AS 15 Employee Benefits

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Scope

- ❖ AS 15 shall be applied to *by an employer* to all types of employee benefits (except to which IFRS 2 applies) which are defined as "all forms of consideration given by an entity in exchange for service rendered by the employee Or for the termination of the employment"

- ❖ Employee benefits covered under this standard, include those provided:
  - (a). under formal plans / arrangements between the entity and employees;
  - (b). Under legislative requirements – viz. contribution plans; AND
  - (c). By informal practices giving rise to constructive obligation – viz. bonus etc.

- ❖ *The standard however does not deal with reporting by employee benefit plan entities*

- ❖ Employee benefits include benefits provided to either the employees, or their spouses, children or other dependents and may be settled by payments made either
- ✓ Directly to the employees or their spouses, children, other dependants, or legal heirs; or
- ✓ To others such as trusts, insurance companies

Categories of Employee benefits

The different types of employee benefits are :-

- Short term Employee benefits
  - Wages, Salaries, Social Contributions;
  - Compensated absences (annual / sick leave);
  - Profit sharing and Bonuses
  - Non Monetary Benefits viz. medical care, cars ETC

  for current employers
- Long term Employee benefits
  - long term paid absences
  - jubilee or other long term service benefits
  - long term disability beenfits
- POST Employment benefits
  - Pensions, provident fund etc on retirement
  - Post retirement life insurance / medical care, plans
- Termination benefits

Short term employee benefits

- *Are benefits other than termination benefits* which fall wholly within 12 months after the end of the reporting period in which the employee renders the related service

- ***Accounting :***

- ✓ fairly straight forward, no actuarial assumptions to measure the obligations or the cost
- ✓ are measured on an undiscounted basis –
- ✓ there is no possibility of any actuarial gains or losses in accounting for short term employee benefits

Recognition and measurement - Short term employee benefits

- ❖ ***All short term employee benefits***
- ✓ Recognise the undiscounted amount expected to be paid in exchange for the service
- ✓ **As a liability (accrued expense)**, after deducting any amount paid and as an **expense (profit and loss)** *unless it is included in the cost of an asset as per other standards*

- ❖ ***Short term paid absences:***
- ✓ Are compensation to employees for absence due to various reasons, sick leave, vacation, maternity or parternity
- ✓ **Accumulating paid absences:** are those that are carried forward and can be used in future periods, *if the current period's entitlements are not fully utilised*
- ✓ **Non Accumulating paid absences:** are those that cannot be carried forward and lapse if the current period's entitlement are not fully used.

Recognition and measurement - Short term employee benefits

❖ ***Short term paid absences (Contd..):***

Paid absences	Sub category , if any	RECOGNITION (when)
Accumulating	**Vesting** – employees are entitled to cash payment for unused entitlement on leaving the entity)	**When the employee renders services that increases their entitlement to future paid absences** *An obligation to pay exists irrespective of whether the paid absences are vesting or non vesting – only affects the measurement of obligation*
	Non Vesting – employees are NOT entitled to cash payment for unused entitlement on leaving the entity)	
Non Accumulating	**-**	**When the absences occur** – no liability or expense is recognised until the time of absence as *employee service does not increase the benefit amounts*

Recognition and measurement - Short term employee benefits

❖ ***Short term paid absences (Contd..):***

Paid absences	Sub category , if any	MEASUREMENT
Accumulating	**Vesting** – employees are entitled to cash payment for unused entitlement on leaving the entity)	at the amounts of additional payments an enterprise is expected to make as the benefits accumulates based on accumulated benefits as at balance sheet date
	Non Vesting – employees are NOT entitled to cash payment for unused entitlement on leaving the entity)	
Non Accumulating	**-**	-- SAME --

Note: *Whether vesting or non vesting, the fact is, that an obligation exists to pay accumulating absences and hence a liability is created at balance sheet– measurement however considers the possibility of the number of people leaving the entity without utilising the accumulated non vesting absences (i.e. an estimate is made of the people and number of the accumulating absences expected to be utilised)*

Recognition and measurement - Short term employee benefits

❖ ***Profit sharing and Bonus plans:***

Type		RECOGNITION (when)
Profit sharing plans	Some employees receive a share of profit ***only*** if they remain with the enterprise for a specified period – such plans create an obligation as employee renders service that increases the amounts to be paid if they remain in service until the end of the specified period	1. Enterprise has a present obligation (legal or constructive) to pay; 2. A reliable estimate of the obligation can be made – (a) formal plan containing pay formula; (b) amounts determined before FS are authorised for issue; (c) past practice gives clear evidence of entity's obligation
Bonus Plans	Some entities have a practice of paying bonuses – this creates an obligation (constructive obligation) – the entity has no alternative but to pay the bonus	

Long Term Employee Benefits

- Are employee benefits (other than post employment benefits and termination benefits) which do not fall wholly *within 12 months after the end of the period in which the employees render the related service*

- *Measurement principles:* same as applied in case of post employment benefit plans

- Recognition of other long term employee benefits:

IN BALANCE SHEET	IN PROFIT AND LOSS
Present value of defined benefit obligation ***Less*** Fair Value of plan assets as at BS out of which obligations are to be settled directly	▪ Current service cost ▪ Interest cost ▪ expected return on plan assets ▪ actuarial gains / losses – recognise immediately ▪ past service cost ▪ effect of curtailments or settlements

Termination benefits

- ❖ Are payable as a result of
- ✓ *An enterprise's decision to terminate employee's employment before the normal retirement period; OR*
- ✓ *An employees decision to accept voluntary redundancy in exchange for those benefits (voluntary retirement)*

- ❖ ***Termination benefits*** are lump sum payments *but may sometimes include* ***(a)*** enhancement to post employment benefits; or ***(b)*** salary until end of the specified period if employee renders no service to the enterprise

Recognition (When)	Measurement
When and only when: ✓ the enterprise has a present obligation as a result of a past event; ✓ it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation ✓ a reliable estimate can be made of the amount of obligation	✓ should be recognised as an expense immediately; ✓ where termination benefits fall due for *more than 12 months after the balance sheet date*, they should be discounted to their present value (market yields of Government bonds at BS date) ✓Exemption to SMC – no discounting required

Post employment benefits

- ❖ Are payable after the completion of employment;
- ❖ Are formal plans or informal arrangements under which an enterprise provides post employment benefits
- ❖ Are classified into the following categories

Defined contribution plans	Defined benefit plans
Are plans under which an enterprise pays a fixed contribution into a separate entity (fund) and will have no obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to an employee service in the current and prior periods The actual risk (that benefits will be less than expected) and investment risk (assets invested will be insufficient to meet expected benefits) ***fall on the employee***	Are post employee benefit plans other than defined contribution plans Under defined plans ✓Enterprise obligations is to provide the agreed benefits to the current and former employees; and ✓ the actuarial risk (that benefits will cost more than expected) and investment risk, ***fall on the enterprise***

Defined contribution plans

- Accounting is fairly simple and straight forward
- No actuarial assumptions required to measure obligation as at the balance sheet date

Recognition	Measurement
The enterprise should recognise the contribution payable in exchange for the service as : (a) A liability ; and (b) An expense *when the employee renders the service to the enterprise* *Where contribution paid exceeds the contribution payable for the period* excess should be recognsied as asset (prepaid contribution	Measurement of obligation for each period – amount of contribution required for each period (on an undiscounted basis) Measured at present values, if contributions are payable not within 12 months after the end of the reporting period in which employees rendered related service (market yields of Government bonds at BS date) Exemption to SMC – no discounting required

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Recognition	Measurement
The enterprise should recognise the contribution payable in exchange for the service as : (a) A liability ; and (b) An expense *when the employee renders the service to the enterprise* *Where contribution paid exceeds the contribution payable for the period* excess should be recognsied as asset (prepaid contribution	Measurement of obligation for each period – amount of contribution required for each period (on an undiscounted basis) Measured at present values, if contributions are payable not within 12 months after the end of the reporting period in which employees rendered related service (market yields of Government bonds at BS date) Exemption to SMC – no discounting required

Defined Benefit plans

- Are complex to calculate
- Obligations are measured on discounted basis using *Projected Unit Credit method*
- *Uses actuarial techniques (services of an actuary) to determine the benefit obligation as at the end of the reporting period*
- ***The components of a defined benefit plan and its recognition are as follows:***

In Balance Sheet		
a	Present Value of defined benefit obligation	XX
b	(-) any past service cost not yet recognised	(X)
c	(-) Fair value of plan assets as at the balance sheet date out of which obligations are settled	(xx)
The defined benefit liability (as at balance sheet date)		**XXX**

In Profit and Loss account		
a	Current service cost	**x**
b	Interest cost	x
c	Expected return – plan assets	x
d	Past service cost – recognised	x
e	Effect of curtailments/ settlements	x
f	Where DBO is –ve (asset), difference between (-ve value and amount recognised in BS)	x

Defined Benefit plans

❖ ***Net Defined Benefit Obligation (Asset Ceiling):***

Where the amount determined (NET) of the defined benefit obligation is –ve (asset) the amounts recognised in the balance sheet as an asset ***is lower of:***

(a) The amount determined as above; and

(b) The present value of economic benefits in the form of refunds from the plan or reductions in future contributions to the plan

In Balance Sheet		
A	Present Value of Obligation	1100
B	(-) Fair Value of plan assets	(1190)
		(90)
	Unrecognised past service cost	(70)
C	Present value of Defined benefit obligation (asset)	(160)
D	**Present value of available future refunds and reductions in contributions**	**90**
	Fair value of Plan assets recognised in BS (lower of 'c' and 'd')	90
	Amounts recognised in Profit and loss	70

Defined Benefit plans

- ***Current Service cost:*** is the increase in the present value of the defined benefit obligation resulting from employee service in the current period .

- ***The important elements in the determination of current service cost are:***

- ✓ **Actuarial method:** use Projected Unit Credit Method to determine the present value of defined benefit obligation – the method considers each period of service as giving rise to additional unit of benefit entitlement ; considers each benefit separately towards building up the final benefit obligation

- ✓ **Attributing benefits to the period of service:** where employee's services in later years will lead to materially higher level of benefit than in earlier years, the enterprise should attribute *benefit on a straight line basis* ***from*** the starting year of the entitlement to the year from where onwards there are no significant increase in the benefits

- ✓ **Actuarial assumptions:** consisting of (PTO)

Defined Benefit plans

- ✓ **Actuarial assumptions:** consisting of

a) Demographic assumptions (features of employees- mortality rate, employee turnover, proportion of plan members, claim rates under medical plan etc)

b) Financial assumptions – discount rate, future salary, benefit levels in case of medical benefits, future medical costs etc.

c) Future salary increases, estimated future changes in level of any state benefits that affects the benefits payable under a defined benefit plan (enacted before balance sheet date or as per certain trends in general price levels based on past history or reliable evidence)

Defined Benefit plans

- ***Past Service cost:*** is the change in defined benefit obligation for employee service in prior years resulting in the current period from introduction of, or changes to, post employment benefits or other long term employee benefits.

- ✓ Can be either positive (benefits are introduced or improved) or negative (existing benefits are reduced) – negative past service cost is recognised over the average period until the reduced portion of the benefits become vested

- ✓ **Recognition of past service cost:**

a. Where benefits have not vested: on a straight line basis over the periods until vesting

b. Where the benefits are already vested: recognise past service cost immediately

- ✓ **Past service costs *does not include:***

a. Adjustments to salary increases – already considered in actuarial valuation

b. Increase in vested benefits not on account of new or improved benefits – again benefits were considered as the services were rendered

c. Effect of plan amendments that reduce benefits for future service (curtailment)

Defined Benefit plans

❖ ***Plan Assets : comprise***

a. Assets held by a long term employee benefit entity (fund), *other than non transferable financial instruments issued by the reporting enterprise,* solely for paying employee benefits – the fund is a legally separate entity from the reporting enterprise; OR

b. Qualifying Insurance policies – issued by an insurer that is not related party of the reporting enterprise (as defined in AS 18) and proceeds of the policy is ONLY to fund employee benefits payments under a defined benefit plan

✓ Plan assets are measured at ***fair value as at balance sheet date***

✓ **Return on plan assets:** The return of plan assets is interest, dividends and other revenue derived from the plan assets, together with realized and unrealized gains or losses on the plan assets, *less* any costs of administering the plan and *less*any tax payable by the plan itself *(definition Para 7.17 of AS 15)*

✓ ***Expected return on plan assets*** =

[Market Yield (%) x (opening FV of plan assets + net increase in plan assets during the period)] Less expected administrative costs

Actual return on plan assets =

FV of plan assets as at end of reporting period – (opening FV of plan assets + net increase in plan assets) *less* expected administrative costs (if not included in determining the fair value of plan assets)

✓ ***Actuarial Gain or loss (return on plan assets) = (expected – actual) return on plan assets***

Discount Rate and Interest cost

- **The discount rate** used to discount post employment benefit obligations (both funded and unfunded) should be determined by reference to *market yields at the balance sheet date on Government bonds*. The currency and term of the government bonds should be consistent with the currency and estimated term of the post employment benefit obligations *(Para 78 of AS 15)*

- **Interest Cost** is computed by multiplying the discount rate *at the start of the period* by the present value of defined benefit liability throughout that period

Curtailment and settlement

- ❖ **Curtailment** a curtailment relating to a defined benefit obligation occurs when an enterprise *either:*

a) Has a present obligation arising from the requirement of a statute / regulator or otherwise, to make a material reduction in the number of employees covered by a plan; OR

b) Amends the terms of a defined benefit plan such that a material element of future service by current employees will no longer qualify for benefits or will qualify only for reduced benefits

- ✓ A curtailment may arise from an isolated event, say, closing of a plant, discontinuance of an operation or termination / suspension of a defined benefit plan. Curtailment is often linked with a restructuring

- ❖ **Settlement:** occurs when an enterprise enters into a transaction that eliminates all further obligations for part or all of the benefits provided under a defined benefit plan. For example, lump sum cash payment in exchange for employee rights to receive post employment benefits *(Para 113 of AS 15)*
- ✓ **A settlement** occurs together with a curtailment if a plan is terminated such that the obligation is settled and the plan ceases to exist

Actuarial Gains and losses

- **Actuarial gains and losses comprise of** *:*

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

b) The effects of changes in actuarial assumptions

- ✓ Actuarial gains and losses may result from increases or decreases in **<u>either</u>** *the present value of defined benefit obligation* or *the fair value of any related plan assets*
- ✓ ***Actuarial gains or losses should be recognised immediately in the statement of profit and loss as an expense or income***

- ✓ **Causes of actuarial gains or losses include**;

a. Unexpectedly high or low rates of employee turnover, early retirement or mortality or of increases in salaries, benefits and the effect of changes in such estimates

b. Effect of changes in the discount rate

c. Differences between the actual return of plan assets and the expected return of plan assets

Defined Benefit plans – some aspects on presentation

❖ **Off set** *:*an enterprise should offset an asset relating to one plan against liability relating to another plan *when and only when*, the enterprise:

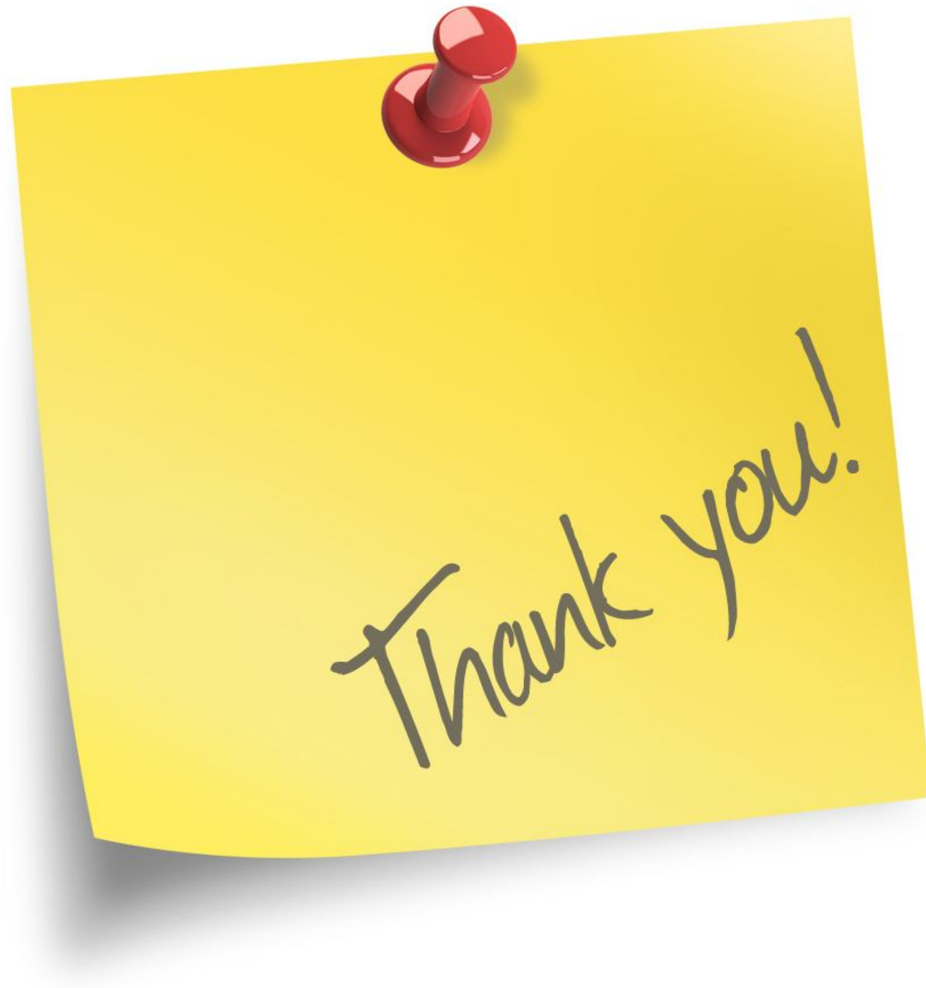
a. has a legally enforceable right to use a surplus in one plan to settle obligations under another plan; and

b. intends either to settle the obligations on a net basis or to realize the surplus in one plan and settle its obligations under another plan simultaneously

(Para 117 of AS 15)

❖ **financial components of post employment benefit cost:** this standard does not specify whether an enterprise should present current service cost, interest cost, and expected return on plan assets, as *components of a single item of income or expense on the face of profit and loss (Para 118 of AS 15)*

❖ **a small and medium sized company,** need not apply the requirements of Para 117 and 118 of the standard in respect of accounting for defined benefit plans


Thank you!