the net rather than gross change in the entity's obligations for defined benefit member liabilities for

---

5 For example, under AASB 137, changes in provisions are recognised as gains or losses in profit or loss in the period they occur.

the period. The net change is the difference between the opening and closing balances of defined benefit member liabilities for the period, after adjusting for movements of member benefits into and out of the defined benefit plan, including net after tax contributions, benefits, transfers between reserves and accrued benefits, and any gains and losses on non-routine settlements, curtailments and plan amendments. Accordingly, the AASB concluded a superannuation entity should recognise and present the net change in defined benefit member liabilities for a reporting period as a gain or loss in the income statement.

## Statement of changes in member benefits

BC91 The AASB noted that paragraph 80 of AASB 101 requires an entity without share capital to disclose information in relation to owners' interests equivalent to that required by paragraph 79(a) of AASB 101. However, the AASB concluded the presentation of member benefits in accordance with paragraph 79(a) of AASB 101 may not facilitate useful information to users in a superannuation context. For example, much of the information described in paragraph 79(a) of AASB 101 does not readily relate to a superannuation context.

BC92 Although some respondents to ED 179 and ED 223 raised concerns about the number of financial statements superannuation entities might have to prepare, given the significance of member benefits, the AASB concluded the financial statements of a superannuation entity should clearly present information that provides users with a basis for understanding changes in member liabilities. Accordingly, the AASB concluded that a statement of changes in member benefits is necessary to ensure that contributions, rollovers, transfers and benefits to members are clearly presented in a manner that enables users to evaluate their significance in relation to the entity's financial position.

## Presentation of taxation amounts

BC93 Tax is levied on superannuation entities in respect of concessional contributions received and taxable earnings.[6]

BC94 Under AAS 25, tax attributable to concessional contributions is recognised as a part of income tax expense in the period contributions are received, consistent with the treatment of contributions under AAS 25. However, consistent with contributions not being treated as revenues, ED 179 and ED 223 proposed that tax levied on concessional contributions be presented separately in the statement of changes in member benefits.

BC95 Some respondents to ED 179 and ED 223 considered that it would be more useful to present all tax amounts in one statement and, preferably, the income statement. However, other respondents acknowledged the distinction between the tax on investment income and tax on concessional contributions and the relevance of presenting them in different statements.

BC96 The AASB concluded that tax levied on concessional contributions should be presented separately in the statement of changes in member benefits because:

(a) information about tax on contributions is important for decision making by users;

(b) tax on concessional contributions is effectively paid by a superannuation entity on behalf of members and should be associated with member benefits; and

(c) recognising tax on contributions as a part of income tax expense attributable to earnings would understate the entity's operating and investment performance.

BC97 The AASB also noted that, under Interpretation 1019 *The Superannuation Contributions Surcharge*, an obligation for the surcharge gives rise to a liability and an expense of a superannuation entity. The AASB also noted that, while the surcharge specifically dealt with in Interpretation 1019 no longer applies to deductible contributions, it will continue to be paid by defined benefit members who have made surchargeable contributions or who had surchargeable contributions made on their behalf between 1996 and 2005 and the surcharge has not yet been paid. Accordingly, under Interpretation 1019, accrued interest on a surcharge amount payable is treated as an expense by the entity. In addition, a new surcharge on superannuation contributions for high income earners has recently been implemented.

BC98 The AASB considered the nature of the surcharge dealt with under Interpretation 1019 and concluded the superannuation entity is essentially acting as an agent for its members because the surcharge was determined on the basis of members' personal taxable income. The AASB also considered contribution surcharge amounts are unlikely to be material in the context of member liabilities.

6 In relation to approved deposit funds, tax is normally only levied on earnings because these entities are not permitted to receive concessional contributions.

BC99 The AASB concluded it will reconsider the status of Interpretation 1019 and whether it might need to address the surcharge on superannuation contributions for high income earners introduced in 2013, once the impact of the implementation of that surcharge is clear.[7]

## Member liabilities

### Recognition

BC100 Under AAS 25, a defined contribution superannuation plan must recognise its members' accrued benefits as a liability whereas a defined benefit superannuation plan can choose to either disclose its members' accrued benefits in a note or recognise them as a liability.

BC101 During its deliberations on ED 179 and ED 223, the AASB considered the merits of retaining these reporting requirements, particularly the requirements for defined benefit superannuation plans, and noted:

(a) the disclosure of liabilities that would otherwise be recognised in the statement of financial position is inconsistent with other Australian Accounting Standards; and

(b) liabilities could be legal (including contractual) obligations or be constructive in nature.

BC102 The AASB considered the respective legal/contractual and constructive obligations of superannuation entities and employer-sponsors and concluded that member liabilities should be recognised as liabilities of superannuation entities because:

(a) the obligation to fund a member's defined contribution entitlements falls on the member's superannuation entity and the obligation is legally enforceable; and

(b) the obligation to fund a member's defined benefit entitlements, as specified in the relevant trust deed, falls primarily on the member's plan and the obligation is contractual and/or constructive in nature.

BC103 The AASB also considered the main characteristics of superannuation members' vested and accrued benefits and noted:

(a) member contributions and benefit transfers into a superannuation entity fully vest in the member upon receipt by the entity;

(b) employer contributions on behalf of a defined contribution member fully vest with the member upon their receipt by the superannuation entity whereas employer contributions on behalf of a defined benefit member may only vest with the member progressively in line with the relevant benefit formula. Accordingly, for the vast majority of defined contribution members, the difference between defined contribution members' vested and accrued benefits is immaterial. However, for some defined benefit members, the amount of defined benefit members' vested benefits may be materially different from the amount of such members' accrued benefits; and

(c) most defined contribution members are entitled to transfer their vested benefits to another regulated superannuation entity under the Superannuation Guarantee (Administration) Act, whereas most defined benefit members are prohibited from transferring their defined benefit entitlements by the same legislation.

BC104 Accordingly, the AASB proposed in ED 179 and ED 223 that:

(a) consistent with the treatment of a financial liability with a demand feature under AASB 139, defined contribution members' vested benefits should be recognised as liabilities of superannuation entities; and

(b) consistent with the recognition of net defined benefit member liabilities of employers under AASB 119, superannuation entities should recognise defined benefit member liabilities.

BC105 Most respondents to ED 179 and ED 223 agreed with the proposal to recognise member liabilities. However, many of them disagreed with the measurement proposals (refer to paragraphs BC120 to BC123 and BC127).

#### Puttable financial instruments and obligations arising on liquidation

BC106 The AASB considered the implications of applying to superannuation entities the exception to the definition of 'financial liability' in AASB 132 to classify as equity instruments certain puttable financial instruments

7 The surcharge was introduced in the *Superannuation (Sustaining the Superannuation Contribution Concession) Imposition Act 2013*.

and certain instruments that impose on an entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation of the entity.[8]

BC107 The AASB noted that applying the puttable instruments exception could give rise to inconsistent reporting outcomes – for example:

(a) defined contribution members' entitlements held by an entity with only defined contribution members might meet the criteria necessary to be classified as equity; and

(b) defined contribution members' entitlements held by a hybrid plan and defined benefit members' entitlements would not generally meet the criteria necessary to be classified as equity.

BC108 The AASB considered that having different reporting outcomes depending upon the impact of the puttable instruments requirements would be inconsistent with principles-based standard-setting and would diminish the comparability and usefulness of the financial statements of superannuation entities. Both ED 179 and ED 223 identified the issue with puttable instruments in a superannuation entity context. The consensus from those commenting on the matter is that it would not be useful to show some or all member benefits as equity of a superannuation entity. Accordingly, the AASB concluded that the puttable instruments exception should not apply to superannuation entities.

## Measurement

### Defined contribution members' vested benefits

BC109 In both ED 179 and ED 223, the AASB identified defined contribution members' vested benefits as representing the amount that would be payable on demand:

(a) upon the member's retirement, death, disablement or other event that qualifies as a condition for releasing their superannuation benefits; or

(b) to another regulated superannuation entity under the Superannuation Guarantee (Administration) Act.

BC110 The AASB noted the net assets attributable to defined contribution members would include items that it proposes be measured at amounts other than their fair values, such as tax liabilities and tax assets. However, the AASB concluded that, as most assets and liabilities attributable to defined contribution members would be measured at their fair values, the difference between defined contribution members' vested benefits measured entirely at fair value or in accordance with AASB 119 would in most cases not be expected to be material.

BC111 Some respondents to ED 179 and ED 223 commented that the expression 'amount payable on demand' is inappropriate because it might imply that members could immediately access their benefits without meeting a condition of release. Some respondents also queried why 'vested benefits' should be specified for defined contribution member liabilities, yet 'accrued benefits' is specified for defined benefit member liabilities.

BC112 The AASB concluded that it could achieve its intended outcome with modified wording and decided to refer to defined contribution member liabilities being measured at the amount of account balances at the reporting date. The AASB also concluded that it should specify the measurement of 'accrued benefits' of defined contribution members to be consistent with the requirements in other Australian Accounting Standards and to be internally consistent in respect of both defined contribution member liabilities and defined benefit member liabilities.

### Defined benefit members' accrued benefits

BC113 In developing ED 179 and ED 223, the AASB considered a number of bases for measuring defined benefit member liabilities, including:

(a) at fair value consistent with the IASB Discussion Paper proposals that have now led to AASB 13;

(b) at current exit value consistent with a model in the IASB's Discussion Paper *Preliminary Views on Insurance Contracts*;[9]

(c) at present value of the expected future benefit payments consistent with the requirements of AAS 25; and

8 AASB 2008-2 *Amendments to Australian Accounting Standards – Puttable Financial Instruments and Obligations arising on Liquidation* amended AASB 132 in February 2008.

9 Issued in May 2007.

(d) at present value of the expected future benefit payments consistent with AASB 119 for defined benefit member liabilities.

BC114 With respect to paragraphs BC113(a) and BC113(b), the AASB noted:

(a) a fair value or current exit value could potentially:

(i) provide useful information to users, particularly in relation to the amount, timing and uncertainty of future benefit payments; and

(ii) facilitate consistency of reporting (with most assets being measured at fair value);

(b) defined benefit member liabilities are not traded as stand-alone items and are generally extinguished in the normal course of business. While the absence of an active market for defined benefit member liabilities does not preclude such fair value measurement, the issues that would need to be addressed to achieve consistency across superannuation entities would be potentially insurmountable. The issues include estimating risk margins, service margins and costs of capital, and putting a price on the 'moral hazard' implications of one or more (third party) employer-sponsors deciding on employees' salary adjustments; and

(c) fair value or current exit value would be inconsistent with:

(i) achieving closer alignment between the treatment of defined benefit member liabilities recognised by employer-sponsors and superannuation entities;

(ii) thinking included in the IASB Exposure Draft of proposed amendments to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and IAS 19 *Employee Benefits*,[10] that the amount an entity would rationally pay to extinguish a liability is the lower of its settlement or transfer amounts; and

(iii) the reasoning behind the proposals to apply a 'fulfilment approach' in the AASB's ED 244 *Insurance Contracts*, which incorporates the IASB's ED/2013/7 *Insurance Contracts*.[11]

BC115 Due to the relative weight of argument, the AASB concluded against proposing that defined benefit members' accrued benefits be measured at fair value or current exit value.

BC116 In relation to paragraph BC113(c), the AASB noted that, while the requirements in AAS 25 for measuring defined benefit members' accrued benefits are conceptually consistent with the requirements in AASB 119 for measuring defined benefit member liabilities, AAS 25 is arguably more permissive. For example, AAS 25:

(a) does not specify the actuarial valuation method required to measure defined benefit members' accrued benefits;

(b) provides little or no guidance in relation to assumptions used in measuring defined benefit member liabilities; and

(c) requires a superannuation plan to measure its defined benefit members' accrued benefits as frequently as required for statutory purposes, which might not be annually.

BC117 The AASB also noted AAS 25 required a superannuation plan to discount defined benefit members' accrued benefits at the rate of return the plan anticipates it could achieve if, at the measurement date, sufficient funds were available to meet members' accrued benefits as they fall due. The AASB considered the merits of this approach and rejected it because the discount rate might be affected by the actual types of assets held by a plan and AAS 25 does not establish a sufficient link between that rate and the nature or amounts of the plan's liabilities. The AASB was particularly concerned that, under AAS 25, a plan could potentially recognise a smaller amount for its defined benefit member liabilities than it would otherwise by holding riskier assets with potentially higher expected rates of return.

BC118 In relation to paragraph BC113(d), the AASB decided that, to achieve greater consistency across superannuation entities, and to facilitate consistency with the measurement of defined benefit and other liabilities by other entities, the approach in AASB 119 should be proposed in ED 179, on the following basis:

(a) use actuarial techniques and assumptions to make a reliable estimate of expected future cash flows;

(b) determine the present value of liabilities using the projected unit credit method;

(c) be permitted to apply estimates, averages and computational shortcuts for determining its liabilities; and

10 Issued in June 2005.
11 Issued in June 2013.

(d) measure liabilities at the end of each reporting period to help ensure users have useful information on a timely basis.

BC119 However, the AASB also decided some of the AASB 119 measurement requirements in respect of defined benefit member liabilities may need to be modified for application in a superannuation entity context. In particular, the AASB decided ED 179 should propose that:

(a) expected administration costs not be included because, although they may be regarded as a component of the ultimate cost of an employer in meeting defined benefit member liabilities, they do not constitute a part of members' accrued benefits;

(b) if a superannuation plan's benefit formula prescribes that members accrue materially higher levels of benefits as they near retirement age, rather than attribute benefits to reporting periods on a straight-line basis, the superannuation entity would attribute member benefits to reporting periods on a basis appropriate to its circumstances;[12]

(c) consistent with the *Framework*, a superannuation entity would consider its assumptions to be unbiased if they are not imprudent or conservative (AASB 119 states actuarial assumptions are unbiased if they are neither imprudent nor excessively conservative); and

(d) expected future benefit payments be discounted for the time value of money using a risk-free discount rate based on current observable, objective rates that relate to the nature, structure and terms of the obligations for future benefit payments. The AASB decided the AASB 119 requirement to determine discount rates by reference to market yields on high quality corporate bonds, or by applying yields on government bonds, is not relevant in a superannuation entity context.

BC120 Many respondents to ED 179 disagreed with the measurement proposals for defined benefit members' accrued benefits. The reasons they cited include the following.

(a) Superannuation plans must currently calculate at least two, and potentially three, different liability measures:

(i) vested benefits on a quarterly basis for prudential reporting, and sometimes more frequently for trustee monitoring and reporting to employer-sponsors;

(ii) accrued benefits (discounted at the entity's estimated earnings rate) at least every three years for funding purposes and to meet prudential and legislative requirements; and

(iii) accrued benefits are potentially required to be calculated every year for the purpose of financial reporting by employer-sponsors under AASB 119.

Accordingly, requiring another liability measure would not be justified on cost-benefit grounds.

(b) The amount of defined benefit members' accrued benefits measured under ED 179 would be likely to differ from the amount for the same members measured under AASB 119, which could give rise to confusion among users.

(c) The amount of defined benefit members' accrued benefits measured under ED 179 would be likely to be greater than the amount for the same members measured for the actuarial review because the entity's estimated earnings rate will generally be used to discount future benefits for the purpose of the actuarial review and will generally be greater than a risk-free rate. Accordingly, deficits would be more likely to be reported under ED 179. As employer-sponsors are generally disinclined to make contributions above those needed for funding purposes, members may incorrectly conclude their entitlements are at risk.

BC121 Some respondents to ED 179 preferred that defined benefit member liabilities be measured at the amount of vested benefits for a number of reasons, including:

(a) the amount of vested benefits is easier and less costly to calculate than accrued benefits;

(b) users, particularly members, are more familiar with the concept of vested benefits (as it is reported in individual benefit statements). Also, users arguably have relatively less understanding of accrued benefits and what they mean in the context of a superannuation entity's financial position;

12 When a benefit formula prescribes that members accrue materially higher levels of benefits as they near retirement age, the allocation of service cost to reporting periods in accordance with the benefit formula would not provide a reliable measure of the employer's periodic cost of providing such benefits to employees, particularly in the earlier years of service. Accordingly, in such circumstances, AASB 119 requires employers to attribute defined benefits to reporting periods on a straight-line basis to more closely reflect the periodic cost of providing such benefits to employees. Unlike employers, superannuation entities do not receive services from members in exchange for entitlements and it would be more relevant for a plan to attribute member benefits to reporting periods on a basis appropriate to the plan's particular circumstances, taking into account the formal terms of the plan and any constructive obligations that go beyond the formal terms of the plan.

(c) the amount of accrued benefits is relevant to an employer-sponsor that promises a future benefit, but arguably less relevant if a plan limits its legal obligation to members to the amount of its assets net of any obligations other than member liabilities;

(d) vested benefits can be a reasonable proxy for accrued benefits, particularly when members are close to expected retirement age; and

(e) measuring defined benefit member liabilities as vested benefits would be consistent with the proposed measurement of defined contribution member liabilities.

BC122 Other respondents to ED 179 expressed a preference for defined benefit member liabilities being measured in accordance with the approach in AASB 119 for defined benefit member liabilities, noting that such an approach:

(a) would facilitate greater consistency between employer-sponsor and superannuation entity financial statements;

(b) would not impose significant additional preparation and audit costs on superannuation entities; and

(c) would be likely to yield a figure that is similar to the amount that would be calculated under ED 179 because:

(i) expected administration costs are generally not material and not normally included in calculating defined benefit member liabilities under AASB 119;

(ii) Superannuation Guarantee minimum benefits have meant few entities provide defined benefit entitlements that accrue materially higher levels of benefits as members approach retirement age; and

(iii) most defined benefit member liabilities for employers are discounted using a rate determined on the basis of government bond yields, which would generally be consistent with a risk-free rate.

BC123 However, the AASB noted the following drawbacks of requiring superannuation entities to measure defined benefit member liabilities as vested benefits or in accordance with the approach in AASB 119.

(a) A vested benefits approach is inconsistent with the going concern concept because it is somewhat akin to a liquidation value and therefore not consistent with the long-term nature of defined benefit member liabilities and the approaches required under Australian Accounting Standards for measuring similar liabilities, such as insurance contract liabilities.

(b) A superannuation plan with an employer-sponsor that applies AASB 119 may still incur additional preparation and audit costs in applying the approach in AASB 119 for defined benefit member liabilities where:

(i) the employer-sponsor's reporting date is different from the superannuation entity's reporting date; or

(ii) there is a multi-employer plan and the criteria in AASB 119 are met that enable the employer-sponsor to account for the plan as if it were a defined contribution plan.

BC124 The AASB also considered that measuring defined benefit member liabilities in accordance with the approach in AASB 119 for defined benefit member liabilities within the APRA reporting timeframe (within four months of period end) may pose challenges for some superannuation entities. However, the AASB decided not to provide special guidance on materiality in respect of measuring defined benefit member liabilities to facilitate plans meeting reporting deadlines because it would arguably need to be rules-based, which is contrary to the AASB's general approach.

BC125 The AASB noted AASB 119 permits the use of particular estimates, averages or computational shortcuts in measuring defined benefit member liabilities in some cases. Accordingly, an entity would be permitted to use those shortcuts that it considers appropriate (including, but not limited to, the shortcut techniques used by employer-sponsors of defined benefit members under AASB 119), provided that the amount calculated using the shortcut techniques is not materially different from the amount that would otherwise have been determined using the comprehensive approach.

BC126 In light of the comments and recommendations of respondents, the AASB decided that, on cost-benefit grounds, ED 223 should propose that a superannuation plan be required to measure its defined benefit member liabilities in accordance with the approach in AASB 119 (without modification) for defined benefit member liabilities.

BC127 In relation to ED 223, respondents reiterated many of the points made above in relation to the ED 179 proposals. In particular, many regard the requirements in AASB 119 in respect of defined benefit member liabilities to be flawed and could identify costs of applying the AASB 119 model in a superannuation entity context and few benefits. In response, the AASB conducted further targeted outreach on the cost and timeliness of implementing a principle similar to the requirements in AAS 25, but with more direction on its implementation designed to overcome the short-comings of the AAS 25 requirement.

BC128 After noting that there is not a consistent approach across the various Australian Accounting Standards to measuring different types of liabilities and having regard to the nature of defined benefit member liabilities and the regulatory environment in which superannuation entities operate, the AASB concluded it should identify a measurement principle for defined benefit member liabilities. That principle is to measure defined benefit member liabilities as the amount of a portfolio of investments that would be needed as at the reporting date to yield future net cash inflows that would be sufficient to meet accrued benefits at that date when they are expected to fall due.

BC129 The AASB noted this principle is consistent with the notion that the superannuation entity needs to fund the liability, taking into account the timing and probabilities attaching to various factors that reflect the characteristics of the members/beneficiaries. Those characteristics include expected mortality; rates of member turnover, disability, and early retirement; salaries and rates of salary adjustment; member choices of available options, such as lump sum or pension options; and any other risks specific to the liability. The AASB further concluded that it would require:

(a) expected cash flows to be discounted by a rate that reflects the expected notional returns, including fair value changes, on a portfolio of investments that is judged by the trustees to be the optimal way to generate the net cash inflows needed to meet benefit payments, based on a realistic assessment of the relative risks and returns on those assets;

(b) the relevant portfolio of investments might not be the same as the existing portfolio of investments, for example, because the existing investments are currently in different asset classes, or the defined benefit member liability is under-funded/unfunded; and

(c) to the extent the relevant portfolio of investments is not the same as the existing portfolio of investments, it would need to be based on investment opportunities that are realistically available to the entity.

BC130 The AASB acknowledged that, in applying the above measurement principle and the concept of materiality, there would often be approaches to measuring defined benefit member liabilities that could be employed which do not involve undertaking a comprehensive actuarial assessment. For example, the AASB noted that vested benefit calculations, including an assessment of the relationship between vested benefits and accrued benefits and the stability of that relationship, are the basis for some of the approaches that might be used in practice to measure defined benefit member liabilities for financial reporting purposes. However, the AASB noted that, because of the varied circumstances facing different plans, it would be inappropriate to identify particular approaches as being those that would apply in any particular cases.

BC131 The AASB discussed an alternative view that a risk-free rate representing only the time value of money should be applied to present value expected cash outflows. The AASB noted that, although arguably facilitating comparability among entities, this would tend to result in overstated defined benefit member liabilities and give rise to up-front deficits that would later reverse.

## ‘Higher of’ benefit options

BC132 During its deliberations on measuring member liabilities, the AASB noted the issues regarding a ‘higher of’ benefit that arises in a case where members are entitled to the higher of a defined benefit entitlement and a contributions-based amount.

BC133 In its Discussion Paper *Preliminary Views on Amendments to IAS 19 Employee Benefits*, the IASB proposed that an employer-sponsor account for a higher of benefit option in a manner consistent with an embedded option under IAS 39 *Financial Instruments*: *Recognition and Measurement* such that an employer-sponsor would:

(a) recognise and account for the host defined benefit promise in the same way as a defined benefit member liability under IAS 19; and

(b) account for the higher of benefit option separately, measured at its fair value assuming the terms of the benefit promise will not change.

BC134 The AASB concluded ED 179 should seek input from constituents on accounting for a higher of benefit option separately from member liabilities, and how the benefit option might be measured (prior to making any proposals on the matter), since the IASB’s proposals were at an early stage of development and had been specifically developed for application by employer-sponsors.

BC135 Respondents to ED 179 confirmed that higher of benefit options are presently measured at their ‘intrinsic values’ as:

(a) the difference between the defined benefit members' accrued benefits and their account balances when account balances are greater than accrued benefits; and

(b) at nil when account balances are less than accrued benefits.

BC136 In addition, most of the respondents to ED 179 disagreed with the IASB's proposed approach because:

(a) there are no compelling reasons to depart from current practice under AAS 25 and AASB 119, which ensures accrued benefits are measured on the basis of future benefit payments that members are likely to receive;

(b) in the Australian context, some higher of benefit options can change depending upon various factors, including investment returns, salary increases, and members' ages and service periods, and a reliable measurement is not feasible; and

(c) using an option valuation technique is not justified on cost-benefit grounds, particularly since the separate recognition of a higher of benefit option could potentially confuse some users.

BC137 Based on the feedback received on ED 179 and the lack of progress at the IASB on its post-employment benefits work, the AASB concluded that neither ED 223 nor AASB 1056 should address higher of benefit options.

## Employer-sponsor receivables

BC138 Neither ED 179 nor ED 223 included explicit recognition or measurement proposals about receivables from an employer-sponsor where there is a net difference between the assets and liabilities of a defined benefit plan. Both exposure drafts proposed disclosure of the main features of any specific contractual arrangement in place between the trustee and the relevant employer-sponsor in relation to funding a 'deficit'. Both also mentioned in their Bases for Conclusions that, unless there is a specific contractual arrangement between the entity and employer-sponsor, the deficit would not in itself give rise to a receivable controlled by the entity.

BC139 Respondents to ED 179 and ED 223 confirmed the AASB's thinking that specific contractual arrangements between the entity and employer-sponsor are rarely, if ever, encountered. However, the AASB's targeted outreach with public sector superannuation entities revealed that legislative guarantees of funding are relatively common in that sector. In addition, some respondents sought guidance on the circumstances in which a plan would recognise contributions receivable in respect of defined benefit members for which there is a deficit of net assets.

BC140 The AASB concluded that AASB 1056 should include a requirement to recognise a receivable from an employer-sponsor to the extent that it meets the definition and recognition criteria for an asset in the *Framework*.

BC141 The AASB considered the various approaches that could be taken to measuring such a receivable and concluded that it should be measured on a basis consistent with the measurement principle for the underlying defined benefit member liability less the fair value of any assets held by the entity to meet that liability, which is effectively the 'intrinsic value' of the asset. The AASB concluded that any other measurement principle for an employer-sponsor receivable in respect of defined benefit member liabilities would be likely to involve taking into account employer-sponsor credit risk, which would not be appropriate for the reasons identified in paragraph BC194(d) in relation to risk disclosure proposals.

BC142 A number of constituents commenting on the Draft AASB 105X for fatal-flaw review sought to know why there would be no requirements in relation to whether entities should accrue for contributions receivable from employers for payroll of the reporting period. The AASB noted that this type of accrual is the subject of other Australian Accounting Standards and the general conventions underpinning accounting, and should not be specifically addressed in AASB 1056.

## Tax liabilities and tax assets

BC143 Under AAS 25, the recognition and measurement requirements of AASB 112 apply in determining income tax expense.

BC144 The AASB considered the merits of requiring superannuation entities to measure tax liabilities and tax assets at fair value, which would imply a need for discounting in some circumstances, thereby requiring such entities to depart from AASB 112. The AASB noted:

(a) AASB 112 prohibits discounting deferred tax assets and liabilities to their present values on the basis that the detailed scheduling necessary to undertake that discounting is usually impracticable or highly complex;

(b) a significant proportion of many superannuation entity tax balances are attributable to unrealised gains and losses on assets held to fund member benefits and measuring those assets at fair value helps ensure that any associated tax balances determined under AASB 112 would be recognised at amounts approximating fair value;[13] and

(c) most of the 'transaction costs' associated with tax balances relate to measuring the assets held to fund member benefits and maintaining adequate records for tax purposes, and the transaction costs directly attributable to extinguishing or settling a tax liability or tax asset are immaterial.

BC145 ED 179 and ED 223 proposed that superannuation entities should measure tax balances in accordance with AASB 112 because:

(a) users' needs do not appear to justify a departure from AASB 112 as the difference between a tax balance measured at fair value or in accordance with AASB 112 would, in most cases, be immaterial; and

(b) the benefits to users from fair valuing deferred tax assets and liabilities are unlikely to be outweighed by the costs incurred in determining their fair values.

BC146 The majority of the respondents to ED 179 and ED 223 that specifically commented on the recognition and measurement proposals for tax liabilities and tax assets generally agreed with the proposals. Accordingly, the AASB concluded that superannuation entities should be required to measure tax balances in accordance with AASB 112.

## Liabilities and assets arising from insurance contracts

BC147 During its deliberations on the proposals in ED 179, the AASB noted many superannuation entities offer life and disability insurance cover to their members and some also offer income protection insurance, and that AAS 25 is silent about how to account for such arrangements. The AASB also noted the forms of these insurance arrangements differ across entities, including those where cover is:

(a) offered to members, with the entity only acting as agent;

(b) offered to members with the entity accepting insurance risk; and

(c) provided to defined benefit members in relation to their projected retirement benefit.

BC148 The AASB noted that, in the case of (a), a superannuation entity is unlikely to be exposed to significant insurance risk as members or their beneficiaries would not generally have recourse to the assets of the plan, even in the event the insurer fails. In other circumstances the entity may have significant insurance risk, even if it reinsures 100% of the risk with a third-party (re)insurer. The AASB noted that, under the insurance standards, reinsurance does not nullify the direct contract with the policyholder.

BC149 The AASB considered a number of approaches to accounting for insurance arrangements that involve a superannuation entity having significant insurance risk, including applying AASB 137, AASB 4 *Insurance Contracts*, AASB 1023 and AASB 1038.

BC150 The AASB considered that many of the insurance contracts entered into by superannuation entities would meet the 'insurance contract' definition. The AASB decided ED 179 should propose that superannuation entities account for any liabilities and assets arising from the insurance arrangements they provide to their members by applying the recognition, measurement and disclosure requirements of AASB 1038 on the basis that:

(a) insurance arrangements provided to superannuation members generally have the same characteristics as life insurance contracts and would meet the 'life insurance contract' definition were it not for the fact that it is confined to contracts regulated under the *Life Insurance Act 1995*;

(b) AASB 1038 has comprehensive requirements;

(c) AASB 4 does not include initial liability recognition requirements or comprehensive measurement requirements;

(d) the liability recognition and measurement requirements of AASB 1023 are based on a premium deferral model, which would not suit the circumstances of superannuation entities that would generally not receive significant premiums in advance that could be deferred; and

(e) AASB 137 applies only to liability recognition and measurement.

13 For example, if a superannuation entity sold an asset for its carrying amount at the end of the period, and that amount is above its tax base, the tax liability measured in accordance with AASB 112 would generally be materially the same as the present value of tax the entity would have to pay in relation to the asset.

BC151 The AASB noted that applying AASB 1038 would potentially change the way in which many superannuation entities account for insurance arrangements and, where the insurance arrangements give rise to obligations, entities would be required to recognise:

(a) insurance contract premiums and claim recoveries as income;

(b) insurance contract claims and premiums ceded to reinsurers as expenses;

(c) claim recoveries and other inflows not yet received from reinsurers as assets; and

(d) insurance contract liabilities.

BC152 In response to ED 179, a number of respondents acknowledged that a superannuation entity that:

(a) 'self-insures' members' benefits (that is, does not reinsure all of the members' insurance benefits with a third-party insurer);

(b) pays discretionary insurance benefits in addition to the benefits provided by a third-party insurer; or

(c) is liable for insurance claims under its trust deeds that are not met by a third-party insurer;

is potentially exposed to insurance risk and therefore should arguably provide information regarding these risks.

BC153 However, nearly all of those commenting on the proposed application of AASB 1038 expressed concerns, including:

(a) applying the recognition and measurement principles and requirements in AASB 1038 would be difficult because:

  (i) contributions in respect of self-insured defined benefit members do not include explicit insurance premium components and, while a plan's actuary would normally estimate that component for tax purposes, that may not meet the relevant requirements;

  (ii) for some plans, a member's resignation benefits and death and/or disability benefits are linked and would be included as part of the defined benefit member liability, with the death and/or disability component not being separately calculated; and

  (iii) the amount of any self-insured defined death and/or disability benefit may not be readily identifiable where the benefit is not defined in terms of an accrued (retirement) amount plus an insured component;

(b) the proposals are not justified on cost-benefit grounds, because:

  (i) applying AASB 1038 would impose significant additional costs, including the cost of systems for capturing the necessary information; and

  (ii) insurance risks are generally not significant in the context of a superannuation entity's operations as a whole because few superannuation entities are self-insured; the provision of insurance arrangements is only an ancillary benefit offered to members; and most plans reinsure all of the relevant risks with third party (re)insurers; and

(c) the potential implications of the changes to AASB 1038 that would result from the IASB's comprehensive insurance contracts project in the next few years.

BC154 Respondents to ED 179 also identified a number of alternative approaches the AASB could adopt, including:

(a) only addressing accounting for insurance arrangements in a superannuation context once the IASB's comprehensive insurance contracts project is completed;

(b) a disclosure-only approach, for example, requiring disclosure of the insurance arrangements provided, the risk exposures and any reserves established in respect of such exposures; or

(c) requiring any liabilities or assets arising from insurance arrangements to be accounted for in a manner consistent with the basis adopted for measuring member liabilities.

BC155 In redeliberating the proposals in ED 179, the AASB noted that, in many cases, superannuation entities act only as agents in respect of the insurance arrangements they have for members and would not be affected by requirements to account for insurance contracts. However, whilst insurance risks may not be significant for many superannuation entities, the AASB noted that some may be exposed to significant insurance risk. For example, (re)insuring member liabilities with a third-party (re)insurer may not mitigate the insurance risks to which a plan is exposed because:

(a) the superannuation entity remains exposed to credit and other performance risk of the (re)insurer, including the possibility a reinsurer declines a claim but the entity remains obliged to meet the benefit;

(b) the excesses and/or deductibles under a group policy might leave the entity exposed to some or all members' insurance claims; and/or

(c) the (re)insurer is in 'run off' and unwilling or unable to pay claims.

BC156 The AASB also noted that self-insured arrangements may expose an entity to non-performance risk and/or economic dependency risk in relation to the employer-sponsor, particularly when there exists a deficit in a defined benefit plan.

BC157 The AASB concluded that it should reconsider the accounting for the insurance arrangements once the IASB's comprehensive insurance contracts project is completed, but that this should not be a barrier to addressing the matter now. In its response to the IASB's ED/2010/8 *Insurance Contracts,* the AASB recommended that the IASB consider the implications of the findings on insurance contracts as a part of its proposed comprehensive review of the accounting for post-employment benefits.

BC158 The AASB concluded a 'disclosure only' approach is not adequate because it would mean assets and liabilities would remain unrecognised.

BC159 The AASB considers the main risks to which most superannuation entities are exposed in relation to insured benefits are credit and operational risks of the (re)insurer, and risks associated with the plan administering policies (such as the risk of higher than expected claims administration expenses).

BC160 The AASB also noted that:

(a) insurance contract liabilities in respect of defined benefit members are measured as part of members' accrued benefits under AAS 25;

(b) for the purpose of recognising a net defined benefit member liability under AASB 119, the level of aggregation (unit of account) is the cohort of employees with defined benefit entitlements and any insurance contract liabilities are calculated as a part of the 'best estimate' cash flows, which contrasts with AASB 1038, which is designed to cater for life insurers and incorporates the notions of experience adjustments as well as adjusting planned margins for the impacts of changes to assumptions;

(c) insurance contract liabilities in respect of defined benefit members are likely to be measured at a similar amount under the accumulation approach in AASB 1038 as they would be under the approach in AASB 119 for defined benefit member liabilities;

(d) under AASB 119, no distinction is made between retirement benefits and insurance benefits in respect of the measurement or presentation of defined benefit member liabilities; and

(e) an entity could use estimates, averages or computational shortcuts permitted in AASB 119 in measuring its defined benefit member liabilities, such as a cash premiums basis to measure the insurance component of its liability to defined benefit members, or its liabilities arising from insurance arrangements provided to defined contribution members, if the outcomes are not materially different from those that would otherwise be achieved using an expected present value basis.

BC161 Accordingly, the AASB decided ED 223 should propose that insurance obligations to members be:

(a) recognised (and derecognised) using the AASB 119 approach for defined benefit member liabilities;

(b) for defined benefit members, measured as part of accrued benefits using the measurement approach in AASB 119 for defined benefit member liabilities;

(c) for defined contribution members, measured using the approach in AASB 119 for defined benefit member liabilities, to facilitate consistency with the requirements for defined benefit member liabilities;

(d) presented separately from any liabilities for defined contribution members' vested benefits (when material) – separate presentation should not be required in relation to defined benefit members' accrued benefits, consistent with the approach in AASB 119; and

(e) any reinsurance assets should be recognised in accordance with AASB 1038.

BC162 The AASB also decided ED 223 should propose that information should be disclosed that explains and provides users with a basis for understanding the amount, timing and uncertainty of future cash flows arising from insurance obligations to members.

BC163 In response to ED 223, a number of respondents made the following points:

(a) it is clear those superannuation entities that ‘self-insure’ should be accounting for any insurance assets and liabilities, and that AASB 119 is a reasonable basis for recognising and measuring the liabilities – it was noted that such self-insurance is becoming less prevalent;

(b) some superannuation entities clearly state that members will only receive insurance benefits if the insurer/reinsurer pays. Accordingly, although superannuation entities may control cash and accrue receivables and payables arising from their insurance arrangements, they are not taking on insurance risk;

(c) those superannuation entities offering group insurance cover that members can elect to have would reinsure those risks with a registered insurer. In many of these arrangements it may not be entirely clear whether the superannuation entities are taking on insurance risk that should cause them to account for insurance assets and liabilities;

(d) in most cases, the insurance offered to defined contribution members can be re-priced at short notice. That is, the premiums charged to member accounts can be adjusted as the insurance costs faced by the superannuation entities change (for example, as the reinsurance premiums change). Accordingly, in such cases, any insurance contracts that might exist between the superannuation entities and their members are short in duration and the associated insurance assets and liabilities might be immaterial;

(e) superannuation entities occasionally make ex gratia payments in respect of death and disability claims where the trustees judge that a benefit should be paid even though it is not covered by reinsurance, but they would not be material;

(f) referring to both AASB 119 and AASB 1038 in relation to insurance is potentially confusing, particularly to those who are not familiar with accounting for insurance contract liabilities; and

(g) further guidance should be provided on when superannuation entities would be considered to be acting as agents.

BC164 The AASB concluded it should include the requirements relating to reinsurance assets from AASB 1038 in the replacement standard, rather than referencing to AASB 1038; particularly in view of the fact that AASB 1038 will be replaced at some stage.

BC165 The AASB also concluded it should proceed with the other recognition and measurement requirements consistent with the proposals in ED 223, but noted that it had concluded on an approach to measuring defined benefit member liabilities, and therefore insurance liabilities, that is different from ED 223. The AASB also concluded that further guidance should be provided on:

(a) factors that are indicative of a superannuation entity acting as an agent in respect of the insurance cover provided to members (or their beneficiaries); and

(b) factors that are indicative of a superannuation entity acting as an insurer.

BC166 The AASB noted that, in the case of superannuation entities acting as agents in relation to insurance arrangements provided to members, whilst these arrangements do not give rise to revenues and expenses of the entity, amounts from members account balances are typically applied to pay insurance premiums and some claims may be received via member accounts. (Many claims would be received directly by members/beneficiaries and would not appear in a superannuation entity’s financial statements.) The AASB concluded that, in respect of the premium amounts and any claim amounts that flow through the superannuation entity, it provides useful information about insurance arrangements a superannuation entity provides as an agent for the statement of cash flows and statement of changes in member benefits to reflect those amounts.

BC167 In arriving at the above conclusions, the AASB was aware of the relatively new regulation designed to phase out so-called ‘self-insurance’ through prudential regulation. Nevertheless, the AASB concluded that the requirements relating to recognising assets, liabilities, revenues and expenses in relation to insurance arrangements might still apply. This is because a superannuation entity that has insurance policies with registered insurers that ‘fully support’ insurance cover provided to members may still leave the superannuation entity acting in the capacity of an insurer (albeit one with reinsurance cover).

## Consolidated and separate financial statements

### Consolidated financial statements

BC168 At the time of preparing both ED 179 and ED 223, the AASB noted there is an expectation that under AASB 127 *Consolidated and Separate Financial Statements* and AASB 10 *Consolidated Financial Statements*,[14] superannuation entities would generally be required to prepare consolidated financial statements. Following the developments explained below, the IASB (and ultimately the AASB) changed the landscape for consolidation when it decided to apply a different approach to 'investment entities' that, generally, would not require consolidation.

BC169 The AASB deliberated at length on the manner in which superannuation entities should prepare consolidated financial statements. Those deliberations were conducted prior to the issue of AASB 2013-5 *Amendments to Australian Accounting Standards – Investment Entities*. They included considering feedback on an AASB Consultation Paper *Consolidation of Subsidiaries by Superannuation Entities* (September 2007) and the consolidation proposals in ED 179 and ED 223. During that process, the AASB considered a number of different ways in which a parent superannuation entity could treat a subsidiary in its consolidated financial statements, including:

(a) on a full fair value basis that involves all assets and liabilities, whether recognised or unrecognised in the separate financial statements of the parent or a subsidiary, being measured at fair values;

(b) on a basis that involves all assets and liabilities recognised by a subsidiary being measured at fair values when fair value is required or permitted under the relevant Australian Accounting Standards;[15]

(c) as per (b) above with the addition, when applicable, of a balancing item in relation to subsidiaries.[16] That balancing item would comprise:

  (i) acquired goodwill remaining at period end;

  (ii) changes in internally generated goodwill associated with subsidiaries subsequent to their acquisition; and

  (iii) measurement differences resulting from subsidiaries' assets and liabilities being recognised in consolidated financial statements at amounts other than their fair values adjusted for transaction costs;

(d) in accordance with AASB 3 and AASB 127,[17] under which a subsidiary's identifiable assets and liabilities are recognised in the consolidated financial statements at their fair values at the subsidiary's date of acquisition, and subsequent to acquisition, a subsidiary's assets and liabilities are recognised in accordance with relevant Australian Accounting Standards, which treat the fair values of assets or liabilities acquired in business combinations as 'cost' for the purposes of subsequent accounting;

(e) a proportionate consolidation model that ensures the net asset amounts reported in the parent's separate and consolidated financial statements are the same; and

(f) recognition of net investments in subsidiaries as a single line item with detailed note disclosure.

BC170 In relation to ED 179, the AASB decided that a parent superannuation entity would be best served by recognising in its consolidated statement of financial position all assets and liabilities of a subsidiary, whether recognised or unrecognised in the statement of financial position of the subsidiary.

BC171 In light of the comments received on ED 179 from respondents the AASB decided, consistent with ED 179, that ED 223 should propose that a parent superannuation entity present consolidated financial statements. However, in contrast to ED 179, the consolidated financial statements would be prepared in accordance with AASB 3 and AASB 10, including in relation to accounting for acquired goodwill. Superannuation entities would also be required to apply the fair value option to measuring non-controlling interests at inception, without subsequent remeasurement, in accordance with AASB 3.

BC172 Consistent with ED 179, under ED 223 it was proposed to require remeasuring acquired intangible assets at fair value at each reporting date in the consolidated financial statements; whether or not they had been acquired in a business combination. The AASB noted that this would be a departure from AASB 3 and AASB 138 *Intangible Assets* when there are not active markets for the intangible assets concerned.

14 AASB 10 superseded AASB 127 for periods beginning on or after 1 January 2013.
15 Consistent with the approach currently applied under AASB 1023 and AASB 1038.
16 Similar to the approach in the now superseded AASB 1038 *Life Insurance Business* (1998).
17 AASB 10 had not yet been issued.

BC173 At the time of preparing ED 223, the AASB also noted the proposals in IASB ED/2011/4 *Investment Entities*[18] to account for most subsidiaries at fair value through profit or loss might address some of the concerns raised by constituents. However, the AASB decided that it would be premature for the AASB to propose in ED 223 permitting or requiring parent superannuation entities to apply investment entity accounting before there is an outcome from the IASB's project.

### Responses to the ED 179 and ED 223 consolidation proposals

BC174 Overall, respondents expressed mixed views on the proposals in ED 179 and ED 223 that a parent superannuation entity present consolidated financial statements. Many of them identified practical difficulties, including:

(a) identifying entities controlled and the times when control arises or is lost;

(b) monitoring changes in holdings in collective investment entities, particularly when there is a high turnover of ownership interests in the investee;

(c) obtaining relevant, reliable and timely information to prepare consolidated financial statements, particularly in relation to 'fund of fund' investment vehicles; and

(d) consolidating for only part of a period because the investment in the subsidiary fluctuates either side of a controlling level (say around 50%) in its outstanding ownership interests.

BC175 Based on these practical difficulties, some constituents recommended the AASB would need to provide application guidance on how the concept of control should be interpreted and applied in a superannuation context. To this end, some suggested a 'substance over form' approach be taken whereby entities that a parent 'actively' controls are consolidated and entities in which there is a 'passive' investment be accounted for as investments.

BC176 Other respondents suggested that, due to the nature of superannuation arrangements in Australia, in some circumstances the parent may be incapable of controlling an investee that would otherwise meet the definition of a subsidiary in a manner consistent with the notions of control in AASB 127 and AASB 10 because:

(a) members exercise investment choice and might collectively acquire a controlling interest in another entity, and the superannuation entity may not be considered to have the power to govern the investee so as to obtain benefits from its activities because the superannuation entity is subject to the independent investment choice decisions of its members; and

(b) the 'sole purpose test' in the Superannuation Industry (Supervision) Act is generally considered to prohibit trustees from being involved in day-to-day operations of the businesses in which their superannuation entities invest.

BC177 The AASB considered the concerns expressed in a superannuation context and noted that most, if not all, the practical difficulties identified are not unique to superannuation entities and are encountered by many other entities, including investment-type entities reporting under Australian Accounting Standards.

BC178 A number of the respondents opposed parent superannuation entities being required to present consolidated financial statements on the grounds that users, particularly members, are unlikely to consider consolidated information useful. They noted that, unlike shareholders in a company, members of a superannuation entity do not necessarily have a notional interest in all the net assets. In particular, some members may have no exposure to a subsidiary held by their superannuation entity because that investment is not part of some members' chosen investment options.

BC179 Some respondents to ED 223 noted their support for the proposals in IASB ED/2011/4 to account for most subsidiaries at fair value through profit or loss.

## Separate financial statements

BC180 The AASB considered whether there is any information that a user of the GPFSs of a superannuation parent might need that is not available in consolidated financial statements and concluded that consolidated financial statements would normally provide such users with the information they need in a superannuation context. However, if a parent superannuation entity prepares separate financial statements for general purpose users, the AASB reasoned the entity presumably considers this information necessary for an understanding of the reported results of the group. Accordingly, for the purposes of both ED 179 and ED 223, the AASB decided to propose that a parent superannuation entity that prepares separate financial statements for general purpose users should present them together with its consolidated financial statements.

18 ED/2011/4 *Investment Entities* (August 2011) was open for comment by 5 January 2012. ED/2011/4 was incorporated in AASB ED 220 *Investment Entities* for comment by 30 November 2011.

### Responses to the ED 179 and ED 223 separate financial statement proposals

BC181 Some respondents to ED 179 and ED 223 expressed concerns about the apparent inconsistency between the proposals about separate financial statements and the prudential reporting requirements in respect of separate financial statements that apply to APRA-regulated superannuation entities. The AASB acknowledged the concerns but concluded its proposals would not prevent an APRA-regulated superannuation entity from preparing separate financial statements for the specific purpose of fulfilling its prudential reporting obligations.

## AASB conclusions on consolidated and separate financial statements

BC182 Given the amendments made through AASB 2013-5, the AASB concluded that there should not be special requirements on consolidated or separate financial statements for superannuation entities. Accordingly, they would be required to account for their subsidiaries under AASB 10. If a superannuation entity qualifies as an 'investment entity' it would be required to account at fair value through profit or loss for its subsidiaries, except for any subsidiary that provides services relating to its investment activities, which would still need to be consolidated.

BC183 The AASB acknowledged this may mean that parent superannuation entities would generally account for their subsidiaries at fair value through profit or loss and not prepare consolidated financial statements. However, the AASB also concluded that superannuation entities that qualify as investment entities might have subsidiaries that provide services that relate to its investment activities[19] and/or it is conceivable that, now or in the future, there may be a superannuation entity that has subsidiaries and does not qualify to be treated as an 'investment entity'. In both these cases, when material, superannuation entities would still need to prepare consolidated financial statements under AASB 10.

# Disclosures

BC184 As outlined in the *Framework*, financial statement disclosures provide information about the risks and uncertainties affecting an entity. In many circumstances, the disclosure requirements of Australian Accounting Standards would provide users of the financial statements of a superannuation entity with useful information for their decision making. However, some disclosure principles and requirements of those Standards may not facilitate the provision of useful information in a superannuation context. For example, AASB 116 *Property, Plant and Equipment* requires entities applying the revaluation model to disclose the carrying amount of each revalued class of property, plant and equipment as it would have been measured under the cost model. However, there are very few circumstances in which users of superannuation entity financial statements might require historical cost information.

BC185 The AASB decided that ED 179 and ED 223 should propose the use of the disclosure requirements in many of the existing Australian Accounting Standards, but should also propose some disclosure principles that particularly suit the superannuation environment, in place of the requirements of some of those other Standards.

BC186 Accordingly, ED 179 and ED 223 proposed that:

(a) a superannuation entity apply the disclosure principles and requirements in other applicable Australian Accounting Standards unless they:

   (i) are not consistent with the measurement requirements for superannuation entities; or

   (ii) address the same items or events as the principles or requirements in the replacement Standard;

(b) superannuation-specific guidance in relation to the disclosure principles and requirements in other Australian Accounting Standards be provided only where it is necessary to facilitate their reliable and consistent application; and

(c) a superannuation entity disclose information that provides users, particularly members and beneficiaries, with a basis for understanding transactions and events specific to superannuation entities that are relevant to the users' decision making needs.

19 Refer to paragraph 32 of AASB 10 as amended by AASB 2013-5.

## Expense items

BC187 Most defined contribution members can choose the superannuation entity that manages their retirement benefits. However, to make informed decisions, members need to be able to compare plans, particularly with respect to expenses. Defined contribution members bear the costs associated with the management of their retirement benefits and the level of a plan's expenses can help provide a basis for understanding the level of fees that might be charged to members' accounts.

BC188 Employers would also be interested in information about the nature and amount of expenses, for example, in attempting to identify a default defined contribution plan for employees or because they sponsor defined benefit arrangements for their employees (and generally bear the costs of providing such arrangements).

BC189 In line with other Australian Accounting Standards, ED 179 and ED 223 proposed a superannuation entity disclose information about the nature and amount of expenses.

BC190 ED 179 and ED 223 also proposed that expense items of particular relevance, such as administration costs and trustees' fees, should be separately disclosed. Most respondents to both exposure drafts who commented on the proposals supported requiring these disclosures.

## Management expense ratio

BC191 The AASB considered whether a superannuation entity should be required to disclose a management expense ratio (MER) for the entity as a whole. The AASB concluded that a better focus of Australian Accounting Standards is to facilitate the provision of information from which users can calculate their own ratios for their particular needs. The AASB also noted MERs of superannuation entities are publicly available from other sources; and other investment-type entities are not required to disclose MERs under Australian Accounting Standards.

## Nature, extent and management of risks

BC192 Having considered the types of risks to which a superannuation entity could be exposed, the AASB decided ED 179 should propose that:

(a) the disclosure requirements in paragraphs 6 to 30 of AASB 7 should not apply; and

(b) disclosure principles based on paragraphs 31 to 42 of AASB 7 and tailored for a superannuation context would facilitate the disclosure of useful information about significant risks to which an entity is exposed.

BC193 The AASB concluded that paragraphs 6 to 30 of AASB 7 are generally not relevant in a superannuation context. For example:

(a) superannuation entities are not permitted to issue compound financial instruments with multiple embedded derivatives;

(b) paragraphs 9 to 11 of AASB 7 are intended to help explain an entity's choice to designate financial instruments at fair value through profit or loss,[20] whereas applying that measurement basis is the subject of specific requirements;

(c) paragraphs 25 to 30 of AASB 7 do not seem relevant because financial assets and any financial liabilities are measured at fair value through profit or loss; and for assets and liabilities relating to member benefits, there are the challenges noted in paragraph BC114(b) about obtaining fair values; and

(d) superannuation entities generally do not have loans and are prohibited from holding a borrowing directly, and therefore accounting mismatches of related loans and liabilities are generally not relevant.

BC194 In light of constituent feedback on ED 179, the AASB redeliberated the risk disclosure proposals and noted:

(a) the support for not requiring the application of paragraphs 6 to 30 of AASB 7 for the reasons in paragraph BC193;

(b) there may be less need for specific principles for superannuation entities regarding disclosures about the nature and extent of risks than assumed for the purposes of ED 179;

20 The Bases for Conclusions to IAS 32, IAS 39 and IFRS 7 suggest that paragraphs 9 to 11 of IFRS 7 are intended to address concerns about how entities exercise their choice to designate financial instruments at fair value through profit or loss.

(c) although AASB 7 scopes out obligations arising from employee benefit plans to which AASB 119 applies, a member liability meets the financial liability definition. This is because meeting members' benefits can be considered a contractual obligation of the superannuation entity (in the sense that defined contribution entitlements must be met and defined benefit entitlements are specified in trust deeds), and members' benefits are normally paid in cash;

(d) information in relation to the risk an employer-sponsor of defined benefit members will not be able to make contributions at a level that would be expected to permit the superannuation entity to meet members' accrued benefits is of critical importance in understanding a superannuation entity's overall financial position (solvency), irrespective of whether there is a surplus or deficit, and such risk is more in the nature of non-performance or economic dependency risk than credit risk; and

(e) additional liquidity risk disclosure about any non-financial liabilities other than tax liabilities of a superannuation entity can be justified on the basis that trustees are required to have an investment strategy that has regard to the entity's overall circumstances, including the liquidity of its investments and its expected cash flow requirements. Accordingly, entities with non-financial liabilities other than tax liabilities (such as provisions) would be expected to have considered the relevant liquidity risks and how they will be managed for prudential purposes. In this regard, the AASB noted that many superannuation entities would not have material non-financial liabilities other than those related to tax.

BC195 Based on its deliberations on the comments on ED 179, the AASB decided ED 223 should propose:

(a) a superannuation entity apply the principles and requirements in AASB 7, as appropriate, and should only include guidance considered necessary to facilitate their application in a superannuation entity context;

(b) a superannuation entity make disclosures consistent with the types of information disclosed under AASB 7 in relation to the liquidity risks arising from any non-financial liabilities other than tax liabilities; and

(c) a superannuation entity with defined benefit members provide qualitative disclosures about non-performance risk and/or economic dependency risk relating to the employer-sponsor(s).

BC196 Respondents to ED 223 expressed concerns that a requirement to disclose qualitative information about non-performance risk and/or economic dependency risk to which the plan is exposed in relation to employer-sponsors would give rise to 'boilerplate' disclosure. This is because, in some cases, the trustees would have no more information about a superannuation entity's reliance on employer-sponsors than is already publicly available and, in other cases, such a requirement might put the trustees in a position where they have to make judgements about the overall viability of an employer that may already be the subject of speculation in the business community.

BC197 Some respondents suggested the disclosure should instead focus on the process superannuation entities use to assess risks associated with employer-sponsors, or provide information focusing on the funding plans of a superannuation entity in relation to defined benefits.

BC198 In relation to defined contribution member liabilities, the AASB concluded the disclosure principles in AASB 7 would be relevant. However, in relation to defined benefit member liabilities, the AASB considers most of the disclosure principles in AASB 7 are not readily applicable, and concluded AASB 1056 should set out disclosure principles and related guidance on explaining the quantitative and/or qualitative information that would be useful, including:

(a) how any funding deficit is expected to be met – in terms of the nature, causes of, and any strategies for, addressing the deficit;

(b) the basis for assumptions and manner in which they are determined; and

(c) the sensitivity of the liabilities to changes in key assumptions.

BC199 The AASB concluded that, consistent with the principles in AASB 7, the subject of the sensitivity disclosures should be reasonably possible changes in the key assumptions, and when there is more than one key assumption for which a change is judged to be reasonably possible, the analysis can be performed on a univariate basis or on a multivariate basis.

BC200 Given the obligations of trustees to have an investment strategy that has regard to the entity's overall circumstances, including the liquidity of its investments and its expected cash flow requirements, the AASB also concluded that, where the entity's actual investment portfolio differs from the portfolio used in measuring defined benefit member liabilities, an explanation should be required of why that is the case.

## Disaggregated financial information

BC201 Information about the way a superannuation entity arranges and manages assets attributable to different groups of members, and the related member liabilities, can help provide users with a basis for understanding the financial performance, financial position and risk exposures of the entity as a whole.

BC202 In framing its ED 179 proposals, the AASB decided the 'through the eyes of management' approach applied to operating segments under AASB 8 *Operating Segments* would be an appropriate approach for superannuation entities to apply in respect of disclosing information about assets attributable to different groups of members and the related member liabilities because:

(a) whilst they generally do not have identifiable operating segments, some superannuation entities segregate their assets into different member groups to facilitate meeting liabilities to those different groups. Users would arguably benefit from these entities disclosing information about such asset groups and the related member liabilities that corresponds to information provided in management reports;

(b) the approach is sufficiently generic to be applied in disclosing information about assets attributable to different member groups;

(c) the approach should be generally less costly to apply than alternative approaches because it uses information already generated for management's use; and

(d) the approach is consistent with that proposed for other disclosures, such as disclosures about risks and risk management arrangements.

BC203 Some respondents to ED 179 agreed with the principle of having segment disclosures, particularly if they result in improved disclosures about risks attaching to different member groups. However, many other constituents expressed concerns about requiring segment-type disclosures because such requirements would:

(a) make some entities' note disclosures excessively long and complex, thereby diminishing their overall usefulness; and

(b) not assist users in understanding the overall financial position and performance of an entity that has member groups with different entitlements but 'pools' all its assets for investment purposes.

BC204 Of significance to many constituents were the potential practical implications of applying a segment-type approach in a superannuation context, including identifying segregated groups of assets. While trustees generally manage member liabilities on a segregated basis, most pool assets to achieve efficiencies. Some respondents expressed concern that some relatively common situations that arise with pooled assets may nevertheless satisfy the criteria for managing assets on a segregated basis. For example, they were concerned entities that provide investment choices to members may be required to treat each investment choice as a segregated asset group because entities' trustees might often:

(a) adjust actual allocations between asset classes within a particular investment option to match target allocations following movements in investment markets; and

(b) adjust actual allocations of assets between investment options to match member liabilities.

BC205 Others were concerned about applying the proposals to master trusts and multi-employer-sponsored plans, some of which have in excess of 100 sub-plans, which comprise members with the same or related employer-sponsors. While trustees generally monitor the financial position of sub-plans in relation to defined benefit members on a regular basis, they do not monitor the financial performance of each sub-plan because a significant proportion of the plan's expenses are not capable of being reliably attributed to individual sub-plans. Accordingly, given the likely cost of determining, presenting and understanding this information, it is unlikely the ED 179 segment disclosure proposals would give rise to sufficient benefits in the context of master trusts and multi-employer-sponsored plans.

BC206 Others are keen to avoid duplication of effort, by aligning any segment-type disclosures with prudential reporting requirements.

BC207 Based on responses to ED 179, the AASB:

(a) noted that a significant number of superannuation entities are managed by their trustees on a segmented basis, although segmentation will often not be clear from the way the entity's assets are managed;

(b) decided that disaggregated financial disclosures would provide useful information for users, particularly for hybrid entities because they are exposed to different types and levels of risks; and

(c) decided that there is a need to mitigate the practical issues identified by constituents.

BC208 The AASB noted that requiring superannuation entities to provide disaggregated disclosures on the basis of member groups would facilitate a hybrid superannuation entity providing risk-based disclosures in respect of its liabilities to the different classes of members and it would potentially address some concerns of constituents around investment options and sub-plans being the subject of disaggregated disclosure. However, disaggregated disclosures may, for example, not be useful for showing how a hybrid plan with a small number of defined benefit members arranges and manages activities.

BC209 The AASB also noted that requiring the use of the principles and requirements in AASB 8, as appropriate, might have drawbacks, including:

(a) some of the terms used in AASB 8 may be ambiguous or irrelevant in a superannuation context. For example, a characteristic of an operating segment is that its operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resource allocations. However, some could interpret this to mean that investment options are not operating segments because members generally decide how the assets of the plan are allocated; and

(b) some entities may provide only limited segment information under the principles and requirements in AASB 8, even when they have both defined contribution and defined benefit members because the operating results regularly reviewed by the trustees do not distinguish between the two groups of members or their related assets.

BC210 Based on these considerations, the AASB decided ED 223 should propose that a superannuation entity provide disaggregated disclosures in accordance with the principles and requirements in AASB 8, except where it is appropriate to modify the requirements for application in a superannuation context. This was intended to provide trustees with more flexibility and enable them to provide disaggregated information that reflects the manner in which they arrange and manage the assets and liabilities of their entity.

BC211 In coming to these proposals, the AASB noted paragraph 19 of AASB 8 comments that there may be a practical limit to the number of reportable segments an entity separately discloses beyond which segment information may become too detailed.

BC212 Respondents to ED 223 raised many of the same concerns with the proposals as were expressed in relation to the ED 179 proposals.

BC213 In redeliberating its approach, the AASB noted that the role of a trustee in a superannuation entity differs from the role of a chief operating decision maker in the context of AASB 8, and the main focus in a superannuation entity context should be on information about different categories of members. Accordingly, the AASB concluded there should be no specific disaggregated information disclosure requirements, but there should be a general requirement to disclose disaggregated information when that would help to explain the risks to which different categories of members are exposed.

## Expected rates of return

BC214 The AASB considered whether a superannuation entity should be required to disclose its expected rates of return. The AASB noted other Australian Accounting Standards do not typically require 'forecast-type' information and that requiring disclosure of expected rates of return in the context of member investment choice would arguably not be helpful. Accordingly, the AASB concluded that AASB 1056 should not require expected rates of return disclosure.

## Member liabilities

BC215 The nature of a defined contribution member liability differs from the nature of a defined benefit member liability. As these differences are likely to affect a user's understanding of a superannuation entity's member liabilities, the AASB concluded a superannuation entity should disclose information that provides users with a basis for understanding the entity's member liabilities.

BC216 AAS 25 required disclosure of defined benefit members' vested benefits at the end of the period. The AASB considered the merits of continuing to require this information and concluded that it is useful information to users because:

(a) items that may be regarded as analogous to vested benefits are reported by other entities. For example, 'demand deposits' are reported by banks; and

(b) vested benefits may be regarded as akin to the current portion of defined benefit member liabilities, and AASB 101 includes classification requirements for separate presentation of current and non-current liabilities.

### AASB 119 requirements

BC217 The AASB considered whether the disclosures required in AASB 119 about member benefits should be required of superannuation entities. This included considering proposals in AASB ED 195, which incorporated the IASB's ED/2010/3 *Defined Benefit Plans – Proposed amendments to IAS 19* (May 2010) as a part of a project to improve accounting for employee benefits. Consistent with ED 195, ED 179 and ED 223 proposed a superannuation entity disclose the main components of any remeasurement changes in defined benefit liabilities, including benefit cost, interest cost and actuarial gains and losses.

BC218 However, ED 179 and ED 223 did not incorporate some other ED 195 disclosure proposals, including disclosure of defined benefit member liabilities adjusted to exclude the effect of projected growth in salaries ('accumulated benefit obligation'), because it is inconsistent with the presumption employers will meet their defined benefit member liabilities in full.

BC219 The AASB considered whether ED 223 should propose that a superannuation entity disclose information required by AASB 119 (as amended in 2011) and decided those requirements are generally not relevant in a superannuation entity context. This was mainly because AASB 119 has an employer perspective, which differs from the member perspective of superannuation entities.

BC220 Instead, the AASB concluded that more relevant information would result by requiring disclosures that satisfy principles regarding providing users with an understanding of the nature of member benefits and the risks associated with them.

### Net assets attributable to defined benefit members

BC221 At any particular time, the amount of net assets attributable to defined benefit members may differ from the amount of such members' accrued benefits. However, the existence of a surplus or deficit does not necessarily mean the superannuation entity will or will not be able to pay these benefits when due. Other factors can influence the capacity to pay defined benefit members, including the expected earnings rate on the net assets attributable to such members and the expected level of future contributions by defined benefit members and/or their employer-sponsors. Nevertheless, knowledge of the relationship between the net assets attributable to defined benefit members and such members' accrued benefits is important for an understanding of a plan's financial position, including its solvency. The AASB concluded that information about the size, nature, causes of, and any strategies for addressing a surplus or deficit should be disclosed.

### Remeasurement changes in defined benefit members' accrued benefits

BC222 During its deliberations on the proposals in ED 179, the AASB considered whether separate disclosures of the components of remeasurement changes in defined benefit members' accrued benefits, particularly benefit cost, interest cost and actuarial gains and losses, would be useful information. The AASB noted some users might consider the amount of benefit cost for a period to be useful in providing an indication of the recurring cost to the superannuation entity of providing defined benefit entitlements. The AASB also noted some users might consider the amount of any actuarial gains and losses for a period to be useful information as it provides an indication of how accurately the superannuation plan has estimated the key determinants of defined benefit members' accrued benefits. However, the AASB also noted information about the components of remeasurement changes in defined benefit member liabilities might be regarded as relatively more useful in an employer-sponsor context. Accordingly, the AASB decided ED 179 should ask constituents whether the separate disclosure of the components of remeasurement changes would provide useful information for users in a superannuation context and, if so, how it should be presented.

BC223 The majority of respondents to ED 179 expressed a view that the disclosures should be required. Other respondents:

(a) did not agree with the proposal that defined benefit member liabilities be measured at the amount of such members' accrued benefits; and/or

(b) did not consider such disclosures would be justified on cost-benefit grounds because the number of defined benefit members is declining.

BC224 The AASB included similar proposals in ED 223. A number of respondents to ED 223 noted that, in the general course of measuring defined benefit member liabilities, an actuarial report would not usually provide quantitative information on components of the change from one period to the next and nor would any of the potential shortcut methods of achieving materially the same measure as would be provided by a full actuarial assessment. They also noted that such information might only be relevant in an employer context where the employer is recognising the net difference between the liabilities and the assets supporting the liabilities.

BC225 Based on the responses received on ED 223, and in view of the likely costs involved in determining quantitative information on components of the change from one period to the next, the AASB concluded disclosure of explanations in either quantitative or qualitative terms about changes in defined benefit member liabilities should be required.

## Related parties

BC226 The AASB noted that, while the disclosure principles and requirements of AASB 124 *Related Party Disclosures* would apply to most of the related party relationships and transactions that a superannuation entity would be involved in, they may not facilitate consistent disclosures across all superannuation entities.

BC227 At the time the AASB deliberated on the proposals in ED 179, the definition of related party in AASB 124 focused predominantly upon relationships premised on control, joint control or significant influence. Nevertheless, the AASB concluded that trustees and employer-sponsors are, in essence, related parties of superannuation entities because they can affect those entities' financing and operating policies. ED 179 proposed disclosure about the entity's relationships with its trustee(s) and employer-sponsor(s), any transactions with trustees or employer-sponsors during the reporting period, and any outstanding balances with trustees and employer-sponsors at the end of the reporting period, if the nature of these relationships, transactions or balances were not considered 'normal' in a superannuation context.

BC228 Some ED 179 respondents expressed concerns with the proposed manner in which related party disclosures would be dealt with and suggested that:

(a) the proposals do not appear to include the materiality threshold that applies in relation to AASB 124; and

(b) the term 'normal' may be difficult to apply in some circumstances to determine whether a transaction and/or balance between a plan, its trustee or an employer-sponsor should be disclosed.

BC229 AASB 124 was reissued in 2009 and related parties of post-employment benefit plans now explicitly include their sponsoring employer(s).

BC230 The AASB decided ED 223 should propose that a superannuation entity apply, when appropriate, the principles and requirements in AASB 124. The AASB also decided it should propose that a trustee be specifically identified as a related party of its superannuation entity, primarily because trustees have the ability to affect the financing and operating policies. Based on the responses received on ED 223, the AASB concluded that a trustee of a superannuation entity is a related party of the entity for the purpose of applying AASB 124.

BC231 The AASB also noted that an employer of members of a superannuation entity (that the employer does not sponsor) may, in some cases, be a related party of the entity. However, the AASB concluded that this would need to be decided on the basis of the facts in each case and that there is no need to specifically identify employers as related parties.

## Insurance contracts

BC232 The AASB included proposed disclosure requirements in ED 179 and ED 223 to complement the proposed recognition and measurement requirements relating to insurance arrangements a superannuation entity provides to its members. Constituents' comments on the ED 179 and ED 223 proposals tended to focus on the recognition and measurement issues, however, the constituents comment on the Draft AASB 1056 for fatal flaw review included feedback on the disclosure issues.

BC233 Based on the feedback received, the AASB concluded that a superannuation entity taking on the role of an insurer in relation to its defined contribution members should separately disclose in their financial statements items such as:

(a) insurance contract revenue, incurred claims expense, reinsurance expense and reinsurance recoveries recognised in the income statement;

(b) insurance contract liabilities and reinsurance contract assets recognised in the statement of financial position; and

(c) insurance contract cash inflows, reinsurance contract cash outflows, claims cash outflows and reinsurance recoveries cash inflows recognised in the statement of cash flows.

BC234 In relation to defined benefit members, the AASB noted that, depending on the conditions set out in the relevant trust deed, those members (or their beneficiaries) might be promised, for example, a lump sum benefit on retirement or resignation, a lump sum benefit on death or disablement, a pension on retirement for their remaining lifetime and/or a pension for the remaining lifetime of a spouse, and the pension may or may not be indexed in some way. The AASB noted that the defined benefit member liability is effectively the sum of the expected values associated with the various ways in which members might be paid their benefits, and can be regarded as a single item made up of inter-related components. Accordingly, the AASB concluded that liabilities and assets arising from insurance arrangements a superannuation entity provides to defined benefit members need not be presented separately from the entity's liabilities for such members' benefits in the statement of financial position. Furthermore, unless there are explicit direct premiums, claims, reinsurance premiums or claim recoveries relating to insurance risks, the AASB concluded that amounts relating to insurance arrangements a superannuation entity provides to defined benefit members need not be presented separately in the income statement, statement of changes in member benefits or statement of cash flows.

## Definitions

BC235 AAS 25 defines a number of terms and phrases relevant to a superannuation context. However, some of these terms are no longer consistent with the definitions of the same or equivalent terms in Australian Accounting Standards. In addition, the AASB decided that some of the terms and phrases defined in AAS 25 are no longer necessary.

BC236 Consistent with its current policies, the AASB decided:

(a) there is no need to define terms in AASB 1056 that are defined elsewhere or are similar to terms defined elsewhere in Australian Accounting Standards, such as 'general purpose financial report' and 'reporting date'; and

(b) to include in AASB 1056 definitions of specific relevance in a superannuation entity context, such as 'defined contribution member' and 'defined benefit member' based on the AAS 25 definitions for 'defined contribution plan' or 'defined benefit plan' (which themselves are not included in AASB 1056 because that entity-based dichotomy is no longer relevant).

### Other issues raised on definitions

BC237 In ED 179, the AASB proposed that:

(a) the definition of the term 'vested benefits' should be based on the definition of the same term in AASB 119, but amended to reflect the nature of such benefits in a superannuation context; and

(b) the term 'accrued benefits' should be defined broadly to cover both defined contribution and defined benefit arrangements.

BC238 Several respondents to ED 179 raised concerns with the applicability of the definition of vested benefits in the context of defined benefit members. The AASB noted, for a superannuation entity with only defined contribution members, the amount of its member liabilities may not change as a consequence of the timing or circumstances of a member's departure (for example, resignation, retrenchment or retirement). However, depending on the relevant trust deed, different timing or circumstances may give rise to different entitlements for defined benefit members. Accordingly, in ED 223 the AASB proposed the definition of vested benefits be amended to clarify that:

(a) vested benefits are the benefits a member would be entitled to on voluntary withdrawal from their superannuation entity at the end of the period; and

(b) in the context of defined benefit members' vested benefits, the term 'withdrawal' could be interpreted to mean voluntary withdrawal by the member from either the defined benefit section of the entity or from the entity itself.

BC239 One respondent to ED 179 noted the proposed 'defined benefit member' definition did not identify the employer-sponsor's responsibility for investment risk as a distinguishing feature, and is not adequately distinguished from defined contribution members. However, the AASB was not persuaded by this view because investment risk is not a defining characteristic of such arrangements, for example, for employer-sponsors of unfunded defined benefit public sector schemes.

## Effective date and transition on initial application

BC240 The AASB noted that, given the extent of the changes, unless comparative information is prepared on the same basis as the current period information in the year of transition, the comparative information would not be useful. Accordingly, the AASB concluded the AASB 1056 requirements should be applied retrospectively in accordance with paragraphs 19 to 27 of AASB 108 *Accounting Policies, Changes in Accounting Estimates* *and Errors* and, therefore, the comparative information on transition should be prepared on the basis of the AASB 1056 requirements.

BC241 The AASB considered the time that superannuation entities would need to adjust their financial reporting systems in order to transition from applying the requirements of AAS 25 to applying the requirements of AASB 1056. In particular, the AASB noted the changes that might need to be made by superannuation entities with defined benefit members liabilities and entities that are so-called 'paragraph 66 plans' (also see paragraph BC34).

BC242 In light of the expected financial reporting impacts on superannuation entities of replacing AAS 25 with AASB 1056 and the need to present comparative information in accordance with AASB 1056, the AASB considered that there should be a period of at least two years between the making of AASB 1056 and its mandatory application date. In particular, the AASB noted that, for superannuation entities that undertake a comprehensive valuation of some or all of their defined benefit member liabilities on a triennial basis, it might be most practicable for there to be at least three year-ends (including the comparative year-end) between the making of AASB 1056 and the year-end relating to the mandatory application date.

BC243 The AASB also noted that paragraph 10(f) of AASB 101 would generally require a statement of financial position to be presented for the beginning of the earliest comparative period, which based on the thinking in paragraph BC242 would mean a mandatory application date of 1 July 2017. The AASB considers this to be an excessively long time to elapse before the mandatory application date and concluded that:

(a) the mandatory application date should be annual reporting periods beginning on or after 1 July 2016; and

(b) superannuation entities should be specifically exempted from presenting a statement of financial position as at the beginning of the earliest comparative period for which information is included in its financial statements when they transition to AASB 1056.

## Implications of the review of the governance, structure and operation of Australia's superannuation system

BC244 On 30 June 2010, the report on the *Review of the Governance, Efficiency, Structure and Operation of Australia's Superannuation System* (the Review) was presented to the Federal Minister for Financial Services, Superannuation and Corporate Law. As a part of its terms of reference, the Review considered issues in relation to the fees, costs and investment returns of superannuation entities, and improving transparency around these items through reporting to advisers, researchers, analysts, regulators and members.

BC245 The Review Panel concluded that the Australian superannuation system currently lacks transparency, comparability and accountability in relation to costs, fees and investment returns. It also concluded that, while the proposals in ED 179 would improve financial reporting by superannuation plans, they would not materially improve the information required by individual users, particularly individual members.

BC246 The Review Panel considered the superannuation industry and members are more concerned about the performance of the investment options in which they are invested than the whole-of-fund information required by AAS 25. It also noted a perceived disconnect between the information provided by superannuation entities in GPFSs and the information needs of users, particularly members, which would be unlikely to be rectified under the proposals in ED 179. However, there was an acknowledgement by the Review Panel that a plan member can be affected by factors impacting on their plan as a whole.[21]

BC247 The AASB considered the Panel's findings and noted, even though the GPFSs of superannuation entities are not targeted at each member's particular interest, the whole-of-fund financial information is useful to members and other users for their decision making.

BC248 In addition, the AASB concluded financial statements play an important role within the current regulatory arrangements by providing a basis for information reported in trustees' annual reports to members and members' individual benefit statements, even though these would not include the same level of disclosure or necessarily have been audited. Consequently, under the current arrangements financial statements are a key medium through which trustees discharge their accountability responsibilities.

BC249 The Stronger Super reforms implemented from 1 July 2013 are the government response to the Review recommendations and the AASB has monitored those reforms and, where relevant, considered them in developing AASB 1056.

21 As noted in the Review Panel's Final Report (page 173) "… during the GFC, previously liquid assets held by some superannuation funds became illiquid due to capital freezes in mortgage, cash management and property trusts. In order to meet portability, switching and capital drawdown requests, some trustees were forced to sell equities into a depressed market, while trustees who were unable to meet these requests applied to APRA for a variation or suspension of portability requirements."

## Certain other matters raised by respondents to ED 179 and ED 223 that the AASB decided not to pursue

BC250 Some respondents to ED 179 and ED 223 sought specific guidance in relation to superannuation entities on the following:

(a) the preparation and presentation of consolidated financial statements under AASB 3 and AASB 10;

(b) presentation of statements of cash flows and disclosures in relation to non-cash transactions under AASB 107 *Statement of Cash Flows*. In doing so, the AASB noted AASB 107 requires entities to:

(i) disclose a reconciliation of cash flows arising from operating activities to profit or loss;

(ii) report cash flows from operating, investing and financing activities on a gross basis; and

(iii) disclose non-cash investing and financing transactions in a way that provides relevant information about such transactions;

(c) risk-based disclosures in relation to asset concentrations and sensitivity analyses;

(d) disclosures in relation to business, non-financial and emerging risks;

(e) disclosures in relation to information about reserves;

(f) how a superannuation entity's tax liability for a period might be allocated between the income statement and the statement of changes in member benefits, particularly since the *Income Tax Assessment Act 1997* does not generally distinguish between income tax on investment earnings and tax on contributions The AASB noted that superannuation entities would currently need to distinguish between tax on earnings and tax attributable to contributions in order to determine member benefits and that non-superannuation entities are required to perform similar calculations under other Australian Accounting Standards;

(g) facilitating separate presentation of realised and unrealised gains and losses. The AASB noted that superannuation entities would not be prevented from presenting or disclosing such additional information if it provides useful information to users of its financial statements;

(h) presentation of 'netted off' revenue and expense items, particularly in relation to entities conducting their investment arrangements through investment managers and/or custodians;

(i) circumstances in which contributions in respect of defined contribution members should be recognised on an accrual basis or a cash basis; and

(j) circumstances in which benefits payable would be disclosed as a current liability. The AASB noted that AASB 101 has relevant criteria for distinguishing between current and non-current liabilities.

BC251 The AASB concluded that the issues underlying some of those concerns:

(a) are outside the scope of general purpose financial reporting;

(b) are dealt with in other Australian Accounting Standards; and/or

(c) arise under other Australian Accounting Standards and are dealt with by non-superannuation entities without additional guidance.

The AASB also noted that providing superannuation-specific guidance on the application of the principles and requirements in other Australian Accounting Standards would run the risk of interpreting IFRS principles and requirements in a way that is not consistent with the way they are interpreted in other contexts.

BC252 Some respondents raised issues about better identifying the 'reporting entity' in a superannuation industry context. They noted that, in the private sector, Registrable Superannuation Entities (RSE) would typically be the entities that apply AAS 25 and would apply AASB 1056, but that this may not be the appropriate entity level at which general purpose financial reporting should take place. At this stage, the AASB concluded that this topic would need to be the subject of future research (refer to paragraph BC2).