The Actuarial Profession
making financial sense of the future

responses

International Accounting Standards Board

Exposure Draft: Financial Instruments - Classification and Measurement

September 2009

About The Actuarial Profession

The Actuarial Profession is governed jointly by the Faculty of Actuaries in Edinburgh and the Institute of Actuaries in London, the two professional bodies for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuing professional development and a professional code of conduct supports high standards reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business's assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals, and advise on social and public interest issues. Members of the Profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.

The Profession also has an obligation to serve the public interest and one method by which it seeks to do so is by making informed contributions to debates on matters of public interest.

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www.iasb.org

30 September 2009

Dear Sir/Madam

IASB Exposure Draft *Financial Instruments: Classification and Measurement*

Thank you for offering The Actuarial Profession the opportunity to comment on this Exposure Draft. The response comes from the part of the Profession representing pensions actuaries.

We do not comment in detail on the proposals. Instead, we draw attention to the high level difference between the proposed model and the current model (and recent consultations and thinking on a new model) for post-employment benefits – in particular pensions – set out in IAS19. We do not see a justification for the differences.

We note that under current accounting standards, the performance statements incorporate a mix of approaches: some items are marked to market through P&L; some are marked to market but through the statement of comprehensive income, and others – which for many companies are just as large and as volatile – are not marked to market at all. The impression is given to management and investors alike that those items which are marked to market are more risky than those which are not. This influences investor pressures on management, and impacts management behaviour both directly and in response to investor pressure. There is clear risk that decisions made are as a result sub-optimal.

The obligation to make payments under a loan arrangement is economically the same as the obligation to pay a portfolio of pensions to former employees. The longer dated the loan the more clear that economic comparison is. The dependence of pension obligations on longevity complicates the calculations, but does not change the economic fundamentals.

However, the exposure draft proposes that loan liabilities should be measured on an amortised cost basis, which is not consistent with the approach for pensions. The arguments in favour and against subsequent measurement of loan obligations at fair value are the same as those that would apply in respect of pension obligations. We could not identify any clear arguments from the paper that would justify a difference in approach.

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As noted above, a difference in measurement approach between economically similar obligations that have different labels attached to them has real world consequences, and leads to sub-optimal management decisions.

If you have any questions or would like to discuss any of these matters further, please do not hesitate to contact us. Should you wish to do so, please contact Martin Hewitt, Pensions Practice Manager on 0207 632 2185 or via martin.hewitt@actuaries.org.uk.

Yours sincerely

Robert Hails
Chairman, Consultations Group, Pensions Practice Executive Committee

Please reply to Staple Inn