

International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH
United Kingdom

6 September 2010

Submitted via the “Open to Comment” page at www.iasb.org

Dear Sirs

**IASB Exposure Draft ED/2010/3
Defined Benefit Plans (Proposed amendments to IAS 19 Employee Benefits)**

I am writing on behalf of AFME (the Association for Financial Markets in Europe) to respond to the IASB’s Exposure Draft ED/2010/03: Defined Benefit Plans (Proposed amendments to IAS 19 Employee Benefits) (the “ED”). AFME is, as you know, the leading European trade association for firms active in investment banking and securities trading; it was established on 1 November 2009 as a result of the merger of LIBA (the London Investment Banking Association) and the European Branch of SIFMA (the US-based Securities Industry and Financial Markets Association), and thus represents the shared interests of a broad range of participants in the wholesale financial markets. We welcome the opportunity to comment on this ED.

While some AFME members could be significantly impacted by the proposed changes to accounting for defined benefit pension schemes, this is not a topic that we normally address as an industry group, and we have therefore not responded to the detailed questions set out on pages 7-12 of the ED. We do however have significant concerns with the current requirements of IAS 19 in relation to the accounting for certain forms of long term employee benefits; the proposed amendments in the ED will, we believe, not resolve, and may in fact exacerbate, these issues.

IAS 19 currently requires an actuarial approach to be applied to long term employee benefits such as deferred compensation schemes. As detailed below, we believe that this does not properly reflect the substance of certain such arrangements and so does not provide the most useful information to users of the accounts.

Furthermore, under the proposed amendments, a portion of the expense for such deferred compensation schemes will be recognised in other comprehensive income (“OCI”) rather than all such costs being recognised through profit or loss, as is currently the case under IAS 19. We believe this will further reduce the relevance of the information provided to users of the accounts in respect of this type of compensation scheme.

This issue is of significant concern for our industry because of the focus that regulators and others are currently placing on the deferral of annual bonuses, which has resulted in greater use of deferred compensation schemes. We have set out below our concerns with the current accounting for these schemes under IAS 19 and our understanding of how the proposals in the ED will impact this.

To illustrate the issue, consider a deferred compensation scheme which provides an employee with a nominal award of £1,000 on grant date. This is invested in notional investments and, at the end of a three-year vesting period, the employee receives cash equal to the value of the notional investments at the settlement date.

If the notional investments underlying the award were the entity’s own equity instruments, this award would be classified as a cash-settled share-based payment scheme under IFRS 2, and the employee liability would be remeasured to fair value at each balance sheet date with changes in fair value being recognised in profit or loss. The current provisions of IAS 19, however, require an “actuarial approach” to be applied to a deferred compensation scheme which holds investments other than the entity’s own equity instruments. This results in inconsistent accounting treatment being applied to essentially similar arrangements, where the sole distinction is the nature of the underlying notional investments (i.e. whether or not they are the entity’s own shares).

We believe that aligning the accounting for deferred compensation schemes that currently come within the scope of IAS 19 with the accounting for similar schemes that come within the scope of IFRS 2 would provide a better framework for the accounting for such arrangements for the following reasons:

- Conceptually, a deferred compensation scheme is far closer to a cash settled share-based payment award than it is to a pension scheme. The employee benefit obligation under the deferred compensation scheme is affected only by the valuation of the underlying assets, while valuing a defined benefit pension scheme requires consideration of a number of more subjective variables such as future salary increases and mortality rates; and
- Measuring the deferred compensation liability at the current fair value of the underlying investments is a superior approach to applying an actuarial method, which requires forecasting the return on the assets and discounting that using a corporate bond rate. The former approach is also far easier to apply and, in our view, provides more relevant information to users of the accounts.

The current requirement in IAS 19 to present a net expense for other long term employee benefits in profit or loss lessens the impact of the above inconsistencies. However, we believe that the changes proposed in the ED would exacerbate these existing issues for the following reasons:

- The employee benefit liability for deferred compensation schemes and any associated hedges tend to be held “on balance sheet” rather than being managed via a separate trust, so the concept of a “net defined benefit liability/asset” cannot be readily applied. As a result, the calculation of the finance cost would be significantly overstated by ignoring the return on the assets held to hedge the liability, and presenting this finance cost separately in profit or loss is meaningless; and
- Valuing the obligation using actuarial methods and the financial instruments used to hedge the obligation on a fair value basis creates a measurement mismatch which adds unnecessary volatility to the financial statements, and thus reduces relevance for users of the accounts. This mismatch is currently confined to profit or loss, but will be exacerbated under the proposals in the ED, which will move the component relating to the re-measurement of the employee obligation to OCI.

We also have conceptual concerns with removing re-measurements of deferred compensation scheme obligations from profit or loss. These schemes are an integral part of employee compensation arrangements for our industry and should therefore, we believe, be included in the reported operating results of the entity. Further, short term fluctuations in the value of the obligation arising under such schemes are likely to have a direct impact on the final obligation due to the employee, whereas, in the case of pension schemes, short term fluctuations are more likely to be averaged out in the long term and thus have less relevance to reporting operating performance.

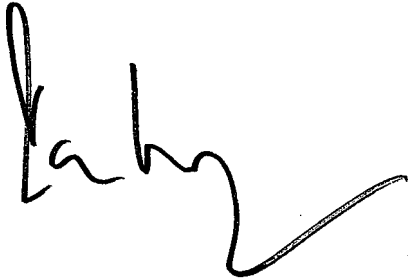
An additional concern of our members with the proposals in the ED in relation to deferred compensation schemes is their impact on the presentation of costs associated with short term and long term awards. The proposed ED requirement to recognise in OCI certain elements of any changes in the value of long-term employment benefits will result very different presentations of the effects of such changes for long-term and for short-term awards. We do not believe there is any conceptual difference between, say, a one-year and a two-year scheme that would justify such a difference in presentation. We also note that this difference in presentation could be open to manipulation: changing the settlement date of the award by as little as one day could, for example, determine whether changes in the value of an award are presented through OCI or through profit or loss.

In summary, we believe IAS 19 should, as a minimum, include a distinction between “long-term employee benefits” and “post employment benefits” in relation to the recognition of re-measurement gains and losses through profit or loss and OCI respectively, so as to avoid the significant presentational issues outlined above. Further, we believe that the Board should address the inconsistency between IFRS 2 and IAS 19 in the accounting for deferred compensation schemes by removing the requirement to apply an actuarial approach to such arrangements.

Finally, we note that the definition of “fair value” in paragraph 7 of the ED is inconsistent with that provided in ED/2009/5 Fair Value Measurement and suggest that this inconsistency should be resolved during the finalisation of the amendments.

I hope the above comments are helpful. We would of course be pleased to discuss any points which you may find unclear, or where you believe AFME members might be able to assist in other ways.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Ian Harrison', with a long, sweeping horizontal stroke at the end.

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