

Public Sector Pensions Briefing

Local Government Pension Scheme: Changes to the FRS17 Disclosures

December 06

Following the publication of a Financial Reporting Exposure Draft (FRED) back in May, earlier this month the UK Accounting Standards Board (ASB) issued an amendment to Financial Reporting Standard FRS 17¹ replacing the existing disclosures with those of the International Accounting Standard IAS19. The amendments come into force for accounting periods beginning on or after 6 April 2007, with early adoption encouraged.

This briefing note has been prepared by Hymans Robertson LLP's Public Sector Practice specifically for employers participating in the LGPS. It summarises the amendments and is intended to assist in planning for the 2007 FRS17 exercise.

INTRODUCTION

The UK Accounting Standards Board (ASB) is conducting a research project to completely re-evaluate accounting for defined benefit pension schemes in companies' financial statements. Independently, it has reviewed the disclosures required under the existing Financial Reporting Standard FRS17, and proposed changes to it, by way of a Financial Reporting Exposure Draft (FRED), many of which have now been adopted.

The intention behind the amendments is to achieve harmonisation, as far as possible, with the corresponding International Accounting Standard, IAS 19: the changes replace the existing FRS 17 disclosures with those in IAS 19.

In addition to the new disclosure requirements, there is a revision to paragraph 9 of FRS17, which relates to the circumstances in which an employer participating in a defined benefit multi-employer scheme (such as LGPS) can account for it as a defined contribution scheme, i.e. on the basis of cash contributions to the scheme. Finally, assets will have to be taken into account at their bid value rather than the mid-market value.

The FRED proposed additional disclosure information to be set out in a draft Reporting Statement in response to criticism that there is currently insufficient information to allow users of the financial statements to obtain a clear view of the risks arising from defined benefit schemes. Following comments on the FRED this additional reporting requirement has not made it into the final amendments although details of the ASB's proposals for best practice extended disclosures are expected in January 2007.

NEW DISCLOSURE REQUIREMENTS

For those interested in comparing the detail of revised FRS 17 disclosures with the IAS 19 equivalent, Appendix I of the amendment includes a specimen set of proposed FRS 17 disclosures, presented as a mark-up of the specimen IAS 19 disclosures.

The main changes to the disclosures and those which are removed from the existing requirements under FRS17 are summarised in the following table:

¹

http://www.frc.org.uk/images/uploaded/documents/Amend_FRS17%20web%20op_timized1.pdf

LOCAL GOVERNMENT PENSION SCHEME: CHANGES TO THE FRS17 DISCLOSURES

Additional disclosures required (following IAS19)	FRS17 disclosures no longer required
<ul style="list-style-type: none"> • Information on the nature of the defined benefit pension scheme and the financial effects of changes in the scheme; • The principal actuarial assumptions at the balance sheet date. (FRS 17 previously only required disclosure of financial assumptions. The ASB anticipates that details of mortality assumptions are likely to be required.) • Separate analyses of changes in scheme assets and liabilities over the year. • Analysis of scheme liabilities into amounts arising from wholly unfunded schemes and amounts from other schemes. 	<ul style="list-style-type: none"> • The date of the most recent full valuation and whether the actuary is a company officer or employee. • The effect of changes in actuarial assumptions over the year • The financial assumptions at the start of the year • An analysis of reserves in the notes to the accounts, distinguishing the amount related to the defined benefit asset or liability net of deferred tax • The expected rate of return on individual asset classes (originally suggested as an item for inclusion in the draft Reporting Statement).

It should be noted that the changes will not affect the balance sheet position or the charge to operating profit. What they do mean is that rather than the current approach, where the subsidiary revenue account statements reconcile the movement in the net pension asset/liability over the year, the new disclosures will separately reconcile the change in assets and liabilities.

MULTI-EMPLOYER SCHEMES

The changes to FRS17 amend paragraph 9(b) so that rather than simply stating that the scheme is a defined benefit scheme but the employer cannot identify its share of the assets and liabilities, the reason why sufficient information is not available to

enable the employer to account for the scheme as a defined benefit scheme, must be given. Given that we are typically able to identify the assets and liabilities (using an analysis of experience approach to the former as described in many funding strategy statements), we suspect that it will be increasingly difficult for employers to continue to adopt defined contribution accounting for their LGPS liabilities.

MEASUREMENT OF SCHEME ASSETS

FRS17 currently states that the fair value of quoted securities is the mid-market value. For accounting periods beginning on or after 6 April 2007, quoted securities will be required to be valued at their bid price. We do not anticipate that this will have a material effect on the figures.

IMPLICATIONS FOR THE 2007 FRS17 EXERCISE

As indicated above, the amendments do not come into force until 6 April 2007. We would expect that LGPS employers following CIPFA's guidance or who adhere to the guidance in the Financial Reporting Manual will consider these changes more of a nuisance than anything else given that employers (and many auditors) are only now becoming familiar with the format of the current FRS17 disclosures. There is also the possible extra cost of reports adhering to the new requirements. We would not expect such employers to adopt the changes early, and indeed, our understanding is that the local authority SORP for 2006/07 has already been finalised.

Whilst we do not yet know if the relevant governing bodies will choose to adopt the amended FRS17 for public sector entities, we suspect that there may be pressure to do so in order to maintain consistency with disclosures in the private sector. Once the changes are implemented, employers should be aware that there could be a further source of extra costs if auditors require prior years' figures to be re-stated.

We will be liaising with both CIPFA and the Audit Commission to confirm their requirements/guidance in advance of the March 2007 FRS17 exercise and

LOCAL GOVERNMENT PENSION SCHEME: CHANGES TO THE FRS17 DISCLOSURES

would encourage employers to discuss their approach with their auditors at an early stage.

Private sector employers who are currently subject to FRS17 will automatically have to adopt the new standard from 6 April 2007, although for many, the similarity to the international accounting standard will be welcomed. In light of this, it seems to us to be more likely that corporate entities will want to consider adopting the amendments early (i.e. as at 31 March 2007), particularly those who are already required to make disclosures under IAS19.

We would ask that any LGPS employers wishing to adopt the new disclosures early, or requiring illustrative figures in line with the new standard, should get in touch with the Administering Authority at an early stage to ensure that the relevant figures can be produced. On the assumption that prior year comparatives may be required for 2006/07 in due course for those not adopting early, we would encourage employers to consider commissioning these figures now rather than wait until 2008.

Following the July 2006 exercise we are aware that many colleges will be reviewing their approach to accounting under FRS17 (some have been able to persuade their auditors that they could account for the LGPS on a defined contribution basis). The change in emphasis in the amended standard may be the final nail in the coffin for defined contribution accounting for the LGPS. Any colleges in such a position may wish to consider the extent to which historic figures will be required well in advance of 31 July 2007.

PROPOSALS FOR A NEW REPORTING STATEMENT

The ASB has noted concerns expressed by commentators that the financial statements do not contain sufficient information to allow their users to adequately assess the risks arising from defined benefit schemes. The original FRED proposed that the compulsory disclosures under FRS 17 should be supplemented, as a matter of best practice, by additional disclosures reflecting the principles set out in a draft Reporting Statement.

Whilst this did not make it into this month's amendment, we expect a further announcement from the ASB in January.

The intention behind the proposals in the FRED is that those preparing accounts should review six stated disclosure principles, and extend the compulsory FRS 17 disclosures to an extent that is appropriate bearing in mind the company's exposure to risks and rewards arising from defined benefit schemes.

The six principles require that adequate disclosure is given on the following issues:

- the relationship between the company and the trustees (managers) of the defined benefit scheme, for example setting out any significant powers of the trustees (managers);
- sufficient information about the principal assumptions (including mortality rates) used to measure scheme liabilities to allow users of accounts to understand the inherent uncertainties affecting measurement;
- a sensitivity analysis for the principal assumptions, showing how the liabilities would have been affected by changes in each assumption;
- information to help understand the method of measurement—the projected unit method—used to measure the liabilities (this should include a statement of the cost of buying out benefits at the balance sheet date with a suitable insurer);
- information that enables users of financial statements to understand the funding obligations that the company has in relation to defined benefit schemes (this might include a summary of the funding principles that the company has agreed, the amount of additional contributions required to eliminate any deficit and the period over which these contributions may be paid, and information about the duration of the liabilities); and
- information that enables users of financial statements to evaluate the nature and extent of the risks and rewards arising from the assets held by the defined benefit schemes at the balance sheet date (this would include the expected rate

LOCAL GOVERNMENT PENSION SCHEME: CHANGES TO THE FRS17 DISCLOSURES

of return on individual asset classes held by the scheme).

As these additional disclosures would be best practice only and some of the details relate to the private sector funding environment, it is not yet clear what additional information LGPS employers might typically expect to disclose. We expect to issue a further briefing note once further details are available from the ASB.

AND FINALLY.....

The ASB is undertaking a long-term research project, with others, which is intended to completely re-evaluate accounting for defined benefit pension schemes in companies' financial statements. As a result, we can expect further changes to FRS17 in due course. This ongoing project was apparently the reason why the ASB did not take the opportunity to extend the amendments to other differences between FRS17 and IAS19 as some respondents to the FRED had suggested.

For further information, or to discuss any matter raised by the Briefing Note, please speak to your usual contact at Hymans Robertson LLP.

This *Briefing Note* is not intended to be a definitive analysis of the subject matter covered. It is not specific to the circumstances of any particular employer or pension scheme. The information contained herein is not intended to constitute advice and should not be considered a substitute for specific advice in relation to individual circumstances. Where the subject of this note involves legal issues you may wish to take legal advice. Hymans Robertson LLP accepts no liability for errors or omissions.

www.hymans.co.uk

Hymans Robertson LLP
One London Wall London EC2Y 5EA T 020 7082 6000 F 020 7082 6082
20 Waterloo Street Glasgow G2 6DB T 0141 566 7777 F 0141 566 7788
6th Floor 120 Edmund Street Birmingham B3 2ED T 0121 210 4333 F 0121 210 4343

Internationally Milliman Global

Hymans Robertson LLP and Hymans Robertson Financial Services LLP are authorised and regulated by the Financial Services Authority

© Hymans Robertson LLP