Chapter 14

IAS 19 Employee Benefits

Objective

The objective of this Standard is to prescribe the accounting and disclosure for employee benefits. The Standard requires an entity to recognize:

(a) a liability when an employee has provided service in exchange for employee benefits to be paid in the future; and

(b) an expense when the entity consumes the economic benefit arising from service provided by an employee in exchange for employee benefits.

Scope

This Standard shall be applied by an employer in accounting for all employee benefits, except those to which IFRS 2 Share-based Payment applies.

This Standard does not deal with reporting by employee benefit plans.

The employee benefits to which this Standard applies include those provided:

(a) under formal plans or other formal agreements between an entity and individual employees, groups of employees or their representatives;

(b) under legislative requirements, or through industry arrangements, whereby entities are required to contribute to national, state, industry or other multi-employer plans; or

(c) by those informal practices that give rise to a constructive obligation. Informal practices give rise to a constructive obligation where the entity has no realistic alternative but to pay employee benefits. An example of a constructive obligation is where a change in the entity's informal practices would cause unacceptable damage to its relationship with employees.

Employee benefits include:

(a) short-term employee benefits, such as the following, if expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related services:
  - (i) wages, salaries and social security contributions;
  - (ii) paid annual leave and paid sick leave;
  - (iii) profit-sharing and bonuses; and
  - (iv) non-monetary benefits (such as medical care, housing, cars and free or subsidized goods or services) for current employees;

(b) post-employment benefits, such as the following:
  - (i) Retirement benefits (eg pensions and lump sum payments on retirement); and
  - (ii) Other post-employment benefits, such as post-employment life insurance and post-employment medical care;

(c) other long-term employee benefits, such as the following:
  - (i) long-term paid absences such as long-service leave or sabbatical leave;
  - (ii) jubilee or other long-service benefits; and
  - (iii) long-term disability benefits; and

(d) termination benefits.

Definitions of employee benefits

Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees or for the termination of employment.

Short-term employee benefits are employee benefits (other than termination benefits) that are expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related service.

Post-employment benefits are employee benefits (other than termination benefits and short-term employee benefits) that are payable after the completion of employment.

Other long-term employee benefits are all employee benefits other than short-term employee benefits, post-employment benefits and termination benefits.

Termination benefits are employee benefits provided in exchange for the termination of an employee's employment as a result of either:

(a) an entity's decision to terminate an employee's employment before the normal retirement date; or

(b) an employee's decision to accept an offer of benefits in exchange for the termination of employment.

Definitions relating to classification of plans

Post-employment benefit plans are formal or informal arrangements under which an entity provides post-employment benefits for one or more employees.

Defined contribution plans are post-employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods.

Defined benefit plans are post-employment benefit plans other than defined contribution plans.

Multi-employer plans are defined contribution plans (other than state plans) or defined benefit plans (other than state plans) that:

(a) pool the assets contributed by various entities that are not under common control; and

(b) use those assets to provide benefits to employees of more than one entity, on the basis that contribution and benefit levels are determined without regard to the identity of the entity that employs the employees.

Definitions relating to the net defined benefit liability (asset)

The net defined benefit liability (asset) is the deficit or surplus, adjusted for any effect of limiting a net defined benefit asset to the asset ceiling.

The deficit or surplus is:

(a) the present value of the defined benefit obligation less

(b) the fair value of plan assets (if any).

The asset ceiling is the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

The present value of a defined benefit obligation is the present value, without deducting any plan assets, of expected future payments required to settle the obligation resulting from employee service in the current and prior periods.

Plan assets comprise:

(a) assets held by a long-term employee benefit fund; and

(b) qualifying insurance policies.

Assets held by a long-term employee benefit fund are assets (other than non-transferable financial instruments issued by the reporting entity) that:

(a) are held by an entity (a fund) that is legally separate from the reporting entity and exists solely to pay or fund employee benefits; and

(b) are available to be used only to pay or fund employee benefits, are not available to the reporting entity's own creditors (even in bankruptcy), and cannot be returned to the reporting entity, unless either:

    (i) the remaining assets of the fund are sufficient to meet all the related employee benefit obligations of the plan or the reporting entity; or

    (ii) the assets are returned to the reporting entity to reimburse it for employee benefits already paid.

A qualifying insurance policy is an insurance policy* issued by an insurer that is not a related party (as defined in IAS 24 Related Party Disclosures) of the reporting entity, if the proceeds of the policy:

(a) can be used only to pay or fund employee benefits under a defined benefit plan; and

(b) are not available to the reporting entity's own creditors (even in bankruptcy) and cannot be paid to the reporting entity, unless either:

(i) the proceeds represent surplus assets that are not needed for the policy to meet all the related employee benefit obligations; or

(ii) the proceeds are returned to the reporting entity to reimburse it for employee benefits already paid.

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction.

Definitions relating to defined benefit cost

Service cost comprises:

(a) current service cost, which is the increase in the present value of the defined benefit obligation resulting from employee service in the current period;

(b) past service cost, which is the change in the present value of the defined benefit obligation for employee service in prior periods, resulting from a plan amendment (the introduction or withdrawal of, or changes to, a defined benefit plan) or a curtailment (a significant reduction by the entity in the number of employees covered by a plan); and

(c) any gain or loss on settlement.

Net interest on the net defined benefit liability (asset) is the change during the period in the net defined benefit liability (asset) that arises from the passage of time.

Re-measurements of the net defined benefit liability (asset) comprise:

(a) actuarial gains and losses;

(b) the return on plan assets, excluding amounts included in net interest on the net defined benefit liability (asset); and

(c) any change in the effect of the asset ceiling, excluding amounts included in net interest on the net defined benefit liability (asset).

Actuarial gains and losses are changes in the present value of the defined benefit obligation resulting from:

(a) experience adjustments (the effects of differences between the previous actuarial assumptions and what has actually occurred); and

(b) the effects of changes in actuarial assumptions.

The return on plan assets is interest, dividends and other income derived from the plan assets, together with realized and unrealized gains or losses on the plan assets, less:

(a) any costs of managing plan assets; and

(b) any tax payable by the plan itself, other than tax included in the actuarial assumptions used to measure the present value of the defined benefit obligation.

A settlement is a transaction that eliminates all further legal or constructive obligations for part or all of the benefits provided under a defined benefit plan, other than a payment of benefits to, or on behalf of, employees that is set out in the terms of the plan and included in the actuarial assumptions.

Short-term employee benefits

Short-term employee benefits include items such as the following, if expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related services:

(a) wages, salaries and social security contributions;

(b) paid annual leave and paid sick leave;

(c) profit-sharing and bonuses; and

(d) non-monetary benefits (such as medical care, housing, cars and free or subsidized goods or services) for current employees.

Recognition and measurement

All short-term employee benefits

When an employee has rendered service to an entity during an accounting period, the entity shall recognize the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service:

(a) as a liability (accrued expense), after deducting any amount already paid. If the amount already paid exceeds the undiscounted amount of the benefits, an entity shall recognize that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund.

(b) as an expense, unless another IFRS requires or permits the inclusion of the benefits in the cost of an asset (see, for example, IAS 2 Inventories and IAS 16 Property, Plant and Equipment).

Short-term paid absences

An entity shall recognize the expected cost of short-term employee benefits in the form of **paid absences** as follows:

(a) in the case of accumulating paid absences, when the employees render service that increases their entitlement to future paid absences.

(b) in the case of non-accumulating paid absences, when the absences occur.

Profit-sharing and bonus plans

An entity shall recognize the expected cost of profit-sharing and bonus payments when and only when:

(a) the entity has a present legal or constructive obligation to make such payments as a result of past events; and

(b) a reliable estimate of the obligation can be made.

A present obligation exists when, and only when, the entity has no realistic alternative but to make the payments.

Disclosure

Although this Standard does not require specific disclosures about short-term employee benefits, other IFRSs may require disclosures. For example, IAS 24 requires disclosures about employee benefits for key management personnel. IAS 1 Presentation of Financial Statements requires disclosure of employee benefits expense.

Post-employment benefits

Distinction between defined contribution plans and defined benefit plans

Post-employment benefit plans are classified as either defined contribution plans or defined benefit plans, depending on the economic substance of the plan as derived from its principal terms and conditions.

Under defined contribution plans the entity's legal or constructive obligation is limited to the amount that it agrees to contribute to the fund. Thus, the amount of the post-employment benefits received by the employee is determined by the amount of contributions paid by an entity (and perhaps also the employee) to a post-employment benefit plan or to an insurance company, together with investment returns arising from the contributions. In consequence, actuarial risk (that benefits will be less than expected) and investment risk (that assets invested will be insufficient to meet expected benefits) fall, in substance, on the employee.

Under defined benefit plans:

(a) the entity's obligation is to provide the agreed benefits to current and former employees; and

(b) actuarial risk (that benefits will cost more than expected) and investment risk fall, in substance, on the entity. If actuarial or investment experience are worse than expected, the entity's obligation may be increased.

Multi-employer plans

An entity shall classify a multi-employer plan as a defined contribution plan or a defined benefit plan under the terms of the plan (including any constructive obligation that goes beyond the formal terms).

If an entity participates in a multi-employer defined benefit plan, it shall account for its proportionate share of the defined benefit obligation, plan assets and cost associated with the plan in the same way as for any other defined benefit plan.

However, when sufficient information is not available to use defined benefit accounting for a multi-employer defined benefit plan, an entity shall:

(a) account for the as if it were a defined contribution plan; and

(b) disclose the information required by this IAS.

State plans

An entity shall account for a state plan in the same way as for a multi-employer plan.

State plans are established by legislation to cover all entities (or all entities in a particular category, for example, a specific industry) and are operated by national or local government or by another body (for example, an autonomous agency created specifically for this purpose) that is not subject to control or influence by the reporting entity. Some plans established by an entity provide both compulsory benefits, as a substitute for benefits that would otherwise be covered under a state plan, and additional voluntary benefits. Such plans are not state plans.

State plans are characterized as defined benefit or defined contribution, depending on the entity's obligation under the plan. Many state plans are funded on a pay-as-you-go basis: contributions are set at a level that is expected to be sufficient to pay the required benefits falling due in the same period; future benefits earned during the current period will be paid out of future contributions. Nevertheless, in most state plans the entity has no legal or constructive obligation to pay those future benefits:

its only obligation is to pay the contributions as they fall due and if the entity ceases to employ members of the state plan, it will have no obligation to pay the benefits earned by its own employees in previous years. For this reason, state plans are normally defined contribution plans. However, when a state plan is a defined benefit plan an entity applies accounting for defined benefit plans.

Insured benefits

An entity may pay insurance premiums to fund a post-employment benefit plan. The entity shall treat such a plan as a defined contribution plan unless the entity will have (either directly or indirectly through the plan) a legal or constructive obligation either:

(a) to pay the employee benefits directly when they fall due; or

(b) to pay further amounts if the insurer does not pay all future employee benefits relating to employee service in the current and prior periods.

If the entity retains such a legal or constructive obligation, the entity shall treat the plan as a defined benefit plan.

The benefits insured by an insurance policy need not have a direct or automatic relationship with the entity's obligation for employee benefits.

Post-employment benefit plans involving insurance policies are subject to the same distinction between accounting and funding as other funded plans.

Where an entity funds a post-employment benefit obligation by contributing to an insurance policy under which the entity (either directly, indirectly through the plan, through the mechanism for setting future premiums or through a related party relationship with the insurer) retains a legal or constructive obligation, the payment of the premiums does not amount to a defined contribution arrangement.

It follows that the entity:

(a) Accounts for a qualifying insurance policy as a plan asset; and

(b) Recognizes other insurance policies as reimbursement rights.

Where an insurance policy is in the name of a specified plan participant or a group of plan participants and the entity does not have any legal or constructive obligation to cover any loss on the policy, the entity has no obligation to pay benefits to the employees and the insurer has sole responsibility for paying the benefits. The payment of fixed premiums under such contracts is, in substance, the settlement of the employee benefit obligation, rather than an investment to meet the obligation.

Consequently, the entity no longer has an asset or a liability. Therefore, an entity treats such payments as contributions to a defined contribution plan.

Post-employment benefits: defined contribution plans

Accounting for defined contribution plans is straightforward because the reporting entity's obligation for each period is determined by the amounts to be contributed for that period. Consequently, no actuarial assumptions are required to measure the obligation or the expense and there is no possibility of any actuarial gain or loss. Moreover, the obligations are measured on an undiscounted basis, except where they are not expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related service.

Recognition and measurement

When an employee has rendered service to an entity during a period, the entity shall recognize the contribution payable to a defined contribution plan in exchange for that service:

(a) as a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the end of the reporting period, an entity shall recognize that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or cash refund.

(b) as an expense, unless another IFRS requires or permits the inclusion of the contribution in the cost of an asset.

When contributions to a defined contribution plan are not expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related service, they shall be discounted using the discount rate specified under this IAS.

Disclosure

An entity shall disclose the amount recognized as an expense for defined contribution plans. Where required by IAS 24 an entity discloses information about contributions to defined contribution plans for key management personnel.

Post-employment benefits: defined benefit plans

Accounting for defined benefit plans is complex because actuarial assumptions are required to measure the obligation and the expense and there is a possibility of actuarial gains and losses. Moreover, the obligations are measured on a discounted basis because they may be settled many years after the employees render the related service.

Recognition and measurement

Defined benefit plans may be unfunded, or they may be wholly or partly funded by contributions by an entity, and sometimes its employees, into an entity, or fund, that is legally separate from the reporting entity and from which the employee benefits are paid. The payment of funded benefits when they fall due depends not only on the financial position and the investment performance of the fund but also on an entity's ability, and willingness, to make good any shortfall in the fund's assets.

Therefore, the entity is, in substance, underwriting the actuarial and investment risks associated with the plan. Consequently, the expense recognized for a defined benefit plan is not necessarily the amount of the contribution due for the period.

Accounting by an entity for defined benefit plans involves the following steps:

(a) determining the deficit or surplus. This involves:

 (i) using an actuarial technique, the projected unit credit method, to make a reliable estimate of the ultimate cost to the entity of the benefit that employees have earned in return for their service in the current and prior periods. This requires an entity to determine how much benefit is attributable to the current and prior periods and to make estimates (actuarial assumptions) about demographic variables (such as employee turnover and mortality) and financial variables (such as future increases in salaries and medical costs) that will affect the cost of the benefit.

 (ii) discounting that benefit in order to determine the present value of the defined benefit obligation and the current service cost.

 (iii) deducting the fair value of any plan assets from the present value of the defined benefit obligation.

(b) determining the amount of the net defined benefit liability (asset) as the amount of the deficit or surplus determined in (a), adjusted for any effect of limiting a net defined benefit asset to the asset ceiling.
(c) determining amounts to be recognized in profit or loss:
   (i) current service cost.
   (ii) any past service cost and gain or loss on settlement.
   (iii) net interest on the net defined benefit liability (asset).
(d) determining the re-measurements of the net defined benefit liability (asset), to be recognized in other comprehensive income, comprising:
   (i) actuarial gains and losses;
   (ii) return on plan assets, excluding amounts included in net interest on the net defined benefit liability (asset); and
   (iii) any change in the effect of the asset ceiling excluding amounts included in net interest on the net defined benefit liability (asset).

Where an entity has more than one defined benefit plan, the entity applies these procedures for each material plan separately.

An entity shall determine the net defined benefit liability (asset) with sufficient regularity that the amounts recognized in the financial statements do not differ materially from the amounts that would be determined at the end of the reporting period.

Accounting for the constructive obligation

An entity shall account not only for its legal obligation under the formal terms of a defined benefit plan, but also for any constructive obligation that arises from the entity's informal practices. Informal practices give rise to a constructive obligation where the entity has no realistic alternative but to pay employee benefits. An example of a constructive obligation is where a change in the entity's informal practices would cause unacceptable damage to its relationship with employees.

Statement of financial position

An entity shall recognize the net defined benefit liability (asset) in the statement of financial position.

When an entity has a surplus in a defined benefit plan, it shall measure the net defined benefit asset at the lower of:

(a) the surplus in the defined benefit plan; and
(b) the asset ceiling, determined using the discount rate specified in this IAS.

A net defined benefit asset may arise where a defined benefit plan has been overfunded or where actuarial gains have arisen. An entity recognizes a net defined benefit asset in such cases because:

(a) the entity controls a resource, which is the ability to use the surplus to generate future benefits;
(b) that control is a result of past events (contributions paid by the entity and service rendered by the employee); and
(c) future economic benefits are available to the entity in the form of a reduction in future contributions or a cash refund, either directly to the entity or indirectly to another plan in deficit. The asset ceiling is the present value of those future benefits.

Recognition and measurement: present value of defined benefit obligations and current service cost

The ultimate cost of a defined benefit plan may be influenced by many variables, such as final salaries, employee turnover and mortality, employee contributions and medical cost trends. The ultimate cost of the plan is uncertain and this uncertainty is likely to persist over a long period of time. In order to measure the present value of the post-employment benefit obligations and the related current service cost, it is necessary:

(a) to apply an actuarial valuation method;
(b) to attribute benefit to periods of service; and
(c) to make actuarial assumptions.

Actuarial valuation method

An entity shall use the projected unit credit method to determine the present value of its defined benefit obligations and the related current service cost and, where applicable, past service cost.

The projected unit credit method (sometimes known as the accrued benefit method pro-rated on service or as the benefit/years of service method) sees each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation.

An entity discounts the whole of a post-employment benefit obligation, even if part of the obligation is expected to be settled before twelve months after the reporting period.

Attributing benefit to periods of service

In determining the present value of its defined benefit obligations and the related current service cost and, where applicable, past service cost, an entity shall attribute benefit to periods of service under the plan's benefit formula. However, if an employee's service in later years will lead to a materially higher level of benefit than in earlier years, an entity shall attribute benefit on a straight-line basis from:

(a) the date when service by the employee first leads to benefits under the plan (whether or not the benefits are conditional on further service) until

(b) the date when further service by the employee will lead to no material amount of further benefits under the plan, other than from further salary increases.

The projected unit credit method requires an entity to attribute benefit to the current period (in order to determine current service cost) and the current and prior periods (in order to determine the present value of defined benefit obligations). An entity attributes benefit to periods in which the obligation to provide post-employment benefits arises. That obligation arises as employees render services in return for post-employment benefits that an entity expects to pay in future reporting periods. Actuarial techniques allow an entity to measure that obligation with sufficient reliability to justify recognition of a liability.

Actuarial assumptions

Actuarial assumptions shall be unbiased and mutually compatible.

Actuarial assumptions are an entity's best estimates of the variables that will determine the ultimate cost of providing post-employment benefits.

Actuarial assumptions comprise:

(a) **demographic assumptions** about the future characteristics of current and former employees (and their dependants) who are eligible for benefits. Demographic assumptions deal with matters such as:
    (i) mortality (see paragraphs 81 and 82);
    (ii) rates of employee turnover, disability and early retirement;
    (iv) the proportion of plan members with dependants who will be eligible for benefits;
    (iv) the proportion of plan members who will select each form of payment option available under the plan terms; and
    (v) claim rates under medical plans.

(b) **financial assumptions**, dealing with items such as:
    (i) the discount rate;
    (ii) benefit levels, excluding any cost of the benefits to be met by employees, and future salary;
    (v) in the case of medical benefits, future medical costs, including claim handling costs (ie the costs that will be incurred in processing and resolving claims, including legal and adjuster's fees); and
    (vi) taxes payable by the plan on contributions relating to service before the reporting date or on benefits resulting from that service.

Actuarial assumptions are unbiased if they are neither imprudent nor excessively conservative.

Actuarial assumptions are mutually compatible if they reflect the economic relationships between factors such as inflation, rates of salary increase and discount rates. For example, all assumptions that depend on a particular inflation level (such as assumptions about interest rates and salary and benefit increases) in any given future period assume the same inflation level in that period.

Actuarial assumptions: mortality

An entity shall determine its mortality assumptions by reference to its best estimate of the mortality of plan members both during and after employment.

Actuarial assumptions: discount rate

The rate used to discount post-employment benefit obligations (both funded and unfunded) shall be determined by reference to market yields at the end of the reporting period on high quality corporate bonds. In countries where there is no deep market in such bonds, the market yields (at the end of the reporting period) on government bonds shall be used. The currency and term of the corporate bonds or government bonds shall be consistent with the currency and estimated term of the post-employment benefit obligations.

Actuarial assumptions: salaries, benefits and medical costs

An entity shall measure its defined benefit obligations on a basis that reflects:

(a) the benefits set out in the terms of the plan (or resulting from any constructive obligation that goes beyond those terms) at the end of the reporting period;

(b) any estimated future salary increases that affect the benefits payable;

(c) the effect of any limit on the employer's share of the cost of the future benefits;

(d) contributions from employees or third parties that reduce the ultimate cost to the entity of those benefits; and

(e) estimated future changes in the level of any state benefits that affect the benefits payable under a defined benefit plan, if, and only if, either:

  (i) those changes were enacted before the end of the reporting period; or

  (ii) historical data, or other reliable evidence, indicate that those state benefits will change in some predictable manner, for example, in line with future changes in general price levels or general salary levels.

Past service cost and gains and losses on settlement

Before determining past service cost, or a gain or loss on settlement, an entity shall re-measure the net defined benefit liability (asset) using the current fair value of plan assets and current actuarial assumptions (including current market interest rates and other current market prices) reflecting the benefits offered under the plan before the plan amendment, curtailment or settlement.

Past service cost

Past service cost is the change in the present value of the defined benefit obligation resulting from a plan amendment or curtailment.

An entity shall recognize past service cost as an expense at the earlier of the following dates:

(a) when the plan amendment or curtailment occurs; and

(b) when the entity recognizes related restructuring costs or termination benefits.

An entity shall recognize a gain or loss on the settlement of a defined benefit plan when the settlement occurs.

Recognition and measurement: plan assets

Fair value of plan assets

The fair value of any plan assets is deducted from the present value of the defined benefit obligation in determining the deficit or surplus. When no market price is available, the fair value of plan assets is estimated, for example, by discounting expected future cash flows using a discount rate that reflects both the risk associated with the plan assets and the maturity or expected disposal date of those assets (or, if they have no maturity, the expected period until the settlement of the related obligation).

Plan assets exclude unpaid contributions due from the reporting entity to the fund, as well as any non-transferable financial instruments issued by the entity and held by the fund. Plan assets are reduced by any liabilities of the fund that do not relate to employee benefits, for example, trade and other payables and liabilities resulting from derivative financial instruments.

Where plan assets include qualifying insurance policies that exactly match the amount and timing of some or all of the benefits payable under the plan, the fair value of those insurance policies is deemed to be the present value of the related obligations (subject to any reduction required if the amounts receivable under the insurance policies are not recoverable in full).

Reimbursements

When and only when, it is virtually certain that another party will reimburse some or all of the expenditure required to settle a defined benefit obligation, an entity shall:

(a) recognize its right to reimbursement as a separate asset. The entity shall measure the asset at fair value.

(b) disaggregate and recognize changes in the fair value of its right to reimbursement in the same way as for changes in the fair value of plan assets. The components of defined benefit cost recognized in accordance with paragraph 120 may be recognized net of amounts relating to changes in the carrying amount of the right to reimbursement.

Components of defined benefit cost

An entity shall recognize the components of defined benefit cost, except to the extent that another IFRS requires or permits their inclusion in the cost of an asset, as follows:

(a) service cost in profit or loss;

(b) net interest on the net defined benefit liability (asset) in profit or loss; and

(c) re-measurements of the net defined benefit liability (asset) in other comprehensive income.

Other IFRSs require the inclusion of some employee benefit costs within the cost of assets, such as inventories and property, plant and equipment. Any post-employment benefit costs included in the cost of such assets include the appropriate proportion of the components listed above.

Re-measurements of the net defined benefit liability (asset) recognized in other comprehensive income shall not be reclassified to profit or loss in a subsequent period. However, the entity may transfer those amounts recognized in other comprehensive income within equity.

Net interest on the net defined benefit liability (asset)

Net interest on the net defined benefit liability (asset) shall be determined by multiplying the net defined benefit liability (asset) by the discount rate, both as determined at the start of the annual reporting period, taking account of any changes in the net defined benefit liability (asset) during the period as a result of contribution and benefit payments.

Net interest on the net defined benefit liability (asset) can be viewed as comprising interest income on plan assets, interest cost on the defined benefit obligation and interest on the effect of the asset ceiling

Interest income on plan assets is a component of the return on plan assets, and is determined by multiplying the fair value of the plan assets by the discount rate, both as determined at the start of the annual reporting period, taking account of any changes in the plan assets held during the period as a result of contributions and benefit payments. The difference between the interest income on plan assets and the return on plan assets is included in the re-measurement of the net defined benefit liability (asset).

Interest on the effect of the asset ceiling is part of the total change in the effect of the asset ceiling, and is determined by multiplying the effect of the asset ceiling by the discount rate, both as determined at the start of the annual reporting period. The difference between that amount and the total change in the effect of the asset ceiling is included in the re-measurement of the net defined benefit liability (asset).

Re-measurements of the net defined benefit liability (asset)

Re-measurements of the net defined benefit liability (asset) comprise:

(a) Actuarial gains and losses;
(b) The return on plan assets, excluding amounts included in net interest on the net defined benefit liability (asset); and
(c) Any change in the effect of the asset ceiling, excluding amounts included in net interest on the net defined benefit liability (asset).

Actuarial gains and losses result from increases or decreases in the present value of the defined benefit obligation because of changes in actuarial assumptions and experience adjustments.

Causes of actuarial gains and losses include, for example:

(a) Unexpectedly high or low rates of employee turnover, early retirement or mortality or of increases in salaries, benefits (if the formal or constructive terms of a plan provide for inflationary benefit increases) or medical costs;
(b) The effect of changes to assumptions concerning benefit payment options;
(c) The effect of changes in estimates of future employee turnover, early retirement or mortality or of increases in salaries, benefits (if the formal or constructive terms of a plan provide for inflationary benefit increases) or medical costs; and
(d) The effect of changes in the discount rate.

Actuarial gains and losses do not include changes in the present value of the defined benefit obligation because of the introduction, amendment, curtailment or settlement of the defined benefit plan, or changes to the benefits payable under the defined benefit plan. Such changes result in past service cost or gains or losses on settlement.

In determining the return on plan assets, an entity deducts the costs of managing the plan assets and any tax payable by the plan itself, other than tax included in the actuarial assumptions used to measure the defined benefit obligation. Other administration costs are not deducted from the return on plan assets.

Presentation

Offset

An entity shall offset an asset relating to one plan against a liability relating to another plan when, and only when, the entity:

(a) has a legally enforceable right to use a surplus in one plan to settle obligations under the other plan; and
(b) intends either to settle the obligations on a net basis, or to realize the surplus in one plan and settle its obligation under the other plan simultaneously.

Current/non-current distinction

Some entities distinguish current assets and liabilities from non-current assets and liabilities. This Standard does not specify whether an entity should distinguish current and non-current portions of assets and liabilities arising from post-employment benefits.

Components of defined benefit cost

IAS requires an entity to recognize service cost and net interest on the net defined benefit liability (asset) in profit or loss. This Standard does not specify how an entity should present service cost and net interest on the net defined benefit liability (asset). An entity presents those components in accordance with IAS 1.

Disclosure

An entity shall disclose information that:

(a) explains the characteristics of its defined benefit plans and risks associated with them;
(b) identifies and explains the amounts in its financial statements arising from its defined benefit plans; and
(c) describes how its defined benefit plans may affect the amount, timing and uncertainty of the entity's future cash flows.

Explanation of amounts in the financial statements

An entity shall provide reconciliation from the opening balance to the closing balance for each of the following, if applicable:

(a) the net defined benefit liability (asset), showing separate reconciliations for:
    (i) plan assets.

(ii) the present value of the defined benefit obligation.
(iii) the effect of the asset ceiling.

(b) any reimbursement rights. An entity shall also describe the relationship between any reimbursement right and the related obligation.

Other long-term employee benefits

Other long-term employee benefits include items such as the following, if not expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related service:

(a) long-term paid absences such as long-service or sabbatical leave;
(b) jubilee or other long-service benefits;
(c) long-term disability benefits;
(d) profit-sharing and bonuses; and
(e) deferred remuneration.

The measurement of other long-term employee benefits is not usually subject to the same degree of uncertainty as the measurement of post-employment benefits. For this reason, this Standard requires a simplified method of accounting for other long-term employee benefits.

Unlike the accounting required for post-employment benefits, this method does not recognize re-measurements in other comprehensive income.

Recognition and measurement

For other long-term employee benefits, an entity shall recognize the net total of the following amounts in profit or loss, except to the extent that another IFRS requires or permits their inclusion in the cost of an asset:

(a) service cost;
(b) net interest on the net defined benefit liability (asset); and
(c) re-measurements of the net defined benefit liability (asset)

Disclosure

Although this Standard does not require specific disclosures about other long-term employee benefits, other IFRSs may require disclosures.

For example, IAS 24 requires disclosures about employee benefits for key management personnel. IAS 1 requires disclosure of employee benefits expense.

Termination benefits

This Standard deals with termination benefits separately from other employee benefits because the event that gives rise to an obligation is the termination of employment rather than employee service. Termination benefits result from either an entity's decision to terminate the employment or an employee's decision to accept an entity's offer of benefits in exchange for termination of employment.

Termination benefits do not include employee benefits resulting from termination of employment at the request of the employee without an entity's offer, or as a result of mandatory retirement requirements, because those benefits are post-employment benefits.

Some entities provide a lower level of benefit for termination of employment at the request of the employee (in substance, a post-employment benefit) than for termination of employment at the request of the entity.

The difference between the benefit provided for termination of employment at the request of the employee and a higher benefit provided at the request of the entity is a termination benefit.

The form of the employee benefit does not determine whether it is provided in exchange for service or in exchange for termination of the employee's employment. Termination benefits are typically lump sum payments, but sometimes also include:

(a) enhancement of post-employment benefits, either indirectly through an employee benefit plan or directly.

(b) salary until the end of a specified notice period if the employee renders no further service that provides economic benefits to the entity.

Indicators that an employee benefit is provided in exchange for services include the following:

(a) the benefit is conditional on future service being provided (including benefits that increase if further service is provided).
(b) the benefit is provided in accordance with the terms of an employee benefit plan.

Recognition

An entity shall recognize a liability and expense for termination benefits at the earlier of the following dates:

(a) when the entity can no longer withdraw the offer of those benefits; and
(b) when the entity recognizes costs for a restructuring that is within the scope of IAS 37 and involves the payment of termination benefits.

For termination benefits payable as a result of an employee's decision to accept an offer of benefits in exchange for the termination of employment, the time when an entity can no longer withdraw the offer of termination benefits is the earlier of:

(a) when the employee accepts the offer; and
(b) when a restriction (eg a legal, regulatory or contractual requirement or other restriction) on the entity's ability to withdraw the offer takes effect. This would be when the offer is made, if the restriction existed at the time of the offer.

For termination benefits payable as a result of an entity's decision to terminate an employee's employment, the entity can no longer withdraw the offer when the entity has communicated to the affected employees a plan of termination meeting all of the following criteria:

(a) Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made.
(b) The plan identifies the number of employees whose employment is to be terminated, their job classifications or functions and their locations (but the plan need not identify each individual employee) and the expected completion date.
(c) The plan establishes the termination benefits that employees will receive in sufficient detail that employees can determine the type and amount of benefits they will receive when their employment is terminated.

Measurement

An entity shall measure termination benefits on initial recognition, and shall measure and recognize subsequent changes, in accordance with the nature of the employee benefit, provided that if the termination benefits are an enhancement to post-employment benefits, the entity shall apply the requirements for post-employment benefits. Otherwise:

(a) if the termination benefits are expected to be settled wholly before twelve months after the end of the annual reporting period in which the termination benefit is recognized, the entity shall apply the requirements for short-term employee benefits.
(b) if the termination benefits are not expected to be settled wholly before twelve months after the end of the annual reporting period, the entity shall apply the requirements for other long-term employee benefits.

Disclosure

Although this Standard does not require specific disclosures about termination benefits, other IFRSs may require disclosures. For example, IAS 24 requires disclosures about employee benefits for key management personnel. IAS 1 requires disclosure of employee benefits expense.

Transition and effective date

An entity shall apply this Standard for annual periods beginning on or after 1 January 2013. Earlier application is permitted. If an entity applies this Standard for an earlier period, it shall disclose that fact.

An entity shall apply this Standard retrospectively, in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors, except that:

(a) An entity need not adjust the carrying amount of assets outside the scope of this Standard for changes in employee benefit costs that were included in the carrying amount before the date of initial application. The date of initial application is the beginning of the earliest prior period presented in the first financial statements in which the entity adopts this Standard.

(b) In financial statements for periods beginning before 1 January 2014, an entity need not present comparative information.

E-1

An entity has 100 employees, who are each entitled to five working days of paid sick leave for each year. Unused sick leave may be carried forward for one calendar year. Sick leave is taken first out of the current year's entitlement and then out of any balance brought forward from the previous. At 30 December 20X1, the average unused entitlement is two days per employee. The entity expects, based on past experience, which is expected to continue, that 92 employees will take no more than five days of paid sick leave in 20X2 and that the remaining eight employees will take an average of six and a half days each. The entity expects that it will pay an additional 12 days of sick pay as a result of the unused entitlement that has accumulated at 31 December 20X1 (one and a half days each, for eight employees).

E-2

A profit-sharing plan requires an entity to pay a specified proportion of its net profit for the year to employees who serve throughout the year. If no employees leave during the year, the total profit-sharing payments for the year will be 3% of net profit. The entity estimates that staff turnover will reduce the payments to 2.5% of net profit.

Post Employment Benefit Plans

E-1

A defined benefit plan has the following characteristics:

	Rs.
Present value of the obligation	1,100
Fair value of plan assets	1,190
Unrecognized actuarial losses	110
Unrecognized past service cost	70
Unrecognized increase in the liability on initial adoption of the Standard	50
Present value of available future refunds and reductions in future contributions	90

Required: - Determine the amount of asset to be recognized under IAS-19?

E-2

A lump sum benefit is payable on termination of service and equal to 1% of final salary for each year of service. The salary in year 1 is 10,000 and is assumed to increase at 7% (compound) each year. The discount rate used is 10% per annum.

Required: - Determine the amounts chargeable to each of years 1 to 5?

E-3

An entity operates a pension plan that provides a pension of 2% of final salary for each year of service. The benefits become vested after five years of service. On 1 January 20X5 the entity improves the pension to 2.5% of final salary for each year of service starting from 1 January 20X1. At the date of the improvement, the present value of the additional benefits for service from 1 January 20X1 to 1 January 20X5 is as follows:

	Rs.
Employees with more than five years' service at 1/1/X5	150
Employees with less than five years' service at 1/1/X5 (average period until vesting: three years)	120
	270

Required: - State the accounting treatment for past service cost?

E-4

At 1 January 20X1, the fair value of plan assets was 10,000 and net cumulative unrecognized actuarial gains were 760. On 30 June 20X1, the plan paid benefits of 1,900 and received contributions of 4,900. At 31 December 20X1, the fair value of plan assets was 15,000 and the present value of the defined benefit obligation was 14,792. Actuarial losses on the obligation for 20X1 were 60.

At 1 January 20X1, the reporting entity made the following estimates, based on market prices at that date:

	%
Interest and dividend income, after tax payable by the fund	9.25
Realized and unrealized gains on plan assets (after tax)	2.00
Administration costs	(1.00)
	10.25

Required: - Calculate the expected and actual return on plan assets, calculate any actuarial gain/loss and give appropriate accounting treatment?

E-5

An entity discontinues a business segment and employees of the discontinued segment will earn no further benefits. This is a curtailment without a settlement. Using current actuarial assumptions immediately before the curtailment, the entity has a defined benefit obligation with a net present value of 1,000, plan assets with a fair value of 820 and net cumulative un-recognized actuarial gains of 50. The entity had first adopted the Standard one-year before. This increased the net liability by 100, which the entity chose to recognize over five years. The curtailment reduces the net present value of the obligation by 100 to 900.

Required: - Show the required treatment of curtailment?

Comprehensive example

The following information is given about a funded defined benefit plan. To keep interest computations simple, all transactions are assumed to occur at the year-end. The present value of the obligation and the fair value of the plan assets were both 1,000 at 1 January 20X1. Net cumulative unrecognized actuarial gains at that date were 140.

	20X1	**20X2**	**20X3**
Discount rate at start of year	10 %	9 %	8 %
Expected rate of return on plan assets at start of year	12%	11.1%	10.3%
Current cost	130	140	150
Benefits paid	150	180	190
Contributions paid	90	100	110
Present value of obligation at 31 December	1,141	1,197	1,295
Fair value of plan assets at 31 December	1,092	1,109	1,093

In 20X2, the plan was amended to provide additional benefits with effect from 1 January 20X2. The present value as at 1 January 20X2 of additional benefits for employee service before 1 January 20X2 was 50 for vested benefits and 30 for non-vested benefits. As at 1 January 20X2, the entity estimated that the average period until the non-vested benefits would become vested was three years.

Required: - Show how the entity will account for the plan in all its accounting years?

PAST PAPERS

Question # 1

A, a public limited company, operates a defined benefit plan. A full actuarial valuation by an independent actuary revealed that the value of the liability at 31 May 2000 was Rs.1,500 million. This was updated to 31 May 2001 by the actuary and the value of the liability at that date was Rs. 2,000 million. The scheme assets comprised mainly bonds and equities and the fair value of these assets was as follows:

	31 May 2000	31 May 2001
	Rs.m	**Rs.m**
Fixed interest and index linked bonds	380	600
Equities	1,300	1,900
Other investments	290	450
	1,970	2,950

The scheme had been altered during the year with improved benefits arising for the employees and this had been taken into account by the actuaries. The increase in the actuarial liability in respect of employee service in prior periods was Rs.25 million (past service cost). The increase in the actuarial liability resulting from employee service in the current period was Rs.70 million (current service cost). The company had not recognized any net actuarial gain or loss in the income statement to date.

The company had paid contributions of Rs.60 million to the scheme during the period. The company expects its return on the scheme assets at 31 May 2001 to be Rs.295 million and the interest on pension liabilities to be Rs.230 million.

The average expected remaining working lives of the employees is 10 years and the net cumulative unrecognized gains at 1 June 2000 were Rs.247 million.

Required:

Calculate the amount which will be shown as the net plan asset in the balance sheet of A as at 31 May 2001, showing a reconciliation of the movement in the plan surplus during the year and a statement of those amounts which would be charged to operating profit. (Candidates should utilize IAS19 .Employee Benefits, in answering the question.)

Question # 2

Marshal Fertilizer Company Limited, a listed company, operates a funded gratuity scheme for its employees. Following relevant information has been extracted from the actuarial reports:

	June 30, 2007	**June 30, 2006**
	Rs. million	**Rs. million**
Present value of defined benefit obligations	900	600
Fair value of plan assets	750	570
Current service cost for the year	25	22
Contributions paid during the year	15	14
Benefits paid during the year	17	15
Net cumulative unrecognized gains		90
Expected return on plan assets	8%	8%
Discount rate for plan liabilities	10%	10%

Required:

(a) Compute the amounts which need to be reported in the Balance Sheet and the Profit and Loss Account of Marshal Fertilizer Company Limited for the year ended June 30, 2007.

(b) Prepare the movement schedule of net cumulative unrecognized gains / (losses) for the year ended June 30, 2007. **(13)**

Question # 3

Savage, a public limited company operates a funded defined benefit plan for its employees. The plan provides a pension of 1% of the final salary for each year of service. The cost for the year is determined is determined using the projected unit credit method. This reflects service rendered to the dates of valuation of the plan and incorporates actuarial assumptions primarily regarding discount rates, which are based on the market yields of high quality corporate bonds. The expected average remaining working lives of the employees is twelve years.

The directors have provided the following information about the defined benefit plan for the current year (year ended October 31, 20X5)

a) The actuarial cost of providing benefits in respect of employees' service for the year to October 31, 20X5 was Rs. 40 million. This is the present value of the pension benefits earned by the employees in the year.

b) The pension benefits paid to former employees in the year were Rs. 42 million.

c) Savage should have paid contribution to the fund of Rs. 28 million. Because of cash flow problems Rs. 8 million of this amount has not been paid at the financial year end of October 31, 20X5.

d) The present value of the obligation to provide benefits to current and former employees was Rs. 3,000 million at October 31, 20X4 and Rs. 3,375 million at October 31, 20X5.

e) The fair value of the plan assets was Rs. 2,900 million at October 31, 20X4 and Rs. 3,170 million (including the contributions owed by Savage) at October 31, 20X5. The actuarial gains recognized at October 31, 20X4 were Rs. 336 million.

With effect from November 01, 20X4, the company had amended the plan so that the employees were now provided with an increased entitlement. The benefits became vested and the actuarial computed that the present value of the cost of these benefits at November 01, 20X4 was Rs. 125 million. The discount rates and expected rates of return on the plan assets were as follows: -

	31-10-X4	**31-10-X5**
	%	**%**
Discount rate	6	7
Expected rate of return on plan assets	8	9

The company has recognized actuarial gains and losses in profit or loss up to October 31, 20X4 but now wishes to recognize such gains and losses outside profit and loss account in a statement of recognized income and expense.

Required: -

a) Show the amounts which will be recognized in the balance sheet, income statement and the statement of recognized income and expenses of Savage for the year ended October 31, 20X5 under IAS -19 and the movement in the net liability in the balance sheet. (Your calculations should show the changes in the present value of the obligation and the fair value of the plan assets during the year. Ignore any deferred taxation effects and assume that pension benefits and the contribution paid were settled at October 31, 20X5.) (21 marks)

b) Explain how the non-payment of contributes and the change in the pension benefits should be treated in the financial statements of Savage for the year ended October 31, 20X5. (4 marks)

Question # 4

Galaxy Textiles Limited (GTL) operates a funded gratuity scheme for all its employees. Contributions to the scheme are made on the basis of annual actuarial valuation. The following relevant information has been extracted from the actuarial report pertaining to the year ended March 31, 2011.

	Rs. in million
Present value of defined benefit obligations as of:	
• April 1, 2010	133
• March 31, 2011	166
Fair value of plan assets as of:	
• April 1, 2010	114
• March 31, 2011	120
Net cumulative unrecognized losses as of April 1, 2010	19

Benefits paid by the plan to the employees	6
Current service cost	15
Interest cost	16
Expected return on plan assets	14

Actuarial gains and losses are recognized using the corridor method, over the expected average remaining working lives of the employees. As of March 31, 2011 the expected average remaining working lives of the employees was 18 years.

Required:

Prepare a note on retirement benefits for presentation in the financial statements for the year ended March 31, 2011 in accordance with International Financial Reporting Standards. ***(14 marks)***

Question # 5

Lion Engineering Limited (LEL) operates an approved pension scheme (defined benefit plan) for all its permanent employees who have completed one year's service. The details for the year ended 30 June 2012 relating to the pension scheme are as follows:

	Rs. in million
Present value of pension scheme obligation at 30 June 2011	100
Fair value of scheme's assets at 30 June 2011	70
Unrecognized actuarial loss at 30 June 2011	20
Current service cost	29
Contribution made during the year	30
Benefits paid during the year	45
Present value of pension scheme obligation at 30 June 2012	110
Fair value of scheme's assets at 30 June 2012	80

Additional information:

(i) With effect from 1 July 2011, LEL had amended the scheme whereby the employees' pension entitlement had been increased. The benefits would become vested after three years. According to actuarial valuation the present value of the cost of additional benefits at 1 July 2011 was Rs. 15 million.

(ii) The discount rate and expected rate of return on the plan assets on 30 June 2012 were as follows:

Discount rate	13%
Expected rate of return on plan assets	10%

(iii) LEL was required to pay Rs. 40 million to the scheme, during the year ended 30 June 2012. Because of cash flow constraints, LEL was able to contribute Rs. 30 million only.

(iv) Average remaining working lives of employees is 10 years.

(v) LEL uses the corridor approach to recognize actuarial gains and losses.

(vi) Last actuarial valuation was made on 30 June 2012 using the Projected Unit Credit Method.

Required:

Prepare the relevant extracts from the statement of financial position and the related notes to the financial statements for the year ended 30 June 2012. Show all necessary workings. ***(Accounting policy note is not required. Deferred tax may be ignored)*** (18)