Deloitte.

Swiss pensions accounting under IFRS/US GAAP

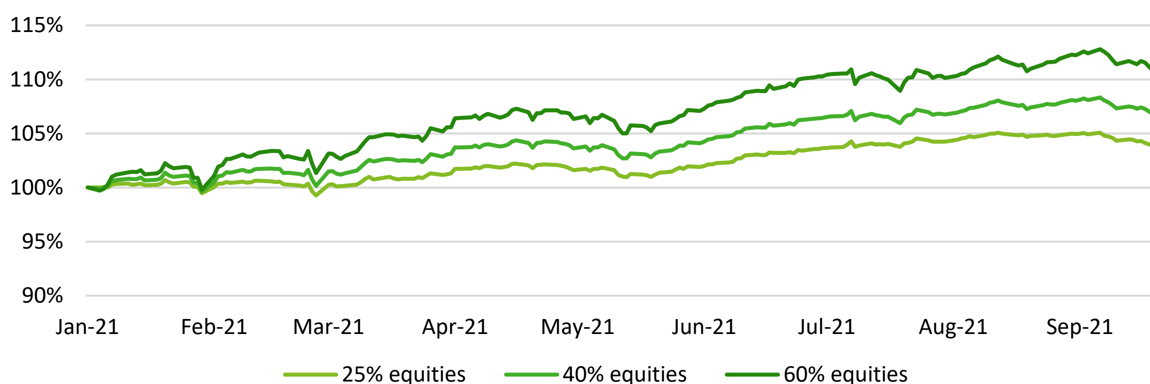
2021 Year-end briefing

Looking ahead to year-end | October 2021

Swiss pensions accounting—2021 year-end briefing

Financial factors – Asset returns and discount rates

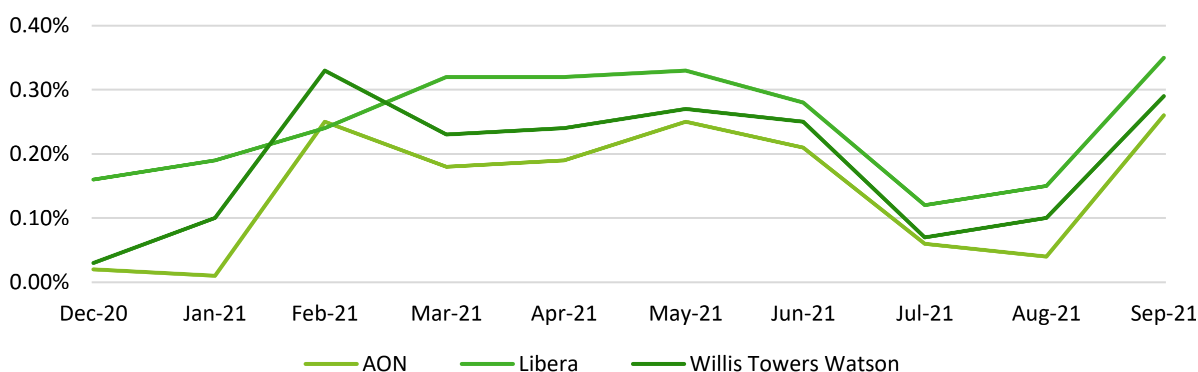
Due to strong asset performance and rises in discount rates, most companies can expect improvements in their balance sheets and next year's pensions expense.



Source: Pictet Asset Management

Swiss pension funds, and particularly those with larger allocations to growth assets, have experienced year to date returns in the range 3-10% (30 September 2021).

Companies with their own pension funds and those using uninsured collective foundations will benefit from these returns through reduced net pension liabilities. For companies using fully insured pension providers, the pension asset value is not linked to market asset prices and as such they will not benefit from these market returns in their financial reporting.



Source: Received from consultancies with permission to publish

Discount rates recommended by actuarial consultancies in Switzerland have increased by around 20-25bps year to date (30 September 2021). Other things being equal, this will reduce gross pension liabilities by around 3-4%.

Each of the consultancies in Switzerland has a different approach to setting their recommended discount rates. However, the range is relatively narrow and the year to date movements during the year are similar.

© 2021 Deloitte Consulting AG. All rights reserved.

Swiss pensions accounting—2021 year-end briefing

Demographic factors – New actuarial tables

The introduction of the new actuarial tables will have a favourable impact for the majority of companies, though less so for those who have made company-specific adjustments in the past.

Assumption	Summary of change	Typical impact
Mortality	Both current mortality probabilities and allowances for future longevity improvements have been updated	2-5% reduction in liabilities, depending on active/pensioner mix and the particulars of the assumption changes (see next slide)
Employee turnover	Average turnover probabilities at key ages have increased by 15% for males and 5% for females (age range 35-55)	1-2% reduction in active liabilities*
Disability	Average disability probabilities at key ages have decreased by 20% for both males and females (age range 35-55)	1-2% reduction in active liabilities*
Other	Various changes to marriage and family statistics	circa 1% reduction in active and pensioner liabilities

The impact of updating assumptions can depend significantly on individual company circumstances

*If company-specific adjustments have been made to these assumptions, we would expect these to be re-calibrated such that the impact on liabilities is close to zero.

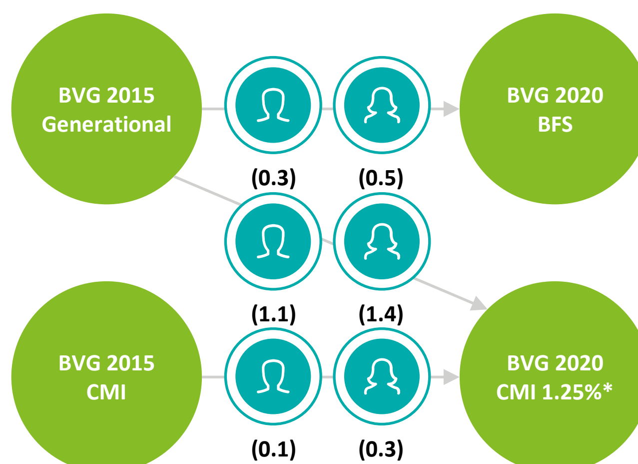
© 2021 Deloitte Consulting AG. All rights reserved.

Swiss pensions accounting—2021 year-end briefing

Demographic factors – New actuarial tables

The impact of applying the new mortality tables will depend significantly on what allowance has been made for future longevity improvements in the past, and what allowance will be made going forward.

Typical expected changes to life expectancies in years (65 year old; in years)



a 1.25% long term rate of improvement was market median practice for Swiss companies using CMI mortality in the past

Context

There are two components to a mortality assumption, the current probabilities of death and the rate at which these are expected to change in future.

When the BVG 2015 tables were released, only one approach to allowing for future longevity improvements was used in the market – the "Generational" approach. However, in the years following their publication, many actuarial firms began using the UK's "CMI" model (the model published by the UK's Continuous Mortality Investigation Bureau) on the basis that it was more sophisticated. Life expectancies, and consequently measured liabilities, were generally reduced when the CMI tables were applied.

When the BVG 2020 tables were released, they included both an updated version of the "Generational" approach (now called "BFS"; Bundesamt für Statistik) and the CMI tables.

Implications

The level of movement in liability following application of the new tables will depend on, in addition to other factors, what allowance was previously made for future improvements in longevity and what allowance will be made going forward. We expect the following scenarios to be the most common:

- "Generational to CMI" – these methodologies are fundamentally different from one another and the impact on liabilities will be relatively large.
- "Generational to BFS" or "CMI to CMI" – in these cases there is no fundamental change in methodology and the impact on liabilities will be lower.

We do not expect a significant number of companies to move from "CMI to BFS".

© 2021 Deloitte Consulting AG. All rights reserved.

Swiss pensions accounting—2021 year-end briefing

Common technical questions

On these pages we discuss common technical questions relating to Swiss pensions accounting. Answers have been generalised and simplified for ease of understanding.

Is defined benefit accounting always needed for Swiss plans?

Yes. Under both IFRS (IAS 19) and US GAAP (ASC 715) defined benefit accounting is always required for Swiss plans due to the guarantees which must be provided on the benefits by law.

This requirement also applies to so-called fully insured plans due to the fixed term nature of insurance contracts meaning they are not qualifying insurance policies under either accounting standard.

For companies that have implemented a so-called “1e” plan (that is, a pure defined contribution plan which is permitted for salaries above a certain threshold), this portion of the benefits may be accounted for as defined contribution, subject to certain requirements being met.

What is “risk sharing”?

Risk sharing refers to alternative methodologies which may be applied to IFRS calculations (but not US GAAP) to reflect that not all of the risk associated with providing pension benefits lies with the employer. Specifically, there are three methodology choices which are commonly referred to as “risk sharing”:

- “Risk Sharing 1” – adjusting gross liabilities to reflect that ongoing employee contributions will increase as the workforce ages, reducing the cost to the employer.
- “Risk Sharing 2.1” – making an allowance in the valuation for anticipated future reductions in conversion rates, beyond those currently set out in the plan’s regulations.
- “Risk Sharing 2.2” – if a pension plan’s financial position is not sustainable and additional contributions are expected to be necessary, the employer is only obliged to pay half of the contributions and can require that employees pay the remainder. These anticipated employee deficit financing contributions can effectively be valued to generate a negative liability which is offset from the gross liability.

Most companies made an accounting policy choice regarding Risk Sharing 1 when the revised IAS 19 standard became effective in 2013 and this is not generally revisited. There is a gradual trend towards companies applying Risk Sharing 2.1 and, to a far lesser degree, 2.2.

How do companies reflect that part of employees’ pension obligations relates to service at previous employer?

As accrued pension benefits transfer with employment, an employee’s hire date at their current employer is not a good reflection of the period over which the liability is being accrued.

Consequently, in most cases actuaries calculate a notional hire date by projecting backwards to determine the date at which an employee would theoretically have started work to arrive at their current savings account balance. This aspect of the calculations can result in some counterintuitive outcomes.

© 2021 Deloitte Consulting AG. All rights reserved.

Swiss pensions accounting—2021 year-end briefing

Common technical questions

On these pages we discuss common technical questions relating to Swiss pensions accounting. Answers have been generalised and simplified for ease of understanding.

Can insured death and disability benefits be excluded from the calculations (i.e., with no liability recorded)?

Not usually. The key factor in determining whether a benefit can be treated as insured for accounting purposes is whether or not the insurer retains responsibility for such benefits upon cancellation of the contract. In most cases this responsibility remains with the company.

Should the Traditional Unit Credit or Projected Unit Credit method be used?

In the majority of, but not all, cases the Projected Unit Credit method should be used.

Are there any issues for companies with a net pension asset position?

Under IFRS, companies may only record a net pension asset on their balance sheet to the extent that this represents economic value to the company. IFRIC 14 provides a specific set of criteria to determine whether there is economic value.

In the majority of, but not all, cases Swiss companies can fully reflect a net pension asset on their balance sheet.

Under US GAAP, there is no such limitation on net asset positions.

How should the pension plan asset value be determined for companies in collective foundations?

The general principle is that the plan asset value should be equal to the sum of:

- Savings capital for active employees
- The mathematical reserve held by the pension provider in respect of any pensioners that would transfer upon cancellation of the affiliation agreement
- Any prepaid contribution balances or accruals, and
- An adjustment to reflect the local statutory coverage ratio of the pension provider.

How should retirees be treated for companies in collective foundations?

The key test is whether retirees would remain with the existing collective foundation upon cancellation of the affiliation agreement (which links the company to the pension plan), or transfer to the replacement plan.

The wording of the affiliation agreement will inform the appropriate treatment and this varies across the various collective foundations in the market.

© 2021 Deloitte Consulting AG. All rights reserved.

Deloitte's pensions advisory offering

Contact details

Daniel Tonks
Director (Pensions)
Deloitte Consulting AG
ddtonks@deloitte.ch

Daniel leads Deloitte Switzerland's Pensions Advisory offering.

He began his pensions consulting career in the UK in 2007 before moving to Switzerland in 2011. Daniel is a Fellow of the Institute and Faculty of Actuaries (UK) and has a broad knowledge of the pensions systems in many countries where defined benefits are common, though with a particular focus on Switzerland and the UK.

He supports companies in dealing with the financing and accounting challenges which operating pension arrangements brings, both on a business-as-usual basis (i.e., regular annual reporting) and during times of changes (i.e., during M&A or restructuring activity).

© 2021 Deloitte Consulting AG. All rights reserved.

This publication has been written in general terms and we recommend that you obtain professional advice before acting or refraining from action on any of the contents of this publication. Deloitte Consulting AG accepts no liability for any loss occasioned to any person acting or refraining from action as a result of any material in this publication.

Deloitte Consulting AG is an affiliate of Deloitte NSE LLP, a member firm of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"). DTTL and each of its member firms are legally separate and independent entities. DTTL and Deloitte NSE LLP do not provide services to clients. Please see www.deloitte.com/ch/about to learn more about our global network of member firms.

© 2021 Deloitte Consulting AG. All rights reserved.