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including International Accounting Standards (IASs™) and Interpretations as
at 31 March 2004

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International Accounting Standard 19

Employee Benefits

This version includes amendments resulting from new and amended IFRSs issued up to 31 March 2004. The section “Changes in this Edition” at the front of this volume provides the application dates of these new and amended IFRSs and also identifies those current IFRSs that are not included in this volume.

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IAS 19

International Accounting Standard 19 *Employee Benefits* (IAS 19) is set out in paragraphs 1-160. All the paragraphs have equal authority but retain the IASC format of the Standard when it was adopted by the IASB. IAS 19 should be read in the context of its objective and the Basis for Conclusions, the *Preface to International Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*. IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Introduction

- IN1. The Standard prescribes the accounting and disclosure by employers for employee benefits. It replaces IAS 19 *Retirement Benefit Costs* which was approved in 1993. The major changes from the old IAS 19 are set out in the *Basis for Conclusions*. The Standard does not deal with reporting by employee benefit plans (see IAS 26 *Accounting and Reporting by Retirement Benefit Plans*).
- IN2. The Standard identifies four categories of employee benefits:
- (a) short-term employee benefits, such as wages, salaries and social security contributions, paid annual leave and paid sick leave, profit-sharing and bonuses (if payable within twelve months of the end of the period) and non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees;
 - (b) post-employment benefits such as pensions, other retirement benefits, post-employment life insurance and post-employment medical care;
 - (c) other long-term employee benefits, including long-service leave or sabbatical leave, jubilee or other long-service benefits, long-term disability benefits and, if they are payable twelve months or more after the end of the period, profit-sharing, bonuses and deferred compensation; and
 - (d) termination benefits.
- IN3. The Standard requires an entity to recognise short-term employee benefits when an employee has rendered service in exchange for those benefits.
- IN4. Post-employment benefit plans are classified as either defined contribution plans or defined benefit plans. The Standard gives specific guidance on the classification of multi-employer plans, state plans and plans with insured benefits.
- IN5. Under defined contribution plans, 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. The Standard requires an entity to recognise contributions to a defined contribution plan when an employee has rendered service in exchange for those contributions.
- IN6. All other post-employment benefit plans are defined benefit plans. Defined benefit plans may be unfunded, or they may be wholly or partly funded. The Standard requires an entity to:
- (a) account not only for its legal obligation, but also for any constructive obligation that arises from the entity's practices;
 - (b) determine the present value of defined benefit obligations and the fair value of any plan assets with sufficient regularity that the amounts recognised in the financial statements do not differ materially from the amounts that would be determined at the balance sheet date;
 - (c) use the Projected Unit Credit Method to measure its obligations and costs;

- (d) attribute benefit to periods of service under the plan's benefit formula, unless an employee's service in later years will lead to a materially higher level of benefit than in earlier years;
- (e) use unbiased and mutually compatible actuarial assumptions about demographic variables (such as employee turnover and mortality) and financial variables (such as future increases in salaries, changes in medical costs and certain changes in state benefits). Financial assumptions should be based on market expectations, at the balance sheet date, for the period over which the obligations are to be settled;
- (f) determine the discount rate by reference to market yields at the balance sheet date on high quality corporate bonds (or, in countries where there is no deep market in such bonds, government bonds) of a currency and term consistent with the currency and term of the post-employment benefit obligations;
- (g) deduct the fair value of any plan assets from the carrying amount of the obligation. Certain reimbursement rights that do not qualify as plan assets are treated in the same way as plan assets, except that they are presented as a separate asset, rather than as a deduction from the obligation;
- (h) limit the carrying amount of an asset so that it does not exceed the net total of:
 - (i) any unrecognised past service cost and actuarial losses; plus
 - (ii) the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan;
- (i) recognise past service cost on a straight-line basis over the average period until the amended benefits become vested;
- (j) recognise gains or losses on the curtailment or settlement of a defined benefit plan when the curtailment or settlement occurs. The gain or loss should comprise any resulting change in the present value of the defined benefit obligation and of the fair value of the plan assets and the unrecognised part of any related actuarial gains and losses and past service cost; and
- (k) recognise a specified portion of the net cumulative actuarial gains and losses that exceed the greater of:
 - (i) 10% of the present value of the defined benefit obligation (before deducting plan assets); and
 - (ii) 10% of the fair value of any plan assets.

The portion of actuarial gains and losses to be recognised for each defined benefit plan is the excess that fell outside the 10% 'corridor' at the previous reporting date, divided by the expected average remaining working lives of the employees participating in that plan.

The Standard also permits systematic methods of faster recognition, provided that the same basis is applied to both gains and losses and the basis is applied consistently from period to period. Such permitted methods include immediate recognition of all actuarial gains and losses.

- IN7. The Standard requires a simpler method of accounting for other long-term employee benefits than for post-employment benefits: actuarial gains and losses and past service cost are recognised immediately.
- IN8. Termination benefits are employee benefits payable as a result of either: an entity's decision to terminate an employee's employment before the normal retirement date; or an employee's decision to accept voluntary redundancy in exchange for those benefits. The event which gives rise to an obligation is the termination rather than employee service. Therefore, an entity should recognise termination benefits when, and only when, the entity is demonstrably committed to either:
- (a) terminate the employment of an employee or group of employees before the normal retirement date; or
 - (b) provide termination benefits as a result of an offer made in order to encourage voluntary redundancy.
- IN9. An entity is demonstrably committed to a termination when, and only when, the entity has a detailed formal plan (with specified minimum contents) for the termination and is without realistic possibility of withdrawal.
- IN10. Where termination benefits fall due more than 12 months after the balance sheet date, they should be discounted. In the case of an offer made to encourage voluntary redundancy, the measurement of termination benefits should be based on the number of employees expected to accept the offer.
- IN11. [Deleted]
- IN12. The Standard is effective for accounting periods beginning on or after 1 January 1999. Earlier application is encouraged. On first adopting the Standard, an entity is permitted to recognise any resulting increase in its liability for post-employment benefits over not more than five years. If the adoption of the standard decreases the liability, an entity is required to recognise the decrease immediately.
- IN13. [Deleted]

International Accounting Standard 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 recognise:

- (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

1. ***This Standard shall be applied by an employer in accounting for all employee benefits, except those to which IFRS 2 Share-based Payment applies.***
2. This Standard does not deal with reporting by employee benefit plans (see IAS 26 *Accounting and Reporting by Retirement Benefit Plans*).
3. 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.
4. Employee benefits include:
 - (a) short-term employee benefits, such as wages, salaries and social security contributions, paid annual leave and paid sick leave, profit-sharing and bonuses (if payable within twelve months of the end of the period) and non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees;
 - (b) post-employment benefits such as pensions, other retirement benefits, post-employment life insurance and post-employment medical care;

- (c) other long-term employee benefits, including long-service leave or sabbatical leave, jubilee or other long-service benefits, long-term disability benefits and, if they are not payable wholly within twelve months after the end of the period, profit-sharing, bonuses and deferred compensation; and
- (d) termination benefits.

Because each category identified in (a)-(d) above has different characteristics, this Standard establishes separate requirements for each category.

5. Employee benefits include benefits provided to either employees or their dependants and may be settled by payments (or the provision of goods or services) made either directly to the employees, to their spouses, children or other dependants or to others, such as insurance companies.
6. An employee may provide services to an entity on a full-time, part-time, permanent, casual or temporary basis. For the purpose of this Standard, employees include directors and other management personnel.

Definitions

7. *The following terms are used in this Standard with the meanings specified:*

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

Short-term employee benefits are employee benefits (other than termination benefits) which fall due wholly within twelve months after the end of the period in which the employees render the related service.

Post-employment benefits are employee benefits (other than termination benefits) which are payable after the completion of employment.

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 concerned.

Other long-term employee benefits are employee benefits (other than post-employment benefits and termination benefits) which do not fall due wholly within twelve months after the end of the period in which the employees render the related service.

Termination benefits are employee benefits payable 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 voluntary redundancy in exchange for those benefits.

Vested employee benefits are employee benefits that are not conditional on future employment.

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.

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

Interest cost is the increase during a period in the present value of a defined benefit obligation which arises because the benefits are one period closer to settlement.

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

* A qualifying insurance policy is not necessarily an insurance contract, as defined in IFRS 4 *Insurance Contracts*.

- (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.*

The return on plan assets *is interest, dividends and other revenue derived from the plan assets, together with realised and unrealised gains or losses on the plan assets, less any costs of administering the plan and less any tax payable by the plan itself.*

Actuarial gains and losses *comprise:*

- (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.*

Past service cost *is the increase in the present value of the defined benefit obligation for employee service in prior periods, resulting in the current period from the introduction of, or changes to, post-employment benefits or other long-term employee benefits. Past service cost may be either positive (where benefits are introduced or improved) or negative (where existing benefits are reduced).*

Short-term Employee Benefits

8. Short-term employee benefits include items such as:
- (a) wages, salaries and social security contributions;
 - (b) short-term compensated absences (such as paid annual leave and paid sick leave) where the absences are expected to occur within twelve months after the end of the period in which the employees render the related employee service;
 - (c) profit-sharing and bonuses payable within twelve months after the end of the period in which the employees render the related service; and
 - (d) non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees.
9. Accounting for short-term employee benefits is generally straightforward because no actuarial assumptions are required to measure the obligation or the cost and there is no possibility of any actuarial gain or loss. Moreover, short-term employee benefit obligations are measured on an undiscounted basis.

Recognition and Measurement

All Short-term Employee Benefits

10. *When an employee has rendered service to an entity during an accounting period, the entity shall recognise 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 recognise 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; and*
- (b) as an expense, unless another Standard 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).*

Paragraphs 11, 14 and 17 explain how an entity shall apply this requirement to short-term employee benefits in the form of compensated absences and profit-sharing and bonus plans.

Short-term Compensated Absences

11. *An entity shall recognise the expected cost of short-term employee benefits in the form of compensated absences under paragraph 10 as follows:*

- (a) in the case of accumulating compensated absences, when the employees render service that increases their entitlement to future compensated absences; and*
- (b) in the case of non-accumulating compensated absences, when the absences occur.*

12. An entity may compensate employees for absence for various reasons including vacation, sickness and short-term disability, maternity or paternity, jury service and military service. Entitlement to compensated absences falls into two categories:

- (a) accumulating; and
- (b) non-accumulating.

13. Accumulating compensated absences are those that are carried forward and can be used in future periods if the current period's entitlement is not used in full. Accumulating compensated absences may be either vesting (in other words, employees are entitled to a cash payment for unused entitlement on leaving the entity) or non-vesting (when employees are not entitled to a cash payment for unused entitlement on leaving). An obligation arises as employees render service that increases their entitlement to future compensated absences. The obligation exists, and is recognised, even if the compensated absences are non-vesting, although the possibility that employees may leave before they use an accumulated non-vesting entitlement affects the measurement of that obligation.

14. *An entity shall measure the expected cost of accumulating compensated absences as the additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the balance sheet date.*
15. The method specified in the previous paragraph measures the obligation at the amount of the additional payments that are expected to arise solely from the fact that the benefit accumulates. In many cases, an entity may not need to make detailed computations to estimate that there is no material obligation for unused compensated absences. For example, a sick leave obligation is likely to be material only if there is a formal or informal understanding that unused paid sick leave may be taken as paid vacation.

Example Illustrating Paragraphs 14 and 15

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 year (a LIFO basis). 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). Therefore, the entity recognises a liability equal to 12 days of sick pay.

16. Non-accumulating compensated absences do not carry forward: they lapse if the current period's entitlement is not used in full and do not entitle employees to a cash payment for unused entitlement on leaving the entity. This is commonly the case for sick pay (to the extent that unused past entitlement does not increase future entitlement), maternity or paternity leave and compensated absences for jury service or military service. An entity recognises no liability or expense until the time of the absence, because employee service does not increase the amount of the benefit.

Profit-sharing and Bonus Plans

17. *An entity shall recognise the expected cost of profit-sharing and bonus payments under paragraph 10 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.*

18. Under some profit-sharing plans, employees receive a share of the profit only if they remain with the entity for a specified period. Such plans create a constructive obligation as employees render service that increases the amount to be paid if they remain in service until the end of the specified period. The measurement of such constructive obligations reflects the possibility that some employees may leave without receiving profit-sharing payments.

Example Illustrating Paragraph 18

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.

The entity recognises a liability and an expense of 2.5% of net profit.

19. An entity may have no legal obligation to pay a bonus. Nevertheless, in some cases, an entity has a practice of paying bonuses. In such cases, the entity has a constructive obligation because the entity has no realistic alternative but to pay the bonus. The measurement of the constructive obligation reflects the possibility that some employees may leave without receiving a bonus.
20. An entity can make a reliable estimate of its legal or constructive obligation under a profit-sharing or bonus plan when, and only when:
- the formal terms of the plan contain a formula for determining the amount of the benefit;
 - the entity determines the amounts to be paid before the financial statements are authorised for issue; or
 - past practice gives clear evidence of the amount of the entity's constructive obligation.
21. An obligation under profit-sharing and bonus plans results from employee service and not from a transaction with the entity's owners. Therefore, an entity recognises the cost of profit-sharing and bonus plans not as a distribution of net profit but as an expense.
22. If profit-sharing and bonus payments are not due wholly within twelve months after the end of the period in which the employees render the related service, those payments are other long-term employee benefits (see paragraphs 126-131).

Disclosure

23. Although this Standard does not require specific disclosures about short-term employee benefits, other Standards may require disclosures. For example, IAS 24 *Related Party Disclosures* 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

24. Post-employment benefits include, for example:
- (a) retirement benefits, such as pensions; and
 - (b) other post-employment benefits, such as post-employment life insurance and post-employment medical care.
- Arrangements whereby an entity provides post-employment benefits are post-employment benefit plans. An entity applies this Standard to all such arrangements whether or not they involve the establishment of a separate entity to receive contributions and to pay benefits.
25. 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:
- (a) 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; and
 - (b) 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 on the employee.
26. Examples of cases where an entity's obligation is not limited to the amount that it agrees to contribute to the fund are when the entity has a legal or constructive obligation through:
- (a) a plan benefit formula that is not linked solely to the amount of contributions;
 - (b) a guarantee, either indirectly through a plan or directly, of a specified return on contributions; or
 - (c) those informal practices that give rise to a constructive obligation. For example, a constructive obligation may arise where an entity has a history of increasing benefits for former employees to keep pace with inflation even where there is no legal obligation to do so.
27. 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.

28. Paragraphs 29-42 below explain the distinction between defined contribution plans and defined benefit plans in the context of multi-employer plans, state plans and insured benefits.

Multi-employer Plans

29. *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). Where a multi-employer plan is a defined benefit plan, an entity shall:*
- (a) *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; and*
 - (b) *disclose the information required by paragraph 120.*
30. *When sufficient information is not available to use defined benefit accounting for a multi-employer plan that is a defined benefit plan, an entity shall:*
- (a) *account for the plan under paragraphs 44-46 as if it were a defined contribution plan;*
 - (b) *disclose:*
 - (i) *the fact that the plan is a defined benefit plan; and*
 - (ii) *the reason why sufficient information is not available to enable the entity to account for the plan as a defined benefit plan; and*
 - (c) *to the extent that a surplus or deficit in the plan may affect the amount of future contributions, disclose in addition:*
 - (i) *any available information about that surplus or deficit;*
 - (ii) *the basis used to determine that surplus or deficit; and*
 - (iii) *the implications, if any, for the entity.*
31. One example of a defined benefit multi-employer plan is one where:
- (a) the plan is financed on a pay-as-you-go basis such that: contributions are set at a level that is expected to be sufficient to pay the benefits falling due in the same period; and future benefits earned during the current period will be paid out of future contributions; and
 - (b) employees' benefits are determined by the length of their service and the participating entities have no realistic means of withdrawing from the plan without paying a contribution for the benefits earned by employees up to the date of withdrawal. Such a plan creates actuarial risk for the entity: if the ultimate cost of benefits already earned at the balance sheet date is more than expected, the entity will have to either increase its contributions or persuade employees to accept a reduction in benefits. Therefore, such a plan is a defined benefit plan.

32. Where sufficient information is available about a multi-employer plan which is a defined benefit plan, an entity accounts for its proportionate share of the defined benefit obligation, plan assets and post-employment benefit cost associated with the plan in the same way as for any other defined benefit plan. However, in some cases, an entity may not be able to identify its share of the underlying financial position and performance of the plan with sufficient reliability for accounting purposes. This may occur if:
- (a) the entity does not have access to information about the plan that satisfies the requirements of this Standard; or
 - (b) the plan exposes the participating entities to actuarial risks associated with the current and former employees of other entities, with the result that there is no consistent and reliable basis for allocating the obligation, plan assets and cost to individual entities participating in the plan.

In those cases, an entity accounts for the plan as if it were a defined contribution plan and discloses the additional information required by paragraph 30.

33. Multi-employer plans are distinct from group administration plans. A group administration plan is merely an aggregation of single employer plans combined to allow participating employers to pool their assets for investment purposes and reduce investment management and administration costs, but the claims of different employers are segregated for the sole benefit of their own employees. Group administration plans pose no particular accounting problems because information is readily available to treat them in the same way as any other single employer plan and because such plans do not expose the participating entities to actuarial risks associated with the current and former employees of other entities. The definitions in this Standard require an entity to classify a group administration plan as a defined contribution plan or a defined benefit plan in accordance with the terms of the plan (including any constructive obligation that goes beyond the formal terms).
34. Defined benefit plans that pool the assets contributed by various entities under common control, for example, a parent and its subsidiaries, are not multi-employer plans. Therefore, an entity treats all such plans as defined benefit plans.
35. IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* requires an entity to recognise, or disclose information about, certain contingent liabilities. In the context of a multi-employer plan, a contingent liability may arise from, for example:
- (a) actuarial losses relating to other participating entities because each entity that participates in a multi-employer plan shares in the actuarial risks of every other participating entity; or
 - (b) any responsibility under the terms of a plan to finance any shortfall in the plan if other entities cease to participate.

State Plans

36. *An entity shall account for a state plan in the same way as for a multi-employer plan (see paragraphs 29 and 30).*

37. 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) which is not subject to control or influence by the reporting entity. Some plans established by an entity provide both compulsory benefits which substitute for benefits that would otherwise be covered under a state plan and additional voluntary benefits. Such plans are not state plans.
38. State plans are characterised as defined benefit or defined contribution in nature based 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, in the rare cases when a state plan is a defined benefit plan, an entity applies the treatment prescribed in paragraphs 29 and 30.

Insured Benefits

39. *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 to either:*
- (a) pay the employee benefits directly when they fall due; or*
 - (b) 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.*
40. The benefits insured by an insurance contract need not have a direct or automatic relationship with the entity's obligation for employee benefits. Post-employment benefit plans involving insurance contracts are subject to the same distinction between accounting and funding as other funded plans.
41. 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 (see paragraph 7); and

- (b) recognises other insurance policies as reimbursement rights (if the policies satisfy the criteria in paragraph 104A).
42. 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

43. 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 do not fall due wholly within twelve months after the end of the period in which the employees render the related service.

Recognition and Measurement

44. *When an employee has rendered service to an entity during a period, the entity shall recognise 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 balance sheet date, an entity shall recognise 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; and*
 - (b) *as an expense, unless another Standard requires or permits the inclusion of the contribution in the cost of an asset (see, for example, IAS 2 Inventories and IAS 16 Property, Plant and Equipment).*
45. *Where contributions to a defined contribution plan do not fall due wholly within twelve months after the end of the period in which the employees render the related service, they shall be discounted using the discount rate specified in paragraph 78.*

Disclosure

46. *An entity shall disclose the amount recognised as an expense for defined contribution plans.*
47. Where required by IAS 24 *Related Party Disclosures* an entity discloses information about contributions to defined contribution plans for key management personnel.

Post-employment Benefits: Defined Benefit Plans

48. 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

49. 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 recognised for a defined benefit plan is not necessarily the amount of the contribution due for the period.
50. Accounting by an entity for defined benefit plans involves the following steps:
- (a) using actuarial techniques to make a reliable estimate of the amount of 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 (see paragraphs 67-71) 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 influence the cost of the benefit (see paragraphs 72-91);
 - (b) discounting that benefit using the Projected Unit Credit Method in order to determine the present value of the defined benefit obligation and the current service cost (see paragraphs 64-66);
 - (c) determining the fair value of any plan assets (see paragraphs 102-104);
 - (d) determining the total amount of actuarial gains and losses and the amount of those actuarial gains and losses to be recognised (see paragraphs 92-95);
 - (e) where a plan has been introduced or changed, determining the resulting past service cost (see paragraphs 96-101); and
 - (f) where a plan has been curtailed or settled, determining the resulting gain or loss (see paragraphs 109-115).

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

51. In some cases, estimates, averages and computational short cuts may provide a reliable approximation of the detailed computations illustrated in this Standard.

Accounting for the Constructive Obligation

52. *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.*
53. The formal terms of a defined benefit plan may permit an entity to terminate its obligation under the plan. Nevertheless, it is usually difficult for an entity to cancel a plan if employees are to be retained. Therefore, in the absence of evidence to the contrary, accounting for post-employment benefits assumes that an entity which is currently promising such benefits will continue to do so over the remaining working lives of employees.

Balance Sheet

54. *The amount recognised as a defined benefit liability shall be the net total of the following amounts:*
- (a) the present value of the defined benefit obligation at the balance sheet date (see paragraph 64);*
 - (b) plus any actuarial gains (less any actuarial losses) not recognised because of the treatment set out in paragraphs 92 and 93;*
 - (c) minus any past service cost not yet recognised (see paragraph 96);*
 - (d) minus the fair value at the balance sheet date of plan assets (if any) out of which the obligations are to be settled directly (see paragraphs 102-104).*
55. The present value of the defined benefit obligation is the gross obligation, before deducting the fair value of any plan assets.
56. *An entity shall determine the present value of defined benefit obligations and the fair value of any plan assets with sufficient regularity that the amounts recognised in the financial statements do not differ materially from the amounts that would be determined at the balance sheet date.*
57. This Standard encourages, but does not require, an entity to involve a qualified actuary in the measurement of all material post-employment benefit obligations. For practical reasons, an entity may request a qualified actuary to carry out a detailed valuation of the obligation before the balance sheet date. Nevertheless, the results of that valuation are updated for any material transactions and other material changes in circumstances (including changes in market prices and interest rates) up to the balance sheet date.
58. *The amount determined under paragraph 54 may be negative (an asset). An entity shall measure the resulting asset at the lower of:*
- (a) the amount determined under paragraph 54; and*

- (b) *the total of:*
- (i) *any cumulative unrecognised net actuarial losses and past service cost (see paragraphs 92, 93 and 96); and*
 - (ii) *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 these economic benefits shall be determined using the discount rate specified in paragraph 78.*
- 58A. *The application of paragraph 58 shall not result in a gain being recognised solely as a result of an actuarial loss or past service cost in the current period or in a loss being recognised solely as a result of an actuarial gain in the current period. The entity shall therefore recognise immediately under paragraph 54 the following, to the extent that they arise while the defined benefit asset is determined in accordance with paragraph 58(b):*
- (a) *net actuarial losses of the current period and past service cost of the current period to the extent that they exceed any reduction in the present value of the economic benefits specified in paragraph 58(b)(ii). If there is no change or an increase in the present value of the economic benefits, the entire net actuarial losses of the current period and past service cost of the current period shall be recognised immediately under paragraph 54.*
 - (b) *net actuarial gains of the current period after the deduction of past service cost of the current period to the extent that they exceed any increase in the present value of the economic benefits specified in paragraph 58(b)(ii). If there is no change or a decrease in the present value of the economic benefits, the entire net actuarial gains of the current period after the deduction of past service cost of the current period shall be recognised immediately under paragraph 54.*
- 58B. Paragraph 58A applies to an entity only if it has, at the beginning or end of the accounting period, a surplus* in a defined benefit plan and cannot, based on the current terms of the plan, recover that surplus fully through refunds or reductions in future contributions. In such cases, past service cost and actuarial losses that arise in the period, the recognition of which is deferred under paragraph 54, will increase the amount specified in paragraph 58(b)(i). If that increase is not offset by an equal decrease in the present value of economic benefits that qualify for recognition under paragraph 58(b)(ii), there will be an increase in the net total specified by paragraph 58(b) and, hence, a recognised gain. Paragraph 58A prohibits the recognition of a gain in these circumstances. The opposite effect arises with actuarial gains that arise in the period, the recognition of which is deferred under paragraph 54, to the extent that the actuarial gains reduce cumulative unrecognised actuarial losses. Paragraph 58A prohibits the recognition of a loss in these circumstances. For examples of the application of this paragraph, see Appendix C.

* A surplus is an excess of the fair value of the plan assets over the present value of the defined benefit obligation.

59. An asset may arise where a defined benefit plan has been overfunded or in certain cases where actuarial gains are recognised. An entity recognises an asset in such cases because:
- the entity controls a resource, which is the ability to use the surplus to generate future benefits;
 - that control is a result of past events (contributions paid by the entity and service rendered by the employee); and
 - 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.
60. The limit in paragraph 58(b) does not override the delayed recognition of certain actuarial losses (see paragraphs 92 and 93) and certain past service cost (see paragraph 96), other than as specified in paragraph 58A. However, that limit does override the transitional option in paragraph 155(b). Paragraph 120(c)(vi) requires an entity to disclose any amount not recognised as an asset because of the limit in paragraph limit in paragraph 58(b).

Example Illustrating Paragraph 60

A defined benefit plan has the following characteristics:

Present value of the obligation	1,100
Fair value of plan assets	(1,190)
	(90)
Unrecognised actuarial losses	(110)
Unrecognised past service cost	(70)
Unrecognised increase in the liability on initial adoption of the Standard under paragraph 155(b)	(50)
Negative amount determined under paragraph 54	<u>(320)</u>
Present value of available future refunds and reductions in future contributions	<u>90</u>

The limit under paragraph 58(b) is computed as follows:

<i>Unrecognised actuarial losses</i>	<i>110</i>
<i>Unrecognised past service cost</i>	<i>70</i>
<i>Present value of available future refunds and reductions in future contributions</i>	<i><u>90</u></i>
<i>Limit</i>	<i><u>270</u></i>

270 is less than 320. Therefore, the entity recognises an asset of 270 and discloses that the limit reduced the carrying amount of the asset by 50 (see paragraph 120(c)(vi)).

Income Statement

61. *An entity shall recognise the net total of the following amounts as expense or (subject to the limit in paragraph 58(b)) income, except to the extent that another Standard requires or permits their inclusion in the cost of an asset:*
- (a) *current service cost (see paragraphs 63-91);*
 - (b) *interest cost (see paragraph 82);*
 - (c) *the expected return on any plan assets (see paragraphs 105-107) and on any reimbursement rights (paragraph 104A);*
 - (d) *actuarial gains and losses, to the extent that they are recognised under paragraphs 92 and 93;*
 - (e) *past service cost, to the extent that paragraph 96 requires an entity to recognise it; and*
 - (f) *the effect of any curtailments or settlements (see paragraphs 109 and 110).*
62. Other Standards require the inclusion of certain employee benefit costs within the cost of assets such as inventories or property, plant and equipment (see IAS 2 *Inventories* and IAS 16 *Property, Plant and Equipment*). Any post-employment benefit costs included in the cost of such assets include the appropriate proportion of the components listed in paragraph 61.

Recognition and Measurement: Present Value of Defined Benefit Obligations and Current Service Cost

63. The ultimate cost of a defined benefit plan may be influenced by many variables, such as final salaries, employee turnover and mortality, medical cost trends and, for a funded plan, the investment earnings on the plan assets. 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 to:
- (a) apply an actuarial valuation method (see paragraphs 64-66);
 - (b) attribute benefit to periods of service (see paragraphs 67-71); and
 - (c) make actuarial assumptions (see paragraphs 72-91).

Actuarial Valuation Method

64. *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.*
65. 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 (see paragraphs 67-71) and measures each unit separately to build up the final obligation (see paragraphs 72-91).

Example Illustrating Paragraph 65

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. The following table shows how the obligation builds up for an employee who is expected to leave at the end of year 5, assuming that there are no changes in actuarial assumptions. For simplicity, this example ignores the additional adjustment needed to reflect the probability that the employee may leave the entity at an earlier or later date.

<i>Year</i>	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
<i>Benefit attributed to:</i>					
- <i>prior years</i>	<i>0</i>	<i>131</i>	<i>262</i>	<i>393</i>	<i>524</i>
- <i>current year (1% of final salary)</i>	<u><i>131</i></u>	<u><i>131</i></u>	<u><i>131</i></u>	<u><i>131</i></u>	<u><i>131</i></u>
- <i>current and prior years</i>	<u><i>131</i></u>	<u><i>262</i></u>	<u><i>393</i></u>	<u><i>524</i></u>	<u><i>655</i></u>
<i>Opening Obligation</i>	-	<i>89</i>	<i>196</i>	<i>324</i>	<i>476</i>
<i>Interest at 10%</i>	-	<i>9</i>	<i>20</i>	<i>33</i>	<i>48</i>
<i>Current Service Cost</i>	<u><i>89</i></u>	<u><i>98</i></u>	<u><i>108</i></u>	<u><i>119</i></u>	<u><i>131</i></u>
<i>Closing Obligation</i>	<u><u><i>89</i></u></u>	<u><u><i>196</i></u></u>	<u><u><i>324</i></u></u>	<u><u><i>476</i></u></u>	<u><u><i>655</i></u></u>

Note:

- 1. The Opening Obligation is the present value of benefit attributed to prior years.*
- 2. The Current Service Cost is the present value of benefit attributed to the current year.*
- 3. The Closing Obligation is the present value of benefit attributed to current and prior years.*

66. An entity discounts the whole of a post-employment benefit obligation, even if part of the obligation falls due within twelve months of the balance sheet date.

Attributing Benefit to Periods of Service

67. *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.*

68. 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 which 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.

Examples Illustrating Paragraph 68

1. A defined benefit plan provides a lump-sum benefit of 100 payable on retirement for each year of service.

A benefit of 100 is attributed to each year. The current service cost is the present value of 100. The present value of the defined benefit obligation is the present value of 100, multiplied by the number of years of service up to the balance sheet date.

If the benefit is payable immediately when the employee leaves the entity, the current service cost and the present value of the defined benefit obligation reflect the date at which the employee is expected to leave. Thus, because of the effect of discounting, they are less than the amounts that would be determined if the employee left at the balance sheet date.

2. A plan provides a monthly pension of 0.2% of final salary for each year of service. The pension is payable from the age of 65.

Benefit equal to the present value, at the expected retirement date, of a monthly pension of 0.2% of the estimated final salary payable from the expected retirement date until the expected date of death is attributed to each year of service. The current service cost is the present value of that benefit. The present value of the defined benefit obligation is the present value of monthly pension payments of 0.2% of final salary, multiplied by the number of years of service up to the balance sheet date. The current service cost and the present value of the defined benefit obligation are discounted because pension payments begin at the age of 65.

69. Employee service gives rise to an obligation under a defined benefit plan even if the benefits are conditional on future employment (in other words they are not vested). Employee service before the vesting date gives rise to a constructive obligation because, at each successive balance sheet date, the amount of future service that an employee will have to render before becoming entitled to the benefit is reduced. In measuring its defined benefit obligation, an entity considers the probability that some employees may not satisfy any vesting requirements. Similarly, although

certain post-employment benefits, for example, post-employment medical benefits, become payable only if a specified event occurs when an employee is no longer employed, an obligation is created when the employee renders service that will provide entitlement to the benefit if the specified event occurs. The probability that the specified event will occur affects the measurement of the obligation, but does not determine whether the obligation exists.

Examples Illustrating Paragraph 69

1. A plan pays a benefit of 100 for each year of service. The benefits vest after ten years of service.
A benefit of 100 is attributed to each year. In each of the first ten years, the current service cost and the present value of the obligation reflect the probability that the employee may not complete ten years of service.
2. A plan pays a benefit of 100 for each year of service, excluding service before the age of 25. The benefits vest immediately.
No benefit is attributed to service before the age of 25 because service before that date does not lead to benefits (conditional or unconditional). A benefit of 100 is attributed to each subsequent year.

70. The obligation increases until the date when further service by the employee will lead to no material amount of further benefits. Therefore, all benefit is attributed to periods ending on or before that date. Benefit is attributed to individual accounting periods 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 attributes benefit on a straight-line basis until the date when further service by the employee will lead to no material amount of further benefits. That is because the employee's service throughout the entire period will ultimately lead to benefit at that higher level.

Examples Illustrating Paragraph 70

1. A plan pays a lump-sum benefit of 1,000 that vests after ten years of service. The plan provides no further benefit for subsequent service.
A benefit of 100 (1,000 divided by ten) is attributed to each of the first ten years. The current service cost in each of the first ten years reflects the probability that the employee may not complete ten years of service. No benefit is attributed to subsequent years.

2. A plan pays a lump-sum retirement benefit of 2,000 to all employees who are still employed at the age of 55 after twenty years of service, or who are still employed at the age of 65, regardless of their length of service.
*For employees who join before the age of 35, service first leads to benefits under the plan at the age of 35 (an employee could leave at the age of 30 and return at the age of 33, with no effect on the amount or timing of benefits). Those benefits are conditional on further service. Also, service beyond the age of 55 will lead to no material amount of further benefits. For these employees, the entity attributes benefit of 100 (2,000 divided by 20) to each year from the age of 35 to the age of 55.
For employees who join between the ages of 35 and 45, service beyond twenty years will lead to no material amount of further benefits. For these employees, the entity attributes benefit of 100 (2,000 divided by 20) to each of the first twenty years.
For an employee who joins at the age of 55, service beyond ten years will lead to no material amount of further benefits. For this employee, the entity attributes benefit of 200 (2,000 divided by 10) to each of the first ten years.
For all employees, the current service cost and the present value of the obligation reflect the probability that the employee may not complete the necessary period of service.*

3. A post-employment medical plan reimburses 40% of an employee's post-employment medical costs if the employee leaves after more than ten and less than twenty years of service and 50% of those costs if the employee leaves after twenty or more years of service.
Under the plan's benefit formula, the entity attributes 4% of the present value of the expected medical costs (40% divided by ten) to each of the first ten years and 1% (10% divided by ten) to each of the second ten years. The current service cost in each year reflects the probability that the employee may not complete the necessary period of service to earn part or all of the benefits. For employees expected to leave within ten years, no benefit is attributed.

continued...

4. A post-employment medical plan reimburses 10% of an employee's post-employment medical costs if the employee leaves after more than ten and less than twenty years of service and 50% of those costs if the employee leaves after twenty or more years of service.

Service in later years will lead to a materially higher level of benefit than in earlier years. Therefore, for employees expected to leave after twenty or more years, the entity attributes benefit on a straight-line basis under paragraph 68. Service beyond twenty years will lead to no material amount of further benefits. Therefore, the benefit attributed to each of the first twenty years is 2.5% of the present value of the expected medical costs (50% divided by twenty).

For employees expected to leave between ten and twenty years, the benefit attributed to each of the first ten years is 1% of the present value of the expected medical costs. For these employees, no benefit is attributed to service between the end of the tenth year and the estimated date of leaving.

For employees expected to leave within ten years, no benefit is attributed.

71. Where the amount of a benefit is a constant proportion of final salary for each year of service, future salary increases will affect the amount required to settle the obligation that exists for service before the balance sheet date, but do not create an additional obligation. Therefore:
- (a) for the purpose of paragraph 67(b), salary increases do not lead to further benefits, even though the amount of the benefits is dependent on final salary; and
 - (b) the amount of benefit attributed to each period is a constant proportion of the salary to which the benefit is linked.

Example Illustrating Paragraph 71

Employees are entitled to a benefit of 3% of final salary for each year of service before the age of 55.

Benefit of 3% of estimated final salary is attributed to each year up to the age of 55. This is the date when further service by the employee will lead to no material amount of further benefits under the plan. No benefit is attributed to service after that age.

Actuarial Assumptions

72. *Actuarial assumptions shall be unbiased and mutually compatible.*
73. 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, both during and after employment;
 - (ii) rates of employee turnover, disability and early retirement;
 - (iii) the proportion of plan members with dependants who will be eligible for benefits; and
 - (iii) claim rates under medical plans; and
 - (b) financial assumptions, dealing with items such as:
 - (i) the discount rate (see paragraphs 78-82);
 - (ii) future salary and benefit levels (see paragraphs 83-87);
 - (iii) in the case of medical benefits, future medical costs, including, where material, the cost of administering claims and benefit payments (see paragraphs 88-91); and
 - (iv) the expected rate of return on plan assets (see paragraphs 105-107).
74. Actuarial assumptions are unbiased if they are neither imprudent nor excessively conservative.
75. Actuarial assumptions are mutually compatible if they reflect the economic relationships between factors such as inflation, rates of salary increase, the return on plan assets and discount rates. For example, all assumptions which 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.
76. An entity determines the discount rate and other financial assumptions in nominal (stated) terms, unless estimates in real (inflation-adjusted) terms are more reliable, for example, in a hyper-inflationary economy (see IAS 29 *Financial Reporting in Hyperinflationary Economies*), or where the benefit is index-linked and there is a deep market in index-linked bonds of the same currency and term.
77. ***Financial assumptions shall be based on market expectations, at the balance sheet date, for the period over which the obligations are to be settled.***

Actuarial Assumptions: Discount Rate

78. ***The rate used to discount post-employment benefit obligations (both funded and unfunded) shall be determined by reference to market yields at the balance sheet date on high quality corporate bonds. In countries where there is no deep market in such bonds, the market yields (at the balance sheet date) 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.***

79. One actuarial assumption which has a material effect is the discount rate. The discount rate reflects the time value of money but not the actuarial or investment risk. Furthermore, the discount rate does not reflect the entity-specific credit risk borne by the entity's creditors, nor does it reflect the risk that future experience may differ from actuarial assumptions.
80. The discount rate reflects the estimated timing of benefit payments. In practice, an entity often achieves this by applying a single weighted average discount rate that reflects the estimated timing and amount of benefit payments and the currency in which the benefits are to be paid.
81. In some cases, there may be no deep market in bonds with a sufficiently long maturity to match the estimated maturity of all the benefit payments. In such cases, an entity uses current market rates of the appropriate term to discount shorter term payments, and estimates the discount rate for longer maturities by extrapolating current market rates along the yield curve. The total present value of a defined benefit obligation is unlikely to be particularly sensitive to the discount rate applied to the portion of benefits that is payable beyond the final maturity of the available corporate or government bonds.
82. Interest cost is computed by multiplying the discount rate as determined at the start of the period by the present value of the defined benefit obligation throughout that period, taking account of any material changes in the obligation. The present value of the obligation will differ from the liability recognised in the balance sheet because the liability is recognised after deducting the fair value of any plan assets and because some actuarial gains and losses, and some past service cost, are not recognised immediately. [Appendix A illustrates the computation of interest cost, among other things]

Actuarial Assumptions: Salaries, Benefits and Medical Costs

83. *Post-employment benefit obligations shall be measured on a basis that reflects:*
- (a) estimated future salary increases;*
 - (b) the benefits set out in the terms of the plan (or resulting from any constructive obligation that goes beyond those terms) at the balance sheet date; and*
 - (c) 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 balance sheet date; or*
 - (ii) past history, or other reliable evidence, indicates 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.*
84. Estimates of future salary increases take account of inflation, seniority, promotion and other relevant factors, such as supply and demand in the employment market.

85. If the formal terms of a plan (or a constructive obligation that goes beyond those terms) require an entity to change benefits in future periods, the measurement of the obligation reflects those changes. This is the case when, for example:
- (a) the entity has a past history of increasing benefits, for example, to mitigate the effects of inflation, and there is no indication that this practice will change in the future; or
 - (b) actuarial gains have already been recognised in the financial statements and the entity is obliged, by either the formal terms of a plan (or a constructive obligation that goes beyond those terms) or legislation, to use any surplus in the plan for the benefit of plan participants (see paragraph 98(c)).
86. Actuarial assumptions do not reflect future benefit changes that are not set out in the formal terms of the plan (or a constructive obligation) at the balance sheet date. Such changes will result in:
- (a) past service cost, to the extent that they change benefits for service before the change; and
 - (b) current service cost for periods after the change, to the extent that they change benefits for service after the change.
87. Some post-employment benefits are linked to variables such as the level of state retirement benefits or state medical care. The measurement of such benefits reflects expected changes in such variables, based on past history and other reliable evidence.
88. ***Assumptions about medical costs shall take account of estimated future changes in the cost of medical services, resulting from both inflation and specific changes in medical costs.***
89. Measurement of post-employment medical benefits requires assumptions about the level and frequency of future claims and the cost of meeting those claims. An entity estimates future medical costs on the basis of historical data about the entity's own experience, supplemented where necessary by historical data from other entities, insurance companies, medical providers or other sources. Estimates of future medical costs consider the effect of technological advances, changes in health care utilisation or delivery patterns and changes in the health status of plan participants.
90. The level and frequency of claims is particularly sensitive to the age, health status and sex of employees (and their dependants) and may be sensitive to other factors such as geographical location. Therefore, historical data is adjusted to the extent that the demographic mix of the population differs from that of the population used as a basis for the historical data. It is also adjusted where there is reliable evidence that historical trends will not continue.

91. Some post-employment health care plans require employees to contribute to the medical costs covered by the plan. Estimates of future medical costs take account of any such contributions, based on the terms of the plan at the balance sheet date (or based on any constructive obligation that goes beyond those terms). Changes in those employee contributions result in past service cost or, where applicable, curtailments. The cost of meeting claims may be reduced by benefits from state or other medical providers (see paragraphs 83(c) and 87).

Actuarial Gains and Losses

92. *In measuring its defined benefit liability under paragraph 54, an entity shall, subject to paragraph 58A, recognise a portion (as specified in paragraph 93) of its actuarial gains and losses as income or expense if the net cumulative unrecognised actuarial gains and losses at the end of the previous reporting period exceeded the greater of:*

- (a) *10% of the present value of the defined benefit obligation at that date (before deducting plan assets); and*
- (a) *10% of the fair value of any plan assets at that date.*

These limits shall be calculated and applied separately for each defined benefit plan.

93. *The portion of actuarial gains and losses to be recognised for each defined benefit plan is the excess determined under paragraph 92, divided by the expected average remaining working lives of the employees participating in that plan. However, an entity may adopt any systematic method that results in faster recognition of actuarial gains and losses, provided that the same basis is applied to both gains and losses and the basis is applied consistently from period to period. An entity may apply such systematic methods to actuarial gains and losses even if they fall within the limits specified in paragraph 92.*

94. Actuarial gains and losses may result from increases or decreases in either the present value of a defined benefit obligation or the fair value of any related plan assets. 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 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;
 - (c) the effect of changes in the discount rate; and
 - (d) differences between the actual return on plan assets and the expected return on plan assets (see paragraphs 105-107).

95. In the long term, actuarial gains and losses may offset one another. Therefore, estimates of post-employment benefit obligations are best viewed as a range (or ‘corridor’) around the best estimate. An entity is permitted, but not required, to recognise actuarial gains and losses that fall within that range. This Standard requires an entity to recognise, as a minimum, a specified portion of the actuarial gains and losses that fall outside a ‘corridor’ of plus or minus 10%. [Appendix A illustrates the treatment of actuarial gains and losses, among other things] The Standard also permits systematic methods of faster recognition, provided that those methods satisfy the conditions set out in paragraph 93. Such permitted methods include, for example, immediate recognition of all actuarial gains and losses, both within and outside the ‘corridor’. Paragraph 155(b)(iii) explains the need to consider any unrecognised part of the transitional liability in accounting for subsequent actuarial gains.

Past Service Cost

96. *In measuring its defined benefit liability under paragraph 54, an entity shall, subject to paragraph 58A, recognise past service cost as an expense on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits are already vested immediately following the introduction of, or changes to, a defined benefit plan, an entity shall recognise past service cost immediately.*
97. Past service cost arises when an entity introduces a defined benefit plan or changes the benefits payable under an existing defined benefit plan. Such changes are in return for employee service over the period until the benefits concerned are vested. Therefore, past service cost is recognised over that period, regardless of the fact that the cost refers to employee service in previous periods. Past service cost is measured as the change in the liability resulting from the amendment (see paragraph 64).

Example Illustrating Paragraph 97

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:

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)	<u>120</u>
	<u>270</u>

The entity recognises 150 immediately because those benefits are already vested. The entity recognises 120 on a straight-line basis over three years from 1 January 20X5.

98. Past service cost excludes:
- (a) the effect of differences between actual and previously assumed salary increases on the obligation to pay benefits for service in prior years (there is no past service cost because actuarial assumptions allow for projected salaries);
 - (b) under and over estimates of discretionary pension increases where an entity has a constructive obligation to grant such increases (there is no past service cost because actuarial assumptions allow for such increases);
 - (c) estimates of benefit improvements that result from actuarial gains that have already been recognised in the financial statements if the entity is obliged, by either the formal terms of a plan (or a constructive obligation that goes beyond those terms) or legislation, to use any surplus in the plan for the benefit of plan participants, even if the benefit increase has not yet been formally awarded (the resulting increase in the obligation is an actuarial loss and not past service cost, see paragraph 85(b));
 - (d) the increase in vested benefits when, in the absence of new or improved benefits, employees complete vesting requirements (there is no past service cost because the estimated cost of benefits was recognised as current service cost as the service was rendered); and
 - (e) the effect of plan amendments that reduce benefits for future service (a curtailment).
99. An entity establishes the amortisation schedule for past service cost when the benefits are introduced or changed. It would be impracticable to maintain the detailed records needed to identify and implement subsequent changes in that amortisation schedule. Moreover, the effect is likely to be material only where there is a curtailment or settlement. Therefore, an entity amends the amortisation schedule for past service cost only if there is a curtailment or settlement.
100. Where an entity reduces benefits payable under an existing defined benefit plan, the resulting reduction in the defined benefit liability is recognised as (negative) past service cost over the average period until the reduced portion of the benefits becomes vested.
101. Where an entity reduces certain benefits payable under an existing defined benefit plan and, at the same time, increases other benefits payable under the plan for the same employees, the entity treats the change as a single net change.

Recognition and Measurement: Plan Assets

Fair Value of Plan Assets

102. The fair value of any plan assets is deducted in determining the amount recognised in the balance sheet under paragraph 54. 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).

103. 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.
104. 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, as described in paragraph 54 (subject to any reduction required if the amounts receivable under the insurance policies are not recoverable in full).

Reimbursements

- 104A.** *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 recognise its right to reimbursement as a separate asset. The entity shall measure the asset at fair value. In all other respects, an entity shall treat that asset in the same way as plan assets. In the income statement, the expense relating to a defined benefit plan may be presented net of the amount recognised for a reimbursement.*
- 104B. Sometimes, an entity is able to look to another party, such as an insurer, to pay part or all of the expenditure required to settle a defined benefit obligation. Qualifying insurance policies, as defined in paragraph 7, are plan assets. An entity accounts for qualifying insurance policies in the same way as for all other plan assets and paragraph 104A does not apply (see paragraphs 39-42 and 104).
- 104C. When an insurance policy is not a qualifying insurance policy, that insurance policy is not a plan asset. Paragraph 104A deals with such cases: the entity recognises its right to reimbursement under the insurance policy as a separate asset, rather than as a deduction in determining the defined benefit liability recognised under paragraph 54; in all other respects, the entity treats that asset in the same way as plan assets. In particular, the defined benefit liability recognised under paragraph 54 is increased (reduced) to the extent that net cumulative actuarial gains (losses) on the defined benefit obligation and on the related reimbursement right remain unrecognised under paragraphs 92 and 93. Paragraph 120(c)(vii) requires the entity to disclose a brief description of the link between the reimbursement right and the related obligation.

Example Illustrating Paragraphs 104A-C	
Present value of obligation	1,241
Unrecognised actuarial gains	17
Liability recognised in balance sheet	<u>1,258</u>
Rights under insurance policies that exactly match the amount and timing of some of the benefits payable under the plan. Those benefits have a present value of 1,092.	<u>1,092</u>
The unrecognised actuarial gains of 17 are the net cumulative actuarial gains on the obligation and on the reimbursement rights.	

104D. If the right to reimbursement arises under an insurance policy that exactly matches the amount and timing of some or all of the benefits payable under a defined benefit plan, the fair value of the reimbursement right is deemed to be the present value of the related obligation, as described in paragraph 54 (subject to any reduction required if the reimbursement is not recoverable in full).

Return on Plan Assets

105. The expected return on plan assets is one component of the expense recognised in the income statement. The difference between the expected return on plan assets and the actual return on plan assets is an actuarial gain or loss; it is included with the actuarial gains and losses on the defined benefit obligation in determining the net amount that is compared with the limits of the 10% ‘corridor’ specified in paragraph 92.
106. The expected return on plan assets is based on market expectations, at the beginning of the period, for returns over the entire life of the related obligation. The expected return on plan assets reflects changes in the fair value of plan assets held during the period as a result of actual contributions paid into the fund and actual benefits paid out of the fund.

Example Illustrating Paragraph 106

At 1 January 20X1, the fair value of plan assets was 10,000 and net cumulative unrecognised 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
Realised and unrealised gains on plan assets (after tax)	2.00
Administration costs	<u>(1.00)</u>
Expected rate of return	<u>10.25</u>

For 20X1, the expected and actual return on plan assets are as follows:

<i>Return on 10,000 held for 12 months at 10.25%</i>	<i>1,025</i>
<i>Return on 3,000 held for six months at 5% (equivalent to 10.25% annually, compounded every six months)</i>	<i><u>150</u></i>
<i>Expected return on plan assets for 20X1</i>	<i><u>1,175</u></i>
<i>Fair value of plan assets at 31 December 20X1</i>	<i>15,000</i>
<i>Less fair value of plan assets at 1 January 20X1</i>	<i>(10,000)</i>
<i>Less contributions received</i>	<i>(4,900)</i>
<i>Add benefits paid</i>	<i><u>1,900</u></i>
<i>Actual return on plan assets</i>	<i><u>2,000</u></i>

The difference between the expected return on plan assets (1,175) and the actual return on plan assets (2,000) is an actuarial gain of 825. Therefore, the cumulative net unrecognised actuarial gains are 1,525 (760 plus 825 less 60). Under paragraph 92, the limits of the corridor are set at 1,500 (greater of: (i) 10% of 15,000 and (ii) 10% of 14,792). In the following year (20X2), the entity recognises in the income statement an actuarial gain of 25 (1,525 less 1,500) divided by the expected average remaining working life of the employees concerned.

The expected return on plan assets for 20X2 will be based on market expectations at 1/1/X2 for returns over the entire life of the obligation.

107. In determining the expected and actual return on plan assets, an entity deducts expected administration costs, other than those included in the actuarial assumptions used to measure the obligation.

Business Combinations

108. In a business combination, an entity recognises assets and liabilities arising from post-employment benefits at the present value of the obligation less the fair value of any plan assets (see IFRS 3 *Business Combinations*). The present value of the obligation includes all of the following, even if the acquiree had not yet recognised them at the acquisition date:
- (a) actuarial gains and losses that arose before the acquisition date (whether or not they fell inside the 10% ‘corridor’);
 - (b) past service cost that arose from benefit changes, or the introduction of a plan, before the acquisition date; and
 - (c) amounts that, under the transitional provisions of paragraph 155(b), the acquiree had not recognised.

Curtailments and Settlements

109. *An entity shall recognise gains or losses on the curtailment or settlement of a defined benefit plan when the curtailment or settlement occurs. The gain or loss on a curtailment or settlement shall comprise:*
- (a) *any resulting change in the present value of the defined benefit obligation;*
 - (b) *any resulting change in the fair value of the plan assets;*
 - (c) *any related actuarial gains and losses and past service cost that, under paragraphs 92 and 96, had not previously been recognised.*
110. *Before determining the effect of a curtailment or settlement, an entity shall remeasure the obligation (and the related plan assets, if any) using current actuarial assumptions (including current market interest rates and other current market prices).*
111. A curtailment occurs when an entity either:
- (a) is demonstrably committed 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, such as the closing of a plant, discontinuance of an operation or termination or suspension of a plan. An event is material enough to qualify as a curtailment if the recognition of a curtailment gain or loss would have a material effect on the financial statements. Curtailments are often linked with a restructuring. Therefore, an entity accounts for a curtailment at the same time as for a related restructuring.

112. A settlement occurs when an entity enters into a transaction that eliminates all further legal or constructive obligation for part or all of the benefits provided under a defined benefit plan, for example, when a lump-sum cash payment is made to, or on behalf of, plan participants in exchange for their rights to receive specified post-employment benefits.
113. In some cases, an entity acquires an insurance policy to fund some or all of the employee benefits relating to employee service in the current and prior periods. The acquisition of such a policy is not a settlement if the entity retains a legal or constructive obligation (see paragraph 39) to pay further amounts if the insurer does not pay the employee benefits specified in the insurance policy. Paragraphs 104A-104D deal with the recognition and measurement of reimbursement rights under insurance policies that are not plan assets.
114. A settlement occurs together with a curtailment if a plan is terminated such that the obligation is settled and the plan ceases to exist. However, the termination of a plan is not a curtailment or settlement if the plan is replaced by a new plan that offers benefits that are, in substance, identical.
115. Where a curtailment relates to only some of the employees covered by a plan, or where only part of an obligation is settled, the gain or loss includes a proportionate share of the previously unrecognised past service cost and actuarial gains and losses (and of transitional amounts remaining unrecognised under paragraph 155(b)). The proportionate share is determined on the basis of the present value of the obligations before and after the curtailment or settlement, unless another basis is more rational in the circumstances. For example, it may be appropriate to apply any gain arising on a curtailment or settlement of the same plan to first eliminate any unrecognised past service cost relating to the same plan.

Example Illustrating Paragraph 115

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 (including current market interest rates and other current market prices) 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 unrecognised 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 recognise over five years (see paragraph 155(b)). The curtailment reduces the net present value of the obligation by 100 to 900.

Of the previously unrecognised actuarial gains and transitional amounts, 10% (100/1,000) relates to the part of the obligation that was eliminated through the curtailment. Therefore, the effect of the curtailment is as follows:

	<i>Before curtailment</i>	<i>Curtailment gain</i>	<i>After curtailment</i>
<i>Net present value of obligation</i>	1,000	(100)	900
<i>Fair value of plan assets</i>	<u>(820)</u>	<u>-</u>	<u>(820)</u>
	180	(100)	80
<i>Unrecognised actuarial gains</i>	50	(5)	45
<i>Unrecognised transitional amount (100 X 4/5)</i>	(80)	8	(72)
<i>Net liability recognised in balance sheet</i>	<u>150</u>	<u>(97)</u>	<u>53</u>

Presentation**Offset**

116. *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 realise the surplus in one plan and settle its obligation under the other plan simultaneously.*

117. The offsetting criteria are similar to those established for financial instruments in IAS 32 *Financial Instruments: Disclosure and Presentation*.

Current / Non-current Distinction

118. 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.

Financial Components of Post-employment Benefit Costs

119. This Standard does not specify whether an entity should present current service cost, interest cost and the expected return on plan assets as components of a single item of income or expense on the face of the income statement.

Disclosure

120. *An entity shall disclose the following information about defined benefit plans:*
- (a) the entity's accounting policy for recognising actuarial gains and losses;*
 - (b) a general description of the type of plan;*
 - (c) a reconciliation of the assets and liabilities recognised in the balance sheet, showing at least:*
 - (i) the present value at the balance sheet date of defined benefit obligations that are wholly unfunded;*
 - (ii) the present value (before deducting the fair value of plan assets) at the balance sheet date of defined benefit obligations that are wholly or partly funded;*
 - (iii) the fair value of any plan assets at the balance sheet date;*
 - (iv) the net actuarial gains or losses not recognised in the balance sheet (see paragraph 92);*
 - (v) the past service cost not yet recognised in the balance sheet (see paragraph 96);*
 - (vi) any amount not recognised as an asset, because of the limit in paragraph 58(b);*
 - (vii) the fair value at the balance sheet date of any reimbursement right recognised as an asset under paragraph 104A (with a brief description of the link between the reimbursement right and the related obligation); and*
 - (viii) the other amounts recognised in the balance sheet;*
 - (d) the amounts included in the fair value of plan assets for:*
 - (i) each category of the reporting entity's own financial instruments; and*
 - (ii) any property occupied by, or other assets used by, the reporting entity;*
 - (e) a reconciliation showing the movements during the period in the net liability (or asset) recognised in the balance sheet;*

- (f) *the total expense recognised in the income statement for each of the following, and the line item(s) of the income statement in which they are included:*
- (i) *current service cost;*
 - (ii) *interest cost;*
 - (iii) *expected return on plan assets;*
 - (iv) *expected return on any reimbursement right recognised as an asset under paragraph 104A;*
 - (v) *actuarial gains and losses;*
 - (vi) *past service cost; and*
 - (vii) *the effect of any curtailment or settlement;*
- (g) *the actual return on plan assets, as well as the actual return on any reimbursement right recognised as an asset under paragraph 104A; and*
- (h) *the principal actuarial assumptions used as at the balance sheet date, including, where applicable:*
- (i) *the discount rates;*
 - (ii) *the expected rates of return on any plan assets for the periods presented in the financial statements;*
 - (iii) *the expected rates of return for the periods presented in the financial statements on any reimbursement right recognised as an asset under paragraph 104A;*
 - (iv) *the expected rates of salary increases (and of changes in an index or other variable specified in the formal or constructive terms of a plan as the basis for future benefit increases);*
 - (v) *medical cost trend rates; and*
 - (vi) *any other material actuarial assumptions used.*

An entity shall disclose each actuarial assumption in absolute terms (for example, as an absolute percentage) and not just as a margin between different percentages or other variables.

121. Paragraph 120(b) requires a general description of the type of plan. Such a description distinguishes, for example, flat salary pension plans from final salary pension plans and from post-employment medical plans. Further detail is not required.
122. When an entity has more than one defined benefit plan, disclosures may be made in total, separately for each plan, or in such groupings as are considered to be the most useful. It may be useful to distinguish groupings by criteria such as the following:
- (a) the geographical location of the plans, for example, by distinguishing domestic plans from foreign plans; or

- (b) whether plans are subject to materially different risks, for example, by distinguishing flat salary pension plans from final salary pension plans and from post-employment medical plans.

When an entity provides disclosures in total for a grouping of plans, such disclosures are provided in the form of weighted averages or of relatively narrow ranges.

- 123. Paragraph 30 requires additional disclosures about multi-employer defined benefit plans that are treated as if they were defined contribution plans.
- 124. Where required by IAS 24 *Related Party Disclosures* an entity discloses information about:
 - (a) related party transactions with post-employment benefit plans; and
 - (b) post-employment benefits for key management personnel.
- 125. Where required by IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* an entity discloses information about contingent liabilities arising from post-employment benefit obligations.

Other Long-term Employee Benefits

- 126. Other long-term employee benefits include, for example:
 - (a) long-term compensated 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 payable twelve months or more after the end of the period in which the employees render the related service; and
 - (e) deferred compensation paid twelve months or more after the end of the period in which it is earned.
- 127. 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. Furthermore, the introduction of, or changes to, other long-term employee benefits rarely causes a material amount of past service cost. For these reasons, this Standard requires a simplified method of accounting for other long-term employee benefits. This method differs from the accounting required for post-employment benefits as follows:
 - (a) actuarial gains and losses are recognised immediately and no ‘corridor’ is applied; and
 - (b) all past service cost is recognised immediately.

Recognition and Measurement

- 128. *The amount recognised as a liability for other long-term employee benefits shall be the net total of the following amounts:*

- (a) *the present value of the defined benefit obligation at the balance sheet date (see paragraph 64);*
- (b) *minus the fair value at the balance sheet date of plan assets (if any) out of which the obligations are to be settled directly (see paragraphs 102-104).*

In measuring the liability, an entity shall apply paragraphs 49-91, excluding paragraphs 54 and 61. An entity shall apply paragraph 104A in recognising and measuring any reimbursement right.

129. *For other long-term employee benefits, an entity shall recognise the net total of the following amounts as expense or (subject to paragraph 58) income, except to the extent that another Standard requires or permits their inclusion in the cost of an asset:*
- (a) *current service cost (see paragraphs 63-91);*
 - (b) *interest cost (see paragraph 82);*
 - (c) *the expected return on any plan assets (see paragraphs 105-107) and on any reimbursement right recognised as an asset (see paragraph 104A);*
 - (d) *actuarial gains and losses, which shall all be recognised immediately;*
 - (e) *past service cost, which shall all be recognised immediately; and*
 - (f) *the effect of any curtailments or settlements (see paragraphs 109 and 110).*
130. One form of other long-term employee benefit is long-term disability benefit. If the level of benefit depends on the length of service, an obligation arises when the service is rendered. Measurement of that obligation reflects the probability that payment will be required and the length of time for which payment is expected to be made. If the level of benefit is the same for any disabled employee regardless of years of service, the expected cost of those benefits is recognised when an event occurs that causes a long-term disability.

Disclosure

131. Although this Standard does not require specific disclosures about other long-term employee benefits, other Standards may require disclosures, for example, where the expense resulting from such benefits is material and so would require disclosure in accordance with IAS 1 *Presentation of Financial Statements*. When required by IAS 24 *Related Party Disclosures*, an entity discloses information about other long-term employee benefits for key management personnel.

Termination Benefits

132. This Standard deals with termination benefits separately from other employee benefits because the event which gives rise to an obligation is the termination rather than employee service.

Recognition

- 133. An entity shall recognise termination benefits as a liability and an expense when, and only when, the entity is demonstrably committed to either:**
- (a) terminate the employment of an employee or group of employees before the normal retirement date; or**
 - (b) provide termination benefits as a result of an offer made in order to encourage voluntary redundancy.**
- 134. An entity is demonstrably committed to a termination when, and only when, the entity has a detailed formal plan for the termination and is without realistic possibility of withdrawal. The detailed plan shall include, as a minimum:**
- (a) the location, function, and approximate number of employees whose services are to be terminated;**
 - (b) the termination benefits for each job classification or function; and**
 - (c) the time at which the plan will be implemented. Implementation shall begin as soon as possible and the period of time to complete implementation shall be such that material changes to the plan are not likely.**
135. An entity may be committed, by legislation, by contractual or other agreements with employees or their representatives or by a constructive obligation based on business practice, custom or a desire to act equitably, to make payments (or provide other benefits) to employees when it terminates their employment. Such payments are termination benefits. Termination benefits are typically lump-sum payments, but sometimes also include:
- (a) enhancement of retirement benefits or of other post-employment benefits, either indirectly through an employee benefit plan or directly; and
 - (b) salary until the end of a specified notice period if the employee renders no further service that provides economic benefits to the entity.
136. Some employee benefits are payable regardless of the reason for the employee's departure. The payment of such benefits is certain (subject to any vesting or minimum service requirements) but the timing of their payment is uncertain. Although such benefits are described in some countries as termination indemnities, or termination gratuities, they are post-employment benefits, rather than termination benefits and an entity accounts for them as post-employment benefits. Some entities provide a lower level of benefit for voluntary termination at the request of the employee (in substance, a post-employment benefit) than for involuntary termination at the request of the entity. The additional benefit payable on involuntary termination is a termination benefit.
137. Termination benefits do not provide an entity with future economic benefits and are recognised as an expense immediately.
138. Where an entity recognises termination benefits, the entity may also have to account for a curtailment of retirement benefits or other employee benefits (see paragraph 109).

Measurement

139. *Where termination benefits fall due more than 12 months after the balance sheet date, they shall be discounted using the discount rate specified in paragraph 78.*
140. *In the case of an offer made to encourage voluntary redundancy, the measurement of termination benefits shall be based on the number of employees expected to accept the offer.*

Disclosure

141. Where there is uncertainty about the number of employees who will accept an offer of termination benefits, a contingent liability exists. As required by IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* an entity discloses information about the contingent liability unless the possibility of an outflow in settlement is remote.
142. As required by IAS 1, an entity discloses the nature and amount of an expense if it is material. Termination benefits may result in an expense needing disclosure in order to comply with this requirement.
143. Where required by IAS 24 *Related Party Disclosures* an entity discloses information about termination benefits for key management personnel.
- 144.-152.[Deleted]

Transitional Provisions

153. This section specifies the transitional treatment for defined benefit plans. Where an entity first adopts this Standard for other employee benefits, the entity applies IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.
154. *On first adopting this Standard, an entity shall determine its transitional liability for defined benefit plans at that date as:*
- (a) *the present value of the obligation (see paragraph 64) at the date of adoption;*
 - (b) *minus the fair value, at the date of adoption, of plan assets (if any) out of which the obligations are to be settled directly (see paragraphs 102-104);*
 - (c) *minus any past service cost that, under paragraph 96, shall be recognised in later periods.*
155. *If the transitional liability is more than the liability that would have been recognised at the same date under the entity's previous accounting policy, the entity shall make an irrevocable choice to recognise that increase as part of its defined benefit liability under paragraph 54:*
- (a) *immediately, under IAS 8; or*
 - (b) *as an expense on a straight-line basis over up to five years from the date of adoption. If an entity chooses (b), the entity shall:*

- (i) *apply the limit described in paragraph 58(b) in measuring any asset recognised in the balance sheet;*
- (ii) *disclose at each balance sheet date: (1) the amount of the increase that remains unrecognised; and (2) the amount recognised in the current period;*
- (iii) *limit the recognition of subsequent actuarial gains (but not negative past service cost) as follows. If an actuarial gain is to be recognised under paragraphs 92 and 93, an entity shall recognise that actuarial gain only to the extent that the net cumulative unrecognised actuarial gains (before recognition of that actuarial gain) exceed the unrecognised part of the transitional liability; and*
- (iv) *include the related part of the unrecognised transitional liability in determining any subsequent gain or loss on settlement or curtailment.*

If the transitional liability is less than the liability that would have been recognised at the same date under the entity's previous accounting policy, the entity shall recognise that decrease immediately under IAS 8.

156. On the initial adoption of the Standard, the effect of the change in accounting policy includes all actuarial gains and losses that arose in earlier periods even if they fall inside the 10% 'corridor' specified in paragraph 92.

Example Illustrating Paragraphs 154 to 156

At 31 December 1998, an entity's balance sheet includes a pension liability of 100. The entity adopts the Standard as of 1 January 1999, when the present value of the obligation under the Standard is 1,300 and the fair value of plan assets is 1,000. On 1 January 1993, the entity had improved pensions (cost for non-vested benefits: 160; and average remaining period at that date until vesting: 10 years).

The transitional effect is as follows:

<i>Present value of the obligation</i>	1,300
<i>Fair value of plan assets</i>	(1,000)
<i>Less: past service cost to be recognised in later periods (160 x 4/10)</i>	<u>(64)</u>
<i>Transitional liability</i>	236
<i>Liability already recognised</i>	<u>100</u>
<i>Increase in liability</i>	<u><u>136</u></u>

The entity may choose to recognise the increase of 136 either immediately or over up to 5 years. The choice is irrevocable.

At 31 December 1999, the present value of the obligation under the Standard is 1,400 and the fair value of plan assets is 1,050. Net cumulative unrecognised actuarial gains since the date of adopting the Standard are 120. The expected average remaining working life of the employees participating in the plan was eight years. The entity has adopted a policy of recognising all actuarial gains and losses immediately, as permitted by paragraph 93.

The effect of the limit in paragraph 155(b)(iii) is as follows.

<i>Net cumulative unrecognised actuarial gains</i>	120
<i>Unrecognised part of transitional liability (136 x 4/5)</i>	<u>(109)</u>
<i>Maximum gain to be recognised (paragraph 155(b)(iii))</i>	<u><u>11</u></u>

Effective Date

157. *This Standard becomes operative for financial statements covering periods beginning on or after 1 January 1999, except as specified in paragraphs 159 and 159A. Earlier adoption is encouraged. If an entity applies this Standard to retirement benefit costs for financial statements covering periods beginning before 1 January 1999, the entity shall disclose the fact that it has applied this Standard instead of IAS 19 Retirement Benefit Costs approved in 1993.*
158. This Standard supersedes IAS 19 Retirement Benefit Costs approved in 1993.

159. The following become operative for annual financial statements* covering periods beginning on or after 1 January 2001:

- (a) the revised definition of plan assets in paragraph 7 and the related definitions of assets held by a long-term employee benefit fund and qualifying insurance policy; and**
- (b) the recognition and measurement requirements for reimbursements in paragraphs 104A, 128 and 129 and related disclosures in paragraphs 120(c)(vii), 120(f)(iv), 120(g) and 120(h)(iii).**

Earlier adoption is encouraged. If earlier adoption affects the financial statements, an entity shall disclose that fact.

159A. The amendment in paragraph 58A becomes operative for annual financial statements* covering periods ending on or after 31 May 2002. Earlier adoption is encouraged. If earlier adoption affects the financial statements, an entity shall disclose that fact.

160. IAS 8 applies when an entity changes its accounting policies to reflect the changes specified in paragraphs 159 and 159A. In applying those changes retrospectively, as required by IAS 8, the entity treats those changes as if they had been applied at the same time as the rest of this Standard.

* Paragraphs 159 and 159A refer to “annual financial statements” in line with more explicit language for writing effective dates adopted in 1998. Paragraph 157 refers to “financial statements”.

Appendix A

Illustrative Example

The appendix accompanies, but is not part of, IAS 19. Extracts from income statements and balance sheets are provided to show the effects of the transactions described below. These extracts do not necessarily conform with all the disclosure and presentation requirements of other Standards.

Background Information

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 unrecognised actuarial gains at that date were 140.

	20X1	20X2	20X3
Discount rate at start of year	10.0%	9.0%	8.0%
Expected rate of return on plan assets at start of year	12.0%	11.1%	10.3%
Current service 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
Expected average remaining working lives of employees (years)	10	10	10

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; the past service cost arising from additional non-vested benefits is therefore recognised on a straight-line basis over three years. The past service cost arising from additional vested benefits is recognised immediately (paragraph 96 of the Standard). The entity has adopted a policy of recognising actuarial gains and losses under the minimum requirements of paragraph 93.

Changes in the Present Value of the Obligation and in the Fair Value of the Plan Assets

The first step is to summarise the changes in the present value of the obligation and in the fair value of the plan assets and use this to determine the amount of the actuarial gains or losses for the period. These are as follows:

	<i>20X1</i>	<i>20X2</i>	<i>20X3</i>
Present value of obligation, 1 January	1,000	1,141	1,197
Interest cost	100	103	96
Current service cost	130	140	150
Past service cost—non-vested benefits	-	30	-
Past service cost—vested benefits	-	50	-
Benefits paid	(150)	(180)	(190)
Actuarial (gain) loss on obligation (balancing figure)	61	(87)	42
Present value of obligation, 31 December	<u>1,141</u>	<u>1,197</u>	<u>1,295</u>
Fair value of plan assets, 1 January	1,000	1,092	1,109
Expected return on plan assets	120	121	114
Contributions	90	100	110
Benefits paid	(150)	(180)	(190)
Actuarial gain (loss) on plan assets (balancing figure)	32	(24)	(50)
Fair value of plan assets, 31 December	<u>1,092</u>	<u>1,109</u>	<u>1,093</u>

Limits of the ‘Corridor’

The next step is to determine the limits of the corridor and then compare these with the cumulative unrecognised actuarial gains and losses in order to determine the net actuarial gain or loss to be recognised in the following period. Under paragraph 92 of the Standard, the limits of the ‘corridor’ are set at the greater of:

- (a) 10% of the present value of the obligation before deducting plan assets; and
- (b) 10% of the fair value of any plan assets.

These limits, and the recognised and unrecognised actuarial gains and losses, are as follows:

	<i>20X1</i>	<i>20X2</i>	<i>20X3</i>
Net cumulative unrecognised actuarial gains (losses) at 1 January	140	107	170
Limits of ‘corridor’ at 1 January	100	114	120
Excess [A]	<u>40</u>	<u>-</u>	<u>50</u>
Average expected remaining working lives (years) [B]	10	10	10
Actuarial gain (loss) to be recognised [A/B]	4	-	5
Unrecognised actuarial gains (losses) at 1 January	140	107	170
Actuarial gain (loss) for year—obligation	(61)	87	(42)
Actuarial gain (loss) for year—plan assets	32	(24)	(50)
Subtotal	<u>111</u>	<u>170</u>	<u>78</u>
Actuarial (gain) loss recognised	(4)	-	(5)
Unrecognised actuarial gains (losses) at 31 December	<u>107</u>	<u>170</u>	<u>73</u>

Amounts Recognised in the Balance Sheet and Income Statement, and Related Analyses

The final step is to determine the amounts to be recognised in the balance sheet and income statement, and the related analyses to be disclosed under paragraph 120(c), (e), (f) and (g) of the Standard. These are as follows.

	<i>20X1</i>	<i>20X2</i>	<i>20X3</i>
Present value of the obligation	1,141	1,197	1,295
Fair value of plan assets	(1,092)	(1,109)	(1,093)
	<u>49</u>	<u>88</u>	<u>202</u>
Unrecognised actuarial gains (losses)	107	170	73
Unrecognised past service cost—non-vested benefits	-	(20)	(10)
Liability recognised in balance sheet	<u>156</u>	<u>238</u>	<u>265</u>
Current service cost	130	140	150
Interest cost	100	103	96
Expected return on plan assets	(120)	(121)	(114)
Net actuarial (gain) loss recognised in year	(4)	-	(5)
Past service cost—non-vested benefits	-	10	10
Past service cost—vested benefits	-	50	-
Expense recognised in the income statement	<u>106</u>	<u>182</u>	<u>137</u>
Movements in the net liability recognised in the balance sheet, to be disclosed under paragraph 120(e):			
Opening net liability	140	156	238
Expense as above	106	182	137
Contributions paid	(90)	(100)	(110)
Closing net liability	<u>156</u>	<u>238</u>	<u>265</u>
Actual return on plan assets, to be disclosed under paragraph 120(g)			
Expected return on plan assets	120	121	114
Actuarial gain (loss) on plan assets	32	(24)	(50)
Actual return on plan assets	<u>152</u>	<u>97</u>	<u>64</u>

Note: see example illustrating paragraphs 104A-104C for presentation of reimbursements.

Appendix B

Illustrative Disclosures

The appendix accompanies, but is not part of, IAS 19. Extracts from notes show how the required disclosures may be aggregated in the case of a large multi-national group that provides a variety of employee benefits. These extracts do not necessarily conform with all the disclosure and presentation requirements of other Standards. In particular, they do not illustrate the disclosure of:

- (a) *accounting policies for employee benefits (see IAS 1 Presentation of Financial Statements) Under paragraph 120(a) of the Standard, this disclosure shall include the entity's accounting policy for recognising actuarial gains and losses.*
- (b) *employee benefits granted to directors and key management personnel (see IAS 24 Related Party Disclosures).*

Employee Benefit Obligations

The amounts recognised in the balance sheet are as follows:

	Defined benefit pension plans		Post-employment medical benefits	
	20X2	20X1	20X2	20X1
Present value of funded obligations	12,310	11,772	2,819	2,721
Fair value of plan assets	(11,982)	(11,188)	(2,480)	(2,415)
	328	584	339	306
Present value of unfunded obligations	6,459	6,123	5,160	5,094
Unrecognised actuarial gains (losses)	(97)	(17)	31	72
Unrecognised past service cost	(450)	(650)	-	-
Net liability in balance sheet	<u>6,240</u>	<u>6,040</u>	<u>5,530</u>	<u>5,472</u>

Amounts in the balance sheet:

liabilities	6,451	6,278	5,530	5,472
assets	(211)	(238)	-	-
Net liability in balance sheet	<u>6,240</u>	<u>6,040</u>	<u>5,530</u>	<u>5,472</u>

The pension plan assets include ordinary shares issued by [name of reporting entity] with a fair value of 317 (20X1: 281). Plan assets also include property occupied by [name of reporting entity] with a fair value of 200 (20X1: 185).

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The amounts recognised in the income statement are as follows:

	Defined benefit pension plans		Post-employment medical benefits	
	20X2	20X1	20X2	20X1
Current service cost	1,679	1,554	471	411
Interest on obligation	1,890	1,650	819	705
Expected return on plan assets	(1,392)	(1,188)	(291)	(266)
Net actuarial losses (gains) recognised in year	90	(187)	-	-
Past service cost	200	200	-	-
Losses (gains) on curtailments and settlements	221	(47)	-	-
Total, included in 'employee benefits expense'	<u>2,688</u>	<u>1,982</u>	<u>999</u>	<u>850</u>
Actual return on plan assets	<u>1,232</u>	<u>1,205</u>	<u>275</u>	<u>254</u>

Movements in the net liability recognised in the balance sheet are as follows:

	Defined benefit pension plans		Post-employment medical benefits	
	20X2	20X1	20X2	20X1
Net liability at start of year	6,040	5,505	5,472	5,439
Net expense recognised in the income statement	2,688	1,982	999	850
Contributions	(2,261)	(1,988)	(941)	(817)
Exchange differences on foreign plan	(227)	221	-	-
Liabilities acquired in business combinations	-	320	-	-
Net liability at end of year	<u>6,240</u>	<u>6,040</u>	<u>5,530</u>	<u>5,472</u>

Principal actuarial assumptions at the balance sheet date (expressed as weighted averages):

	20X2	20X1
Discount rate at 31 December	10.0%	9.1%
Expected return on plan assets at 31 December	12.0%	10.9%
Future salary increases	5%	4%
Future pension increases	3%	2%
Proportion of employees opting for early retirement	30%	30%
Annual increase in health care costs	8%	8%
Future changes in maximum state healthcare benefits	3%	2%

The group also participates in an industry-wide defined benefit plan which provides pensions linked to final salaries and is funded on a pay-as-you-go basis. It is not practicable to determine the present value of the group's obligation or the related current service cost as the plan computes its obligations on a basis that differs materially from the basis used in [name of reporting entity]'s financial statements. [describe basis] On that basis, the plan's financial statements to 30 June 20X0 show an unfunded liability of 27,525. The unfunded liability will result in future payments by participating employers. The plan has approximately 75,000 members, of whom approximately 5,000 are current or former employees of [name of reporting entity] or their dependants. The expense recognised in the income statement, which is equal to contributions due for the year, and is not included in the above amounts, was 230 (20X1: 215). The group's future contributions may be increased substantially if other entities withdraw from the plan.

Appendix C

The appendix accompanies, but is not part of, IAS 19.

Illustration of the application of paragraph 58A

The issue

Paragraph 58 of the Standard imposes a ceiling on the defined benefit asset that can be recognised.

58. *The amount determined under paragraph 54 may be negative (an asset). An entity shall measure the resulting asset at the lower of:*

- (a) *the amount determined under paragraph 54 [ie the surplus/deficit in the plan plus (minus) any unrecognised losses (gains)]; and*
- (b) *the total of:*
 - (i) *any cumulative unrecognised net actuarial losses and past service cost (see paragraphs 92, 93 and 96); and*
 - (ii) *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 these economic benefits shall be determined using the discount rate specified in paragraph 78.*

Without paragraph 58A (see below), paragraph 58(b)(i) has the following consequence: sometimes deferring the recognition of an actuarial loss (gain) in determining the amount specified by paragraph 54 leads to a gain (loss) being recognised in the income statement.

The following example illustrates the effect of applying paragraph 58 without paragraph 58A. The example assumes that the entity's accounting policy is not to recognise actuarial gains and losses within the 'corridor' and to amortise actuarial gains and losses outside the 'corridor'. (Whether the 'corridor' is used is not significant. The issue can arise whenever there is deferred recognition under paragraph 54.)

Example 1

	A	B	C	D=A+C	E=B+C	F=lower of D and E	G
Year	Surplus in plan	Economic benefits available (paragraph 58(b)(ii))	Losses unrecognised under paragraph 54	Paragraph 54	Paragraph 58(b)	Asset ceiling, ie recognised asset	Gain recognised in year 2
1	100	0	0	100	0	0	-
2	70	0	30	100	30	30	30

At the end of year 1, there is a surplus of 100 in the plan (column A in the table above), but no economic benefits are available to the entity either from refunds or reductions in future contributions* (column B). There are no unrecognised gains and losses under paragraph 54 (column C). So, if there were no asset ceiling, an asset of 100 would be recognised, being the amount specified by paragraph 54 (column D). The asset ceiling in paragraph 58 restricts the asset to nil (column F).

In year 2 there is an actuarial loss in the plan of 30 that reduces the surplus from 100 to 70 (column A) the recognition of which is deferred under paragraph 54 (column C). So, if there were no asset ceiling, an asset of 100 (column D) would be recognised. The asset ceiling without paragraph 58A would be 30 (column E). An asset of 30 would be recognised (column F), giving rise to a gain in income (column G) even though all that has happened is that a surplus from which the entity cannot benefit has decreased.

A similarly counter-intuitive effect could arise with actuarial gains (to the extent that they reduce cumulative unrecognised actuarial losses).

Paragraph 58A

Paragraph 58A prohibits the recognition of gains (losses) that arise solely from past service cost and actuarial losses (gains).

58A. *The application of paragraph 58 shall not result in a gain being recognised solely as a result of an actuarial loss or past service cost in the current period or in a loss being recognised solely as a result of an actuarial gain in the current period. The entity shall therefore recognise immediately under paragraph 54 the following, to the extent that they arise while the defined benefit asset is determined in accordance with paragraph 58(b):*

- (a) *net actuarial losses of the current period and past service cost of the current period to the extent that they exceed any reduction in the present value of the economic benefits specified in paragraph 58(b)(ii). If there is no change or an increase in the present value of the economic benefits, the entire net actuarial losses of the current period and past service cost of the current period shall be recognised immediately under paragraph 54.*
- (b) *net actuarial gains of the current period after the deduction of past service cost of the current period to the extent that they exceed any increase in the present value of the economic benefits specified in paragraph 58(b)(ii). If there is no change or a decrease in the present value of the economic benefits, the entire net actuarial gains of the current period after the deduction of past service cost of the current period shall be recognised immediately under paragraph 54.*

* based on the current terms of the plan.

Examples

The following examples illustrate the result of applying paragraph 58A. As above, it is assumed that the entity's accounting policy is not to recognise actuarial gains and losses within the 'corridor' and to amortise actuarial gains and losses outside the 'corridor'. For the sake of simplicity the periodic amortisation of unrecognised gains and losses outside the corridor is ignored in the examples.

Example 1 continued - adjustment when there are actuarial losses and no change in the economic benefits available

	A	B	C	D=A+C	E=B+C	F=lower of D and E	G
Year	Surplus in plan	Economic benefits available (paragraph 58(b)(ii))	Losses unrecognised under paragraph 54	Paragraph 54	Paragraph 58(b)	Asset ceiling, ie recognised asset	Gain recognised in year 2
1	100	0	0	100	0	0	-
2	70	0	0	70	0	0	0

The facts are as in example 1 above. Applying paragraph 58A, there is no change in the economic benefits available to the entity* so the entire actuarial loss of 30 is recognised immediately under paragraph 54 (column D). The asset ceiling remains at nil (column F) and no gain is recognised.

In effect, the actuarial loss of 30 is recognised immediately, but is offset by the reduction in the effect of the asset ceiling.

	Balance sheet asset under paragraph 54 (column D above)	Effect of the asset ceiling	Asset ceiling (column F above)
Year 1	100	(100)	0
Year 2	70	(70)	0
Gain/(loss)	(30)	30	0

In the above example, there is no change in the present value of the economic benefits available to the entity. The application of paragraph 58A becomes more complex when there are changes in present value of the economic benefits available, as illustrated in the following examples.

* The term 'economic benefits available to the entity' is used to refer to those economic benefits that qualify for recognition under paragraph 58(b)(ii).

Example 2 - adjustment when there are actuarial losses and a decrease in the economic benefits available

	A	B	C	D=A+C	E=B+C	F=lower of D and E	G
Year	Surplus in plan	Economic benefits available (paragraph 58(b)(ii))	Losses unrecognised under paragraph 54	Paragraph 54	Paragraph 58(b)	Asset ceiling, ie recognised asset	Gain recognised in year 2
1	60	30	40	100	70	70	-
2	25	20	50	75	70	70	0

At the end of year 1, there is a surplus of 60 in the plan (column A) and economic benefits available to the entity of 30 (column B). There are unrecognised losses of 40 under paragraph 54* (column C). So, if there were no asset ceiling, an asset of 100 would be recognised (column D). The asset ceiling restricts the asset to 70 (column F).

In year 2, an actuarial loss of 35 in the plan reduces the surplus from 60 to 25 (column A). The economic benefits available to the entity fall by 10 from 30 to 20 (column B). Applying paragraph 58A, the actuarial loss of 35 is analysed as follows:

Actuarial loss equal to the reduction in economic benefits	10
Actuarial loss that exceeds the reduction in economic benefits	25

In accordance with paragraph 58A, 25 of the actuarial loss is recognised immediately under paragraph 54 (column D). The reduction in economic benefits of 10 is included in the cumulative unrecognised losses that increase to 50 (column C). The asset ceiling, therefore, also remains at 70 (column E) and no gain is recognised.

In effect, an actuarial loss of 25 is recognised immediately, but is offset by the reduction in the effect of the asset ceiling.

* The application of paragraph 58A allows the recognition of some actuarial gains and losses to be deferred under paragraph 54 and, hence, to be included in the calculation of the asset ceiling. For example, cumulative unrecognised actuarial losses that have built up while the amount specified by paragraph 58(b) is not lower than the amount specified by paragraph 54 will not be recognised immediately at the point that the amount specified by paragraph 58(b) becomes lower. Instead their recognition will continue to be deferred in line with the entity's accounting policy. The cumulative unrecognised losses in this example are losses the recognition of which is deferred even though paragraph 58A applies.

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	Balance sheet asset under paragraph 54 (column D above)	Effect of the asset ceiling	Asset ceiling (column F above)
Year 1	100	(30)	70
Year 2	75	(5)	70
Gain/(loss)	(25)	25	0

Example 3 - adjustment when there are actuarial gains and a decrease in the economic benefits available to the entity

	A	B	C	D=A+C	E=B+C	F=lower of D and E	G
Year	Surplus in plan	Economic benefits available (paragraph 58(b)(ii))	Losses unrecognised under paragraph 54	Paragraph 54	Paragraph 58(b)	Asset ceiling, ie recognised asset	Loss recognised in year 2
1	60	30	40	100	70	70	-
2	110	25	40	150	65	65	-5

At the end of year 1 there is a surplus of 60 in the plan (column A) and economic benefits available to the entity of 30 (column B). There are unrecognised losses of 40 under paragraph 54 that arose before the asset ceiling had any effect (column C). So, if there were no asset ceiling, an asset of 100 would be recognised (column D). The asset ceiling restricts the asset to 70 (column F).

In year 2, an actuarial gain of 50 in the plan increases the surplus from 60 to 110 (column A). The economic benefits available to the entity decrease by 5 (column B). Applying paragraph 58A, there is no increase in economic benefits available to the entity. Therefore, the entire actuarial gain of 50 is recognised immediately under paragraph 54 (column D) and the cumulative unrecognised loss under paragraph 54 remains at 40 (column C). The asset ceiling decreases to 65 because of the reduction in economic benefits. That reduction is not an actuarial loss as defined by IAS 19 and therefore does not qualify for deferred recognition.

In effect, an actuarial gain of 50 is recognised immediately, but is (more than) offset by the increase in the effect of the asset ceiling.

	Balance sheet asset under paragraph 54 (column D above)	Effect of the asset ceiling	Asset ceiling (column F above)
Year 1	100	(30)	70
Year 2	150	(85)	65
Gain/(loss)	50	(55)	(5)

In both examples 2 and 3 there is a reduction in economic benefits available to the entity. However, in example 2 no loss is recognised whereas in example 3 a loss is recognised. This difference in treatment is consistent with the treatment of changes in the present value of economic benefits before paragraph 58A was introduced. The purpose of paragraph 58A is solely to prevent gains (losses) being recognised because of past service cost or actuarial losses (gains). As far as is possible, all other consequences of deferred recognition and the asset ceiling are left unchanged.

Example 4 - adjustment in a period in which the asset ceiling ceases to have an effect

	A	B	C	D=A+C	E=B+C	F=lower of D and E	G
Year	Surplus in plan	Economic benefits available (paragraph 58(b)(ii))	Losses unrecognised under paragraph 54	Paragraph 54	Paragraph 58(b)	Asset ceiling, ie recognised asset	Gain recognised in year 2
1	60	25	40	100	65	65	-
2	(50)	0	115	65	115	65	0

At the end of year 1 there is a surplus of 60 in the plan (column A) and economic benefits are available to the entity of 25 (column B). There are unrecognised losses of 40 under paragraph 54 that arose before the asset ceiling had any effect (column C). So, if there were no asset ceiling, an asset of 100 would be recognised (column D). The asset ceiling restricts the asset to 65 (column F).

In year 2, an actuarial loss of 110 in the plan reduces the surplus from 60 to a deficit of 50 (column A). The economic benefits available to the entity decrease from 25 to 0 (column B). To apply paragraph 58A it is necessary to determine how much of the actuarial loss arises while the defined benefit asset is determined in accordance with paragraph 58(b). Once the surplus becomes a deficit, the amount determined by paragraph 54 is lower than the net total under paragraph 58(b). So, the actuarial loss that arises while the defined benefit asset is determined in accordance with paragraph 58(b) is the loss that reduces the surplus to nil, ie 60. The actuarial loss is, therefore, analysed as follows:

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Actuarial loss that arises while the defined benefit asset is measured under paragraph 58(b):	
Actuarial loss that equals the reduction in economic benefits	25
Actuarial loss that exceeds the reduction in economic benefits	<u>35</u>
	60
Actuarial loss that arises while the defined benefit asset is measured under paragraph 54	<u>50</u>
Total actuarial loss	110

In accordance with paragraph 58A, 35 of the actuarial loss is recognised immediately under paragraph 54 (column D); 75 (25+50) of the actuarial loss is included in the cumulative unrecognised losses which increase to 115 (column C). The amount determined under paragraph 54 becomes 65 (column D) and under paragraph 58(b) becomes 115 (column E). The recognised asset is the lower of the two, ie 65 (column F), and no gain or loss is recognised (column G).

In effect, an actuarial loss of 35 is recognised immediately, but is offset by the reduction in the effect of the asset ceiling.

	Balance sheet asset under paragraph 54 (column D above)	Effect of the asset ceiling	Asset ceiling (column F above)
Year 1	100	(35)	65
Year 2	65	0	65
Gain/(loss)	(35)	35	0

Notes

1. In applying paragraph 58A in situations when there is an increase in the present value of the economic benefits available to the entity, it is important to remember that the present value of the economic benefits available cannot exceed the surplus in the plan.*
2. In practice, benefit improvements often result in a past service cost and an increase in expected future contributions due to increased current service costs of future years. The increase in expected future contributions may increase the economic benefits available to the entity in the form of anticipated reductions in those future contributions. The prohibition against recognising a gain solely as a result of past service cost in the current period does not prevent the recognition of a gain because

* The example following paragraph 60 of IAS 19 is corrected so that the present value of available future refunds and reductions in contributions equals the surplus in the plan of 90 (rather than 100), with a further correction to make the limit 270 (rather than 280).

of an increase in economic benefits. Similarly, a change in actuarial assumptions that causes an actuarial loss may also increase expected future contributions and, hence, the economic benefits available to the entity in the form of anticipated reductions in future contributions. Again, the prohibition against recognising a gain solely as a result of an actuarial loss in the current period does not prevent the recognition of a gain because of an increase in economic benefits.

Appendix D

Approval of 2002 amendment by the Board

The 2002 amendment to IAS 19 was approved for issue by an affirmative vote of thirteen members of the International Accounting Standards Board. Ms O'Malley dissented. Her dissenting opinion is set out in the following Appendix.

Sir David Tweedie	Chairman
Thomas E Jones	Vice-Chairman
Mary E Barth	
Hans-Georg Bruns	
Anthony T Cope	
Robert P Garnett	
Gilbert Gélard	
James J Leisenring	
Warren J McGregor	
Patricia L O'Malley	
Harry K Schmid	
John T Smith	
Geoffrey Whittington	
Tatsumi Yamada	

Appendix E

Dissenting opinion (2002 amendment)

Ms O'Malley dissents from this amendment of IAS 19. In her view, the perceived problem being addressed is an inevitable result of the interaction of two fundamentally inconsistent notions in IAS 19. The corridor approach allowed by IAS 19 permits the recognition of amounts on the balance sheet that do not meet the Framework's definition of assets. The asset ceiling then imposes a limitation on the recognition of some of those assets based on a recoverability notion. A far preferable limited amendment would be to delete the asset ceiling in paragraph 58. This would resolve the identified problem and at least remove the internal inconsistency in IAS 19.

It is asserted that the amendment to the standard will result in a more representationally faithful portrayal of economic events. Ms O'Malley believes that it is impossible to improve the representational faithfulness of a standard that permits recording an asset relating to a pension plan that actually has a deficiency, or a liability in respect of a plan that actually has a surplus.

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Basis for Conclusions

[The original text has been marked up to reflect the revision of IAS 39 (as revised in 2003) and subsequently IFRS 2; new text is underlined and deleted text is struck through.]

This appendix gives the Board's reasons for rejecting certain alternative solutions. Individual Board members gave greater weight to some factors than to others.

Background

1. The IASC Board (the 'Board') approved IAS 19 *Accounting for Retirement Benefits in the Financial Statements of Employers*, in 1983. Following a limited review, the Board approved a revised Standard IAS 19 *Retirement Benefit Costs* ('the old IAS 19'), in 1993. The Board began a more comprehensive review of IAS 19 in November 1994. In August 1995, the IASC Staff published an Issues Paper on *Retirement Benefit and Other Employee Benefit Costs*. In October 1996, the Board approved E54 *Employee Benefits*, with a comment deadline of 31 January 1997. The Board received more than 130 comment letters on E54 from over 20 countries. The Board approved IAS 19 *Employee Benefits* ('the new IAS 19') in January 1998.
2. The Board believes that the new IAS 19 is a significant improvement over the old IAS 19. Nevertheless, the Board believes that further improvement may be possible in due course. In particular, several Board members believe that it would be preferable to recognise all actuarial gains and losses immediately in a statement of financial performance. However, the Board believes that such a solution is not feasible for actuarial gains and losses until the Board makes further progress on various issues relating to the reporting of financial performance. When the Board makes further progress with those issues, it may decide to revisit the treatment of actuarial gains and losses.

Summary of Changes to IAS 19

3. The most significant feature of the new IAS 19 is a market based approach to measurement. The main consequences are that the discount rate is based on market yields at the balance sheet date and any plan assets are measured at fair value. In summary, the main changes from the old IAS 19 are the following:
 - (a) there is a revised definition of defined contribution plans and related guidance (see paragraphs 5 and 6 below), including more detailed guidance than the old IAS 19 on multi-employer plans and state plans (see paragraphs 7-10 below) and on insured plans;
 - (b) there is improved guidance on the balance sheet treatment of liabilities and assets arising from defined benefit plans (see paragraphs 11-14 below).

- (c) defined benefit obligations should be measured with sufficient regularity that the amounts recognised in the financial statements do not differ materially from the amounts that would be determined at the balance sheet date (see paragraphs 15 and 16 below);
- (d) projected benefit methods are eliminated and there is a requirement to use the accrued benefit method known as the Projected Unit Credit Method (see paragraphs 17-22 below). The use of an accrued benefit method makes it essential to give detailed guidance on the attribution of benefit to individual periods of service (see paragraphs 23-25 below);
- (e) the rate used to discount post-employment benefit obligations and other long-term employee benefit obligations (both funded and unfunded) should be determined by reference to market yields at the balance sheet date on high quality corporate bonds. In countries where there is no deep market in such bonds, the market yields (at the balance sheet date) on government bonds should be used. The currency and term of the corporate bonds or government bonds should be consistent with the currency and estimated term of the post-employment benefit obligations (see paragraphs 26-34 below);
- (f) defined benefit obligations should consider all benefit increases that are set out in the terms of the plan (or result from any constructive obligation that goes beyond those terms) at the balance sheet date (see paragraphs 35-37 below);
- (g) an entity should recognise, as a minimum, a specified portion of those actuarial gains and losses (arising from both defined benefit obligations and any related plan assets) that fall outside a 'corridor'. An entity is permitted, but not required, to adopt certain systematic methods of faster recognition. Such methods include, among others, immediate recognition of all actuarial gains and losses (see paragraphs 38-48 below);
- (h) an entity should recognise past service cost on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits are already vested immediately, an entity should recognise past service cost immediately (see paragraphs 49-62 below);
- (i) plan assets should be measured at fair value. Fair value is estimated by discounting expected future cash flows only if no market price is available (see paragraphs 66-75 below);
- (j) amounts recognised by the reporting entity as an asset should not exceed the net total of:
 - (i) any unrecognised actuarial losses and past service cost; and
 - (ii) the present value of any economic benefits available in the form of refunds from the plan or reductions in contributions to the plan (see paragraphs 76-78 below);
- (k) curtailment and settlement losses should be recognised not when it is probable that the settlement or curtailment will occur, but when the settlement or curtailment occurs (see paragraphs 79 and 80 below);

- (l) improvements have been made to the disclosure requirements (see paragraphs 81-85 below);
- (m) the new IAS 19 deals with all employee benefits, whereas IAS 19 deals only with retirement benefits and certain similar post-employment benefits (see paragraphs 86-94 below); and
- (n) the transitional provisions for defined benefit plans are amended (see paragraphs 95 and 96 below).

The Board rejected a proposal to require recognition of an 'additional minimum liability' in certain cases (see paragraphs 63-65 below).

Summary of Changes to E54

4. The new IAS 19 makes the following principal changes to the proposals in E54:
 - (a) an entity should attribute benefit to periods of service following the plan's benefit formula, but the straight-line basis should be used if employee service in later years leads to a materially higher level of benefit than in earlier years (see paragraphs 23-25 below);
 - (b) actuarial assumptions should include estimates of benefit increases not if there is reliable evidence that they will occur, but only if the increases are set out in the terms of the plan (or result from any constructive obligation that goes beyond those terms) at the balance sheet date (see paragraphs 35-37 below);
 - (c) actuarial gains and losses that fall outside the 10% 'corridor' need not be recognised immediately as proposed in E54. The minimum amount that an entity should recognise for each defined benefit plan is the part that fell outside the 'corridor' as at the end of the previous reporting period, divided by the expected average remaining working lives of the employees participating in that plan. The new IAS 19 also permits certain systematic methods of faster recognition. Such methods include, among others, immediate recognition of all actuarial gains and losses (see paragraphs 38-48 below);
 - (d) E54 set out two alternative treatments for past service cost and indicated that the Board would eliminate one of these treatments after considering comments on the Exposure Draft. One treatment was immediate recognition of all past service cost. The other treatment was immediate recognition for former employees, with amortisation for current employees over the remaining working lives of the current employees. The new IAS 19 requires that an entity should recognise past service cost on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits are already vested immediately an entity should recognise past service cost immediately (see paragraphs 49-59 below);
 - (e) the effect of 'negative plan amendments' should not be recognised immediately (as proposed in E54) but treated in the same way as past service cost (see paragraphs 60-62 below);

- (f) non-transferable securities issued by the reporting entity have been excluded from the definition of plan assets (see paragraphs 67 and 68 below);
- (g) plan assets should be measured at fair value rather than market value, as defined in E54 (see paragraphs 69 and 70 below);
- (h) plan administration costs (not just investment administration costs, as proposed in E54), are to be deducted in determining the return on plan assets (see paragraph 75 below);
- (i) the limit on the recognition of plan assets has been changed in two respects from the proposals in E54. The limit does not over-ride the corridor for actuarial losses or the deferred recognition of past service cost. Also, the limit refers to **available** refunds or reductions in future contributions. E54 referred to the **expected** refunds or reductions in future contributions (see paragraphs 76-78 below);
- (j) unlike E54, the new IAS 19 does not specify whether an income statement should present interest cost and the expected return on plan assets in the same line item as current service cost. The new IAS 19 requires an entity to disclose the line items in which they are included;
- (k) improvements have been made to the disclosure requirements (see paragraphs 81-85 below);
- (l) the guidance in certain areas (particularly termination benefits, curtailments and settlements, profit-sharing and bonus plans and various references to constructive obligations) has been conformed to the proposals in E59 *Provisions, Contingent Liabilities and Contingent Assets*. Also, the Board has added explicit guidance on the measurement of termination benefits, requiring discounting for termination benefits not payable within one year (see paragraphs 91-93 below); and
- (m) on initial adoption of the new IAS 19, there is a transitional option to recognise an increase in defined benefit liabilities over not more than five years. The new IAS 19 is operative for financial statements covering periods beginning on or after 1 January 1999, rather than 2001 as proposed in E54 (see paragraphs 95 and 96 below).

Defined Contribution Plans (paragraphs 24-47 of the Standard)

5. The old IAS 19 defined:
- (a) **defined contribution plans** as retirement benefit plans under which amounts to be paid as retirement benefits are determined by reference to contributions to a fund together with investment earnings thereon; and
 - (b) **defined benefit plans** as retirement benefit plans under which amounts to be paid as retirement benefits are determined by reference to a formula usually based on employees' remuneration and/or years of service.

The Board considers these definitions unsatisfactory because they focus on the benefit receivable by the employee, rather than on the cost to the entity. The definitions in paragraph 7 of the new IAS 19 focus on the downside risk that the cost to the entity may increase. The definition of defined contribution plans does not exclude the upside potential that the cost to the entity may be less than expected.

6. The new IAS 19 does not change the accounting for defined contribution plans, which is straightforward because there is no need for actuarial assumptions and an entity has no possibility of any actuarial gain or loss. The new IAS 19 gives no guidance equivalent to paragraphs 20 (past service costs in defined contribution plans) and 21 (curtailment of defined contribution plans) of the old IAS 19. The Board believes that these issues are not relevant to defined contribution plans.

Multi-employer Plans and State Plans (paragraphs 29-38 of the Standard)

7. An entity may not always be able to obtain sufficient information from multi-employer plans to use defined benefit accounting. The Board considered three approaches to this problem:
 - (a) use defined contribution accounting for some and defined benefit accounting for others;
 - (b) use defined contribution accounting for all multi-employer plans, with additional disclosure where the multi-employer plan is a defined benefit plan; or
 - (c) use defined benefit accounting for those multi-employer plans that are defined benefit plans. However, where sufficient information is not available to use defined benefit accounting, an entity should disclose that fact and use defined contribution accounting.
8. The Board believes that there is no conceptually sound, workable and objective way to draw a distinction so that an entity could use defined contribution accounting for some multi-employer defined benefit plans and defined benefit accounting for others. Also, the Board believes that it is misleading to use defined contribution accounting for multi-employer plans that are defined benefit plans. This is illustrated by the case of French banks that used defined contribution accounting for defined benefit pension plans operated under industry-wide collective agreements on a pay-as-you-go basis. Demographic trends made these plans unsustainable and a major reform in 1993 replaced these by defined contribution arrangements for future service. At this point, the banks were compelled to quantify their obligations. Those obligations had previously existed, but had not been recognised as liabilities.

9. The Board concluded that an entity should use defined benefit accounting for those multi-employer plans that are defined benefit plans. However, where sufficient information is not available to use defined benefit accounting, an entity should disclose that fact and use defined contribution accounting. The Board agreed to apply the same principle to state plans. The new IAS 19 notes that most state plans are defined contribution plans.
10. In response to comments on E54, the Board considered a proposal to exempt wholly owned subsidiaries (and their parents) participating in group defined benefit plans from the recognition and measurement requirements in their individual non-consolidated financial statements, on cost-benefit grounds. The Board concluded that such an exemption would not be appropriate.

Defined Benefit Plans

Recognition and Measurement: Balance Sheet (paragraphs 49-60 of the Standard)

11. Paragraph 54 of the new IAS 19 summarises the recognition and measurement of liabilities arising from defined benefit plans and paragraphs 55-107 of the new IAS 19 describe various aspects of recognition and measurement in greater detail. Although the old IAS 19 did not deal explicitly with the recognition of retirement benefit obligations as a liability, it is likely that most entities would recognise a liability for retirement benefit obligations at the same time under both Standards. However, the two Standards differ in the measurement of the resulting liability.
12. Paragraph 54 of the new IAS 19 is based on the definition of, and recognition criteria for, a liability in IASC's *Framework for the Preparation and Presentation of Financial Statements* (the 'Framework'). The *Framework* defines a liability as *a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits*. The *Framework* states that an item which meets the definition of a liability should be recognised if:
 - (a) it is probable that any future economic benefit associated with the item will flow from the entity; and
 - (b) the item has a cost or value that can be measured with reliability.
13. The Board believes that:
 - (a) an entity has an obligation under a defined benefit plan when an employee has rendered service in return for the benefits promised under the plan. Paragraphs 67-71 of the new IAS 19 deal with the attribution of benefit to individual periods of service in order to determine whether an obligation exists;
 - (b) an entity should use actuarial assumptions to determine whether the entity will pay those benefits in future reporting periods (see paragraphs 72-91 of the Standard); and

- (c) actuarial techniques allow an entity to measure the obligation with sufficient reliability to justify recognition of a liability.
14. The Board believes that an obligation exists even if a benefit is not vested, in other words if the employee's right to receive the benefit is conditional on future employment. For example, consider an entity that provides a benefit of 100 to employees who remain in service for two years. At the end of the first year, the employee and the entity are not in the same position as at the beginning of the first year, because the employee will only need to work for one year, instead of two, before becoming entitled to the benefit. Although there is a possibility that the benefit may not vest, that difference is an obligation and, in the Board's view, should result in the recognition of a liability at the end of the first year. The measurement of that obligation at its present value reflects the entity's best estimate of the probability that the benefit may not vest.

Measurement Date (paragraphs 56 and 57 of the Standard)

15. Some national standards permit entities to measure the present value of defined benefit obligations at a date up to three months before the balance sheet date. However, the Board decided that entities should measure the present value of defined benefit obligations, and the fair value of any plan assets, at the balance sheet date. Therefore, if an entity carries out a detailed valuation of the obligation at an earlier date, the results of that valuation should be updated to take account of any significant transactions and other significant changes in circumstances up to the balance sheet date.
16. In response to comments on E54, the Board has clarified that full actuarial valuation is not required at the balance sheet date, provided that an entity determines the present value of defined benefit obligations and the fair value of any plan assets with sufficient regularity that the amounts recognised in the financial statements do not differ materially from the amounts that would be determined at the balance sheet date.

Actuarial Valuation Method (paragraphs 64-66 of the Standard)

17. The old IAS 19 permitted both accrued benefit valuation methods (benchmark treatment) and projected benefit valuation methods (allowed alternative treatment). The two groups of methods are based on fundamentally different, and incompatible, views of the objectives of accounting for employee benefits:
- (a) **accrued benefit methods** (sometimes known as 'benefit', 'unit credit' or 'single premium' methods) determine the present value of employee benefits attributable to service to date; but
 - (b) **projected benefit methods** (sometimes described as 'cost', 'level contribution' or 'level premium' methods) project the estimated total obligation at retirement and then calculate a level funding cost, taking into account investment earnings, that will provide the total benefit at retirement.

The differences between the two groups of methods were discussed in more detail in the Issues Paper published in August 1995.

18. The two methods may have similar effects on the income statement, but only by chance or if the number and age distribution of participating employees remains relatively stable over time. There can be significant differences in the measurement of liabilities under the two groups of methods. For these reasons, the Board believes that a requirement to use a single group of methods will significantly enhance comparability.
19. The Board considered whether it should continue to permit projected benefit methods as an allowed alternative treatment while introducing a new requirement to disclose information equivalent to the use of an accrued benefit method. However, the Board believes that disclosure cannot rectify inappropriate accounting in the balance sheet and income statement. The Board concluded that projected benefit methods are not appropriate, and should be eliminated, because such methods:
 - (a) focus on future events (future service) as well as past events, whereas accrued benefit methods focus only on past events;
 - (b) generate a liability which does not represent a measure of any real amount and can be described only as the result of cost allocations; and
 - (c) do not attempt to measure fair value and cannot, therefore, be used in a business combination, as required by IAS 22 *Business Combinations*¹. If an entity uses an accrued benefit method in a business combination, it would not be feasible for the entity to use a projected benefit method to account for the same obligation in subsequent periods.
20. The old IAS 19 did not specify which forms of accrued benefit valuation method should be permitted under the benchmark treatment. The new IAS 19 requires a single accrued benefit method: the most widely used accrued benefit method, which is known as the Projected Unit Credit Method (sometimes known as the 'accrued benefit method pro-rated on service' or as the 'benefit/years of service method').
21. The Board acknowledges that the elimination of projected benefit methods, and of accrued benefit methods other than the Projected Unit Credit Method, has cost implications. However, with modern computing power, it will be only marginally more expensive to run a valuation on two different bases and the advantages of improved comparability will outweigh the additional cost.
22. An actuary may sometimes, for example, in the case of a closed fund, recommend a method other than the Projected Unit Credit Method for funding purposes. Nevertheless, the Board agreed to require the use of the Projected Unit Credit Method in all cases because that method is more consistent with the accounting objectives laid down in the new IAS 19.

¹ IAS 22 was withdrawn in 2004 and replaced with IFRS 3 *Business Combinations*.

Attributing Benefit to Periods of Service (paragraphs 67-71 of the Standard)

23. As explained in paragraph 13 above, the Board believes that an entity has an obligation under a defined benefit plan when an employee has rendered service in return for the benefits promised under the plan. The Board considered three alternative methods of accounting for a defined benefit plan which attributes different amounts of benefit to different periods:

- (a) apportion the entire benefit on a straight-line basis over the entire period to 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;
- (b) apportion benefit under the plan's benefit formula. However, a straight-line basis should be used if the plan's benefit formula attributes a materially higher benefit to later years; or
- (c) apportion the benefit that vests at each interim date on a straight-line basis over the period between that date and the previous interim vesting date.

The three methods are illustrated by the following two examples.

Example 1

A plan provides a benefit of 400 if an employee retires after more than ten and less than twenty years of service and a further benefit of 100 (500 in total) if an employee retires after twenty or more years of service.

The amounts attributed to each year are as follows:

	<i>Years 1-10</i>	<i>Years 11-20</i>
<i>Method (a)</i>	25	25
<i>Method (b)</i>	40	10
<i>Method (c)</i>	40	10

Example 2

A plan provides a benefit of 100 if an employee retires after more than ten and less than twenty years of service and a further benefit of 400 (500 in total) if an employee retires after twenty or more years of service.

The amounts attributed to each year are as follows:

	<i>Years 1-10</i>	<i>Years 11-20</i>
<i>Method (a)</i>	25	25
<i>Method (b)</i>	25	25
<i>Method (c)</i>	10	40

Note: this plan attributes a higher benefit to later years, whereas the plan in Example 1 attributes a higher benefit to earlier years.

24. In approving E54, the Board adopted method (a) on the grounds that this method was the most straightforward and that there were no compelling reasons to attribute different amounts of benefit to different years, as would occur under either of the other methods.
25. A significant minority of commentators on E54 favoured following the benefit formula (or alternatively, if the final Standard were to retain straight-line attribution, the recognition of a minimum liability based on the benefit formula). The Board agreed with these comments and decided to require method (b).

Actuarial Assumptions: Discount Rate (paragraphs 78-82 of the Standard)

26. One of the most important issues in measuring defined benefit obligations is the selection of the criteria used to determine the discount rate. According to the old IAS 19, the discount rate assumed in determining the actuarial present value of promised retirement benefits reflected the long-term rates, or an approximation thereto, at which such obligations are expected to be settled. The Board rejected the use of such a rate because it is not relevant for an entity that does not contemplate settlement and it is an artificial construct, as there may be no market for settlement of such obligations.
27. Some believe that, for funded benefits, the discount rate should be the expected rate of return on the plan assets actually held by a plan, on the grounds that the return on plan assets represents faithfully the expected ultimate cash outflow (i.e. future contributions). The Board rejected this approach because the fact that a fund has chosen to invest in certain kinds of asset does not affect the nature or amount of the obligation. In particular, assets with a higher expected return carry more risk and an entity should not recognise a smaller liability merely because the plan has chosen to invest in riskier assets with a higher expected return. Therefore, the measurement of the obligation should be independent of the measurement of any plan assets actually held by a plan.
28. The most significant decision is whether the discount rate should be a risk-adjusted rate (one that attempts to capture the risks associated with the obligation). Some argue that the most appropriate risk-adjusted rate is given by the expected return on an appropriate portfolio of plan assets that would, over the long term, provide an effective hedge against such an obligation. An appropriate portfolio might include:
 - (a) fixed-interest securities for obligations to former employees to the extent that the obligations are not linked, in form or in substance, to inflation;
 - (b) index-linked securities for index-linked obligations to former employees; and
 - (c) equity securities for benefit obligations towards current employees that are linked to final pay. This is based on the view that the long-term performance of equity securities is correlated with general salary progression in the economy as a whole and hence with the final-pay element of a benefit obligation.

It is important to note that the portfolio actually held need not necessarily be an appropriate portfolio in this sense. Indeed, in some countries, regulatory constraints may prevent plans from holding an appropriate portfolio. For example, in some countries, plans are required to hold a certain proportion of their assets in the form of fixed-interest securities. Furthermore, if an appropriate portfolio is a valid reference point, it is equally valid for both funded and unfunded plans.

29. Those who support using the interest rate on an appropriate portfolio as a risk-adjusted discount rate argue that:
- (a) portfolio theory suggests that the expected return on an asset (or the interest rate inherent in a liability) is related to the undiversifiable risk associated with that asset (or liability). Undiversifiable risk reflects not the variability of the returns (payments) in **absolute** terms but the **correlation** of the returns (or payments) with the returns on other assets. If cash inflows from a portfolio of assets react to changing economic conditions over the long term in the same way as the cash outflows of a defined benefit obligation, the undiversifiable risk of the obligation (and hence the appropriate discount rate) must be the same as that of the portfolio of assets;
 - (b) an important aspect of the economic reality underlying final salary plans is the correlation between final salary and equity returns that arises because they both reflect the same long-term economic forces. Although the correlation is not perfect, it is sufficiently strong that ignoring it will lead to systematic over-statement of the liability. Also, ignoring this correlation will result in misleading volatility due to short-term fluctuations between the rate used to discount the obligation and the discount rate that is implicit in the fair value of the plan assets. These factors will deter entities from operating defined benefit plans and lead to switches from equities to fixed interest investments. Where defined benefit plans are largely funded by equities, this could have a serious impact on share prices. This switch will also increase the cost of pensions. There will be pressure on companies to remove the apparent (but non-existent) shortfall;
 - (c) if an entity settled its obligation by purchasing an annuity, the insurance company would determine the annuity rates by looking to a portfolio of assets that provides cash inflows that substantially offset all the cash flows from the benefit obligation as those cash flows fall due. Therefore, the expected return on an appropriate portfolio measures the obligation at an amount that is close to its market value. In practice, it is not possible to settle a final pay obligation by buying annuities since no insurance company would insure a final pay decision that remained at the discretion of the person insured. However, evidence can be derived from the purchase/sale of businesses that include a final salary pension scheme. In this situation the vendor and purchaser would negotiate a price for the pension obligation by reference to its present value, discounted at the rate of return on an appropriate portfolio;

- (d) although investment risk is present even in a well-diversified portfolio of equity securities, any general decline in securities would, in the long term, be reflected in declining salaries. Since employees accepted that risk by agreeing to a final salary plan, the exclusion of that risk from the measurement of the obligation would introduce a systematic bias into the measurement; and
 - (e) time-honoured funding practices in some countries use the expected return on an appropriate portfolio as the discount rate. Although funding considerations are distinct from accounting issues, the long history of this approach calls for careful scrutiny of any other proposed approach.
30. Those who oppose a risk-adjusted rate argue that:
- (a) it is incorrect to look at returns on assets in determining the discount rate for liabilities;
 - (b) if a sufficiently strong correlation between asset returns and final pay actually existed, a market for final salary obligations would develop, yet this has not happened. Furthermore, where any such apparent correlation does exist, it is not clear whether the correlation results from shared characteristics of the portfolio and the obligations or from changes in the contractual pension promise;
 - (c) the return on equity securities does not correlate with other risks associated with defined benefit plans, such as variability in mortality, timing of retirement, disability and adverse selection;
 - (d) in order to evaluate a liability with uncertain cash flows, an entity would normally use a discount rate lower than the risk-free rate, yet the expected return on an appropriate portfolio is higher than the risk-free rate;
 - (e) the assertion that final salary is strongly correlated with asset returns implies that final salary will tend to decrease if asset prices fall, yet experience shows that salaries tend not to decline;
 - (f) the notion that equities are not risky in the long term, and the associated notion of long-term value, are based on the fallacious view that the market always bounces back after a crash. Shareholders do not get credit in the market for any additional long-term value if they sell their shares today. Even if some correlation exists over long periods, benefits must be paid as they become due. An entity that funds its obligations with equity securities runs the risk that equity prices may be down when benefits must be paid. Also, the hypothesis that the real return on equities is uncorrelated with inflation does not mean that equities offer a risk-free return, even in the long term; and
 - (g) the expected long-term rate of return on an appropriate portfolio cannot be determined sufficiently objectively in practice to provide an adequate basis for an accounting standard. The practical difficulties include specifying the characteristics of the appropriate portfolio, selecting the time horizon for estimating returns on the portfolio and estimating those returns.

31. The Board has not identified clear evidence that the expected return on an appropriate portfolio of assets provides a relevant and reliable indication of the risks associated with a defined benefit obligation, or that such a rate can be determined with reasonable objectivity. Therefore, the Board decided that the discount rate should reflect the time value of money but should not attempt to capture those risks. Furthermore, the discount rate should not reflect the entity's own credit rating, as otherwise an entity with a lower credit rating would recognise a smaller liability. The rate that best achieves these objectives is the yield on high quality corporate bonds. In countries where there is no deep market in such bonds, the yield on government bonds should be used.
32. Another issue is whether the discount rate should be the long-term average rate, based on past experience over a number of years, or the current market yield at the balance sheet date for an obligation of the appropriate term. Those who support a long-term average rate argue that:
- (a) a long-term approach is consistent with the transaction-based historical cost approach that is either required or permitted in other International Accounting Standards;
 - (b) point in time estimates pursue a level of precision that is not attainable in practice and lead to volatility in reported profit that may not be a faithful representation of changes in the obligation but may simply reflect an unavoidable inability to predict accurately the future events that are anticipated in making period-to-period measures;
 - (c) for an obligation based on final salary, neither market annuity prices nor simulation by discounting expected future cash flows can determine an unambiguous annuity price; and
 - (d) over the long term, a suitable portfolio of plan assets may provide a reasonably effective hedge against an employee benefit obligation that increases in line with salary growth. However, there is much less assurance that, at a given measurement date, market interest rates will match the salary growth built into the obligation.
33. The Board decided that the discount rate should be determined by reference to market yields at the balance sheet date as:
- (a) there is no rational basis for expecting efficient market prices to drift towards any assumed long-term average, because prices in a market of sufficient liquidity and depth incorporate all publicly available information and are more relevant and reliable than an estimate of long-term trends by any individual market participant;
 - (b) the cost of benefits attributed to service during the current period should reflect prices of that period;
 - (c) if expected future benefits are defined in terms of projected future salaries that reflect current estimates of future inflation rates, the discount rate should be based on current market interest rates (in nominal terms), as these also reflect current market expectations of inflation rates; and

- (d) if plan assets are measured at a current value (i.e. fair value), the related obligation should be discounted at a current discount rate in order to avoid introducing irrelevant volatility through a difference in the measurement basis.
34. The reference to market yields at the balance sheet date does not mean that short-term discount rates should be used to discount long-term obligations. The new IAS 19 requires that the discount rate should reflect market yields (at the balance sheet date) on bonds with an expected term consistent with the expected term of the obligations.

Actuarial Assumptions: Salaries, Benefits and Medical Costs (paragraphs 83-91 of the Standard)

35. Some argue that estimates of future increases in salaries, benefits and medical costs should not affect the measurement of assets and liabilities until they are granted, on the grounds that:
- (a) future increases are future events; and
 - (b) such estimates are too subjective.
36. The Board believes that the assumptions are used not to determine whether an obligation exists, but to measure an existing obligation on a basis which provides the most relevant measure of the estimated outflow of resources. If no increase is assumed, this is an implicit assumption that no change will occur and it would be misleading to assume no change if an entity expects a change. The new IAS 19 maintains the existing requirement that measurement should take account of estimated future salary increases. The Board also believes that increases in future medical costs can be estimated with sufficient reliability to justify incorporation of those estimated increases in the measurement of the obligation.
37. E54 proposed that measurement should also assume future benefit increases if there is reliable evidence that those benefit increases will occur. In response to comments, the Board concluded that future benefit increases do not give rise to a present obligation and that there would be no reliable or objective way of deciding which future benefit increases were reliable enough to be incorporated in actuarial assumptions. Therefore, the new IAS 19 requires that future benefit increases should be assumed only if they are set out in the terms of the plan (or result from any constructive obligation that goes beyond the formal terms) at the balance sheet date.

Actuarial Gains and Losses (paragraphs 92-95 of the Standard)

38. The Board considered five methods of accounting for actuarial gains and losses:
- (a) deferred recognition in both the balance sheet and the income statement over the average expected remaining working life of the employees concerned (see paragraph 39 below);

- (b) immediate recognition both in the balance sheet and outside the income statement in equity (IAS 1 *Presentation of Financial Statements* sets out requirements for the presentation or disclosure of such movements in equity) (see paragraphs 40 and 41 below);
 - (c) a ‘corridor’ approach, with immediate recognition in both the balance sheet and the income statement for amounts falling outside a ‘corridor’ (see paragraph 42 below);
 - (d) a modified ‘corridor’ approach with deferred recognition of items within the ‘corridor’ and immediate recognition for amounts falling outside the ‘corridor’ (see paragraph 43 below); and
 - (e) deferred recognition for amounts falling outside a ‘corridor’ (see paragraphs 44-46 below).
39. The old IAS 19 required a deferred recognition approach: actuarial gains and losses were recognised as an expense or as income systematically over the expected remaining working lives of those employees. Arguments for this approach are that:
- (a) immediate recognition (even when reduced by a ‘corridor’) can cause volatile fluctuations in liability and expense and implies a degree of accuracy which can rarely apply in practice. This volatility may not be a faithful representation of changes in the obligation but may simply reflect an unavoidable inability to predict accurately the future events that are anticipated in making period-to-period measures; and
 - (b) in the long term, actuarial gains and losses may offset one another. Actuarial assumptions are projected over many years, for example, until the expected date of death of the last pensioner, and are, accordingly, long-term in nature. Departures from the assumptions do not normally denote definite changes in the underlying assets or liability, but are indicators which, if not reversed, may accumulate to denote such changes in the future. They are not a gain or loss of the period but a fine tuning of the cost that emerges over the long term; and
 - (c) the immediate recognition of actuarial gains and losses in the income statement would cause unacceptable volatility.
40. Arguments for an immediate recognition approach are that:
- (a) deferred recognition and ‘corridor’ approaches are complex, artificial and difficult to understand. They add to cost by requiring entities to keep complex records. They also require complex provisions to deal with curtailments, settlements and transitional matters. Also, as such approaches are not used for other uncertain assets and liabilities, it is not clear why they should be used for post-employment benefits;
 - (b) it requires less disclosure because all actuarial gains and losses are recognised;

- (c) it represents faithfully the entity's financial position. An entity will report an asset only when a plan is in surplus and a liability only when a plan has a deficit. Paragraph 95 of the *Framework* notes that the application of the matching concept does not allow the recognition of items in the balance sheet which do not meet the definition of assets or liabilities. Deferred actuarial losses do not represent future benefits and hence do not meet the Framework's definition of an asset, even if offset against a related liability. Similarly, deferred actuarial gains do not meet the *Framework's* definition of a liability;
- (d) the balance sheet treatment is consistent with the proposals in the Financial Instruments Steering Committee's March 1997 Discussion Paper *Accounting for Financial Assets and Liabilities*;
- (e) it generates income and expense items that are not arbitrary and that have information content;
- (f) it is not reasonable to assume that all actuarial gains or losses will be offset in future years; on the contrary, if the original actuarial assumptions are still valid, future fluctuations will, on average, offset each other and thus will not offset past fluctuations;
- (g) deferred recognition attempts to avoid volatility. However, a financial measure should be volatile if it purports to represent faithfully transactions and other events that are themselves volatile. Moreover, concerns about volatility could be addressed adequately by using a second performance statement or a statement of changes in equity;
- (h) immediate recognition is consistent with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Under IAS 8, the effect of changes in accounting estimates should be included in profit or loss for the period if the change affects the current period only but not future periods. Actuarial gains and losses are not an estimate of future events, but result from events before the balance sheet date that resolve a past estimate (experience adjustments) or from changes in the estimated cost of employee service before the balance sheet date (changes in actuarial assumptions);
- (i) any amortisation period (or the width of a 'corridor') is arbitrary. In addition, the amount of benefit remaining at a subsequent date is not objectively determinable and this makes it difficult to carry out an impairment test on any expense that is deferred; and
- (j) in some cases, even supporters of amortisation or the 'corridor' may prefer immediate recognition. One possible example is where plan assets are stolen. Another possible example is a major change in the basis of taxing pension plans (such as the abolition of dividend tax credits for UK pension plans in 1997). However, although there might be agreement on extreme cases, it would prove very difficult to develop objective and non-arbitrary criteria for identifying such cases.

41. The Board found the immediate recognition approach attractive. However, the Board believes that it is not feasible to use this approach for actuarial gains and losses until the Board resolves substantial issues about performance reporting. These issues include:

- (a) whether financial performance includes those items that are recognised directly in equity;
- (b) the conceptual basis for determining whether items are recognised in the income statement or directly in equity;
- (c) whether net cumulative actuarial losses should be recognised in the income statement, rather than directly in equity; and
- (d) whether certain items reported initially in equity should subsequently be reported in the income statement ('recycling').

When the Board makes further progress with those issues, it may decide to revisit the treatment of actuarial gains and losses.

42. E54 proposed a 'corridor approach'. Under this approach, an entity does not recognise actuarial gains and losses to the extent that the cumulative unrecognised amounts do not exceed 10% of the present value of the obligation (or, if greater, 10% of the fair value of plan assets). Arguments for such approaches are that they:

- (a) acknowledge that estimates of post-employment benefit obligations are best viewed as a range around the best estimate. As long as any new best estimate of the liability stays within that range, it would be difficult to say that the liability has really changed. However, once the new best estimate moves outside that range, it is not reasonable to assume that actuarial gains or losses will be offset in future years. If the original actuarial assumptions are still valid, future fluctuations will, on average, offset each other and thus will not offset past fluctuations;
- (b) are easy to understand, do not require entities to keep complex records and do not require complex provisions to deal with settlements, curtailments and transitional matters;
- (c) result in the recognition of an actuarial loss only when the liability (net of plan assets) has increased in the current period and an actuarial gain only when the (net) liability has decreased. By contrast, amortisation methods sometimes result in the recognition of an actuarial loss even if the (net) liability is unchanged or has decreased in the current period, or an actuarial gain even if the (net) liability is unchanged or has increased;
- (d) represent faithfully transactions and other events that are themselves volatile. Paragraph 34 of the *Framework* notes that it may be relevant to recognise items and to disclose the risk of error surrounding their recognition and measurement despite inherent difficulties either in identifying the transactions and other events to be measured or in devising and applying measurement and presentation techniques that can convey messages that correspond with those transactions and events; and

- (e) are consistent with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Under IAS 8, the effect of changes in accounting estimates is included in profit or loss for the period if the change affects the current period only but not future periods. Actuarial gains and losses are not an estimate of future events, but arise from events before the balance sheet date that resolve a past estimate (experience adjustments) or from changes in the estimated cost of employee service before the balance sheet date (changes in actuarial assumptions).
43. Some commentators on E54 argued that an entity should, over a period, recognise actuarial gains and losses within the ‘corridor’. Otherwise, certain gains and losses would be deferred permanently, even though it would be more appropriate to recognise them (for example, to recognise gains and losses that persist for a number of years without reversal or to avoid a cumulative effect on the income statement where the net liability returns ultimately to the original level). However, the Board concluded that such a requirement would add complexity for little benefit.
44. The ‘corridor’ approach was supported by fewer than a quarter of the commentators on E54. In particular, the vast majority of preparers argued that the resulting volatility would not be a realistic portrayal of the long-term nature of post-employment benefit obligations. The Board concluded that there was not sufficient support from its constituents for such a significant change in current practice.
45. Approximately one third of the commentators on E54 supported the deferred recognition approach. Approximately another third of the respondents proposed a version of the corridor approach which applies deferred recognition to amounts falling outside the corridor. It results in less volatility than the corridor alone or deferred recognition alone. In the absence of any compelling conceptual reasons for choosing between these two approaches, the Board concluded that the latter approach would be a pragmatic means of avoiding a level of volatility that many of its constituents consider to be unrealistic.
46. In approving the final Standard, the Board decided to specify the minimum amount of actuarial gains or losses to be recognised, but permit any systematic method of faster recognition, provided that the same basis is applied to both gains and losses and the basis is applied consistently from period to period. The Board was persuaded by the following arguments:
- (a) both the extent of volatility reduction and the mechanism adopted to effect it are essentially practical issues. From a conceptual point of view, the Board found the immediate recognition approach attractive. Therefore, the Board saw no reason to preclude entities from adopting faster methods of recognising actuarial gains and losses. In particular, the Board did not wish to discourage entities from adopting a consistent policy of recognising all actuarial gains and losses immediately. Similarly, the Board did not wish to discourage national standard setters from requiring immediate recognition; and

- (b) where mechanisms are in place to reduce volatility, the amount of actuarial gains and losses recognised during the period is largely arbitrary and has little information content. Also, the new IAS 19 requires an entity to disclose both the recognised and unrecognised amounts. Therefore, although there is some loss of comparability in allowing entities to use different mechanisms, the needs of users are not likely to be compromised if faster (and systematic) recognition methods are permitted.
47. The Board noted that changes in the fair value of any plan assets are, in effect, the results of changing estimates by market participants and are, therefore, inextricably linked with changes in the present value of the obligation. Consequently, the Board decided that changes in the fair value of plan assets are actuarial gains and losses and should be treated in the same way as the changes in the related obligation.
48. The width of a ‘corridor’ (i.e. the point at which it becomes necessary to recognise gains and losses) is arbitrary. To enhance comparability, the Board decided that the width of the ‘corridor’ should be consistent with the current requirement in those countries that have already adopted a ‘corridor’ approach, notably the USA. The Board noted that a significantly narrower ‘corridor’ would suffer from the disadvantages of the ‘corridor’, without being large enough to generate the advantages. On the other hand, a significantly wider ‘corridor’ would lack credibility.

Past Service Cost (paragraphs 96-101 of the Standard)

49. E54 included two alternative treatments for past service cost. The first approach was similar to that used in the old IAS 19 (amortisation for current employees and immediate recognition for former employees). The second approach was immediate recognition of all past service cost.
50. Those who support the first approach argue that:
- (a) an entity introduces or improves employee benefits for current employees in order to generate future economic benefits in the form of reduced employee turnover, improved productivity, reduced demands for increases in cash compensation and improved prospects for attracting additional qualified employees;
 - (b) although it may not be feasible to improve benefits for current employees without also improving benefits for former employees, it would be impracticable to assess the resulting economic benefits for an entity and the period over which those benefits will flow to the entity; and
 - (c) immediate recognition is too revolutionary. It would also have undesirable social consequences because it would deter companies from improving benefits.

51. Those who support immediate recognition of all past service cost argue that:
- (a) amortisation of past service cost is inconsistent with the view of employee benefits as an exchange between an entity and its employees for services rendered: past service cost relates to past events and affects the employer's present obligation arising from employees' past service. Although an entity may improve benefits in the expectation of future benefits, an obligation exists and should be recognised;
 - (b) deferred recognition of the liability reduces comparability; an entity that retrospectively improves benefits relating to past service will report lower liabilities than an entity that granted identical benefits at an earlier date, yet both have identical benefit obligations. Also, deferred recognition encourages entities to increase pensions instead of salaries;
 - (c) past service cost does not give an entity control over a resource and thus does not meet the *Framework's* definition of an asset. Therefore, it is not appropriate to defer recognition of the expense; and
 - (d) there is not likely to be a close relationship between cost—the only available measure of the effect of the amendment—and any related benefits in the form of increased loyalty.
52. Under the old IAS 19, past service cost for current employees was recognised as an expense systematically over the expected remaining working lives of the employees concerned. Similarly, under the first approach set out in E54, past service cost was to be amortised over the average expected remaining working lives of the employees concerned. However, E54 also proposed that the attribution period for current service cost should end when the employee's entitlement to receive all significant benefits due under the plan is no longer conditional on further service. Some commentators on E54 felt that these two provisions were inconsistent.
53. In the light of comments received, the Board concluded that past service cost should be amortised over the average period until the amended benefits become vested, because:
- (a) once the benefits become vested, there is clearly a liability that should be recognised; and
 - (b) although non-vested benefits give rise to an obligation, any method of attributing non-vested benefits to individual periods is essentially arbitrary. In determining how that obligation builds up, no single method is demonstrably superior to all others.
54. Some argue that a 'corridor' approach should be used for past service cost because the use of a different accounting treatment for past service cost than for actuarial gains and losses may create an opportunity for accounting arbitrage. However, the purpose of the 'corridor' is to deal with the inevitable imprecision in the measurement of defined benefit obligations. Past service cost results from a management decision, rather than inherent measurement uncertainty. Consequently, the Board rejected the 'corridor' approach for past service cost.

55. The Board rejected proposals that:
- (a) past service cost should (as under the old IAS 19) be recognised over a shorter period where plan amendments provide an entity with economic benefits over that shorter period: for example, when plan amendments were made regularly, the old IAS 19 stated that the additional cost may be recognised as an expense or income systematically over the period to the next expected plan amendment. The Board believes that the actuarial assumptions should allow for such regular plan amendments and that subsequent differences between the assumed increase and the actual increase are actuarial gains or losses, not a past service cost;
 - (b) past service cost should be recognised over the remaining life expectancy of the participants if all or most plan participants are inactive. The Board believes that it is not clear that the past service cost will lead to economic benefits to the entity over that period; and
 - (c) even if past service cost is generally recognised on a delayed basis, past service cost should not be recognised immediately if the past service cost results from legislative changes (such as a new requirement to equalise retirement ages for men and women) or from decisions by trustees who are not controlled, or influenced, by the entity's management. The Board decided that such a distinction would not be practicable.

56. The old IAS 19 did not specify the basis upon which an entity should amortise the unrecognised balance of past service cost. The Board agreed that any amortisation method is arbitrary and decided to require straight-line amortisation, as that is the simplest method to apply and understand. To enhance comparability, the Board decided to require a single method and not to permit alternative methods, such as methods that assign:

- (a) an equal amount of past service cost to each expected year of employee service; or
- (b) past service cost to each period in proportion to estimated total salaries in that period.

Paragraph 99 confirms that the amortisation schedule is not amended for subsequent changes in the average remaining working life, unless there is a curtailment or settlement.

57. Unlike the old IAS 19, the new IAS 19 treats past service cost for current employees differently from actuarial gains. This means that some benefit improvements may be funded out of actuarial gains that have not yet been recognised in the financial statements. Some argue that the resulting past service cost should not be recognised because:

- (a) the cost of the improvements does not meet the *Framework's* definition of an expense, as there is no outflow or depletion of any asset which was previously recognised in the balance sheet; and
- (b) in some cases, benefit improvements may have been granted only because of actuarial gains.

The Board decided to require the same accounting treatment for all past service cost (ie recognise over the average period until the amended benefits become vested) whether or not they are funded out of an actuarial gain that is already recognised in the entity's balance sheet.

58. Some commentators on E54 argued that the recognition of actuarial gains should be limited if there is unamortised past service cost. The Board rejected this proposal because it would introduce additional complexity for limited benefit. Other commentators would prohibit the recognition of actuarial gains that are earmarked for future benefit improvements. However, the Board believes that if such earmarking is set out in the formal (or constructive) terms of the plan, the benefit improvements should be included in the actuarial assumptions. In other cases, there is insufficient linkage between the actuarial gains and the benefit improvements to justify an exceptional treatment.
59. The old IAS 19 did not specify the balance sheet treatment for past service cost. Some argue that an entity should recognise past service cost immediately both as an addition to the liability and as an asset (prepaid expense) on the grounds that deferred recognition of the liability offsets a liability against an asset (unamortised past service cost) that cannot be used to settle the liability. However, the Board decided that an entity should recognise past service cost for current employees as an addition to the liability gradually over a period, because:
- (a) past service cost does not give an entity control over a resource and thus does not meet the Framework's definition of an asset;
 - (b) separate presentation of a liability and a prepaid expense may confuse users; and
 - (c) although non-vested benefits give rise to an obligation, any method of attributing non-vested benefits to individual periods is essentially arbitrary. In determining how that obligation builds up, no single method is demonstrably superior to all others.
60. The old IAS 19 appeared to treat plan amendments that reduce benefits as negative past service cost (ie amortisation for current employees, immediate recognition for former employees). However, some argue that this results in the recognition of deferred income that conflicts with the *Framework*. They also argue that there is only an arbitrary distinction between amendments that should be treated in this way and curtailments or settlements. Therefore, E54 proposed that:
- (a) plan amendments are:
 - (i) a curtailment if the amendment reduces benefits for future service; and
 - (ii) a settlement if the amendment reduces benefits for past service; and
 - (b) any gain or loss on the curtailment or settlement should be recognised immediately when the curtailment or settlement occurs.

61. Some commentators on E54 argued that such ‘negative plan amendments’ should be treated as negative past service cost by being recognised as deferred income and amortised into the income statement over the working lives of the employees concerned. The basis for this view is that ‘negative’ amendments reduce employee morale in the same way that ‘positive’ amendments increase morale. Also, a consistent treatment avoids the abuses that might occur if an entity could improve benefits in one period (and recognise the resulting expense over an extended period) and then reduce the benefits (and recognise the resulting income immediately). The Board agreed with this view. Therefore, the new IAS 19 treats both ‘positive’ and ‘negative’ plan amendments in the same way.
62. The distinction between negative past service cost and curtailments would be important if:
- (a) a material amount of negative past service cost were amortised over a long period (this is unlikely, as the new IAS 19 requires that negative past service cost should be amortised until the time when those (reduced) benefits that relate to prior service are vested); or
 - (b) unrecognised past service cost or actuarial gains exist. For a curtailment these would be recognised immediately, whereas they would not be affected directly by negative past service cost.

The Board believes that the distinction between negative past service cost and curtailments is unlikely to have any significant effect in practice and that any attempt to deal with exceptional cases would result in excessive complexity.

Recognition and Measurement: an Additional Minimum Liability

63. The Board considered whether it should require an entity to recognise an additional minimum liability where:
- (a) an entity's immediate obligation if it discontinued a plan at the balance sheet date would be greater than the present value of the liability that would otherwise be recognised in the balance sheet;
 - (b) vested post-employment benefits are payable at the date when an employee leaves the entity. Consequently, because of the effect of discounting, the present value of the vested benefit would be greater if an employee left immediately after the balance sheet date than if the employee completes the expected period of service; or
 - (c) the present value of vested benefits exceeds the amount of the liability that would otherwise be recognised in the balance sheet. This could occur where a large proportion of the benefits are fully vested and an entity has not recognised actuarial losses or past service cost.
64. One example of a requirement for an entity to recognise an additional minimum liability is in the US Standard SFAS 87 *Employers' Accounting for Pensions*: the minimum liability is based on current salaries and excludes the effect of deferring certain past service cost and actuarial gains and losses. If the minimum liability exceeds the obligation measured on the normal projected salary basis (with

deferred recognition of certain income and expense), the excess is recognised as an intangible asset (not exceeding the amount of any unamortised past service cost, with any further excess deducted directly from equity) and as an additional minimum liability.

65. The Board believes that such additional measures of the liability are potentially confusing and do not provide relevant information. They would also conflict with the *Framework's* going concern assumption and with its definition of a liability. The new IAS 19 does not require the recognition of an additional minimum liability. Certain of the circumstances discussed in the preceding two paragraphs may give rise to contingent liabilities requiring disclosure under IAS 10 *Events after the Balance Sheet Date*.

Plan Assets (paragraphs 102-107 of the Standard)

66. The new IAS 19 requires explicitly that defined benefit obligations should be recognised as a liability after deducting plan assets (if any) out of which the obligations are to be settled directly (see paragraph 54 of the Standard). This is already widespread, and probably universal, practice. The Board believes that plan assets reduce (but do not extinguish) an entity's own obligation and result in a single, net liability. Although the presentation of that net liability as a single amount in the balance sheet differs conceptually from the offsetting of separate assets and liabilities, the Board decided in issuing IAS 19 in 1998 that the definition of plan assets should be consistent with the offsetting criteria in IAS 32 *Financial Instruments: Disclosure and Presentation*. IAS 32 states that a financial asset and a financial liability should be offset and the net amount reported in the balance sheet when an entity:
- (a) has a legally enforceable right to set off the recognised amounts; and
 - (b) intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.
67. IAS 19 (revised 1998) defined plan assets as assets (other than non-transferable financial instruments issued by the reporting entity) held by an entity (a fund) that satisfies all of the following conditions:
- (a) the entity is legally separate from the reporting entity;
 - (b) the assets of the fund are to be used only to settle the employee benefit obligations, are not available to the entity's own creditors and cannot be returned to the entity (or can be returned to the entity only if the remaining assets of the fund are sufficient to meet the plan's obligations); and
 - (c) to the extent that sufficient assets are in the fund, the entity will have no legal or constructive obligation to pay the related employee benefits directly.
- 67A. In issuing IAS 19 in 1998, the Board considered whether the definition of plan assets should include a fourth condition: that the entity does not control the fund. The Board concluded that control is not relevant in determining whether the assets in a fund reduce an entity's own obligation.

68. In response to comments on E54, the Board decided to modify the definition of plan assets to exclude non-transferable financial instruments issued by the reporting entity. If this were not done, an entity could reduce its liabilities, and increase its equity, by issuing non-transferable equity instruments to a defined benefit plan.

Plan Assets—Revised Definition Adopted in 2000

- 68A. In 1999, the Board began a limited scope project to consider the accounting for assets held by a fund that satisfies parts (a) and (b) of the definition set out in paragraph 67 above, but does not satisfy condition (c) because the entity retains a legal or constructive obligation to pay the benefits directly. IAS 19 (revised 1998) did not address assets held by such funds.
- 68B. The Board considered two main approaches to such funds:
- (a) a **net** approach - the entity recognises its entire obligation as a liability after deducting the fair value of the assets held by the fund; and
 - (b) a **gross** approach - the entity recognises its entire obligation as a liability and recognises its rights to a refund from the fund as a separate asset.
- 68C. Supporters of a net approach made one or more of the following arguments:
- (a) a gross presentation would be misleading, because:
 - (i) where conditions (a) and (b) of the definition in paragraph 67 above are met, the entity does not control the assets held by the fund; and
 - (ii) even if the entity retains a legal obligation to pay the entire amount of the benefits directly, this legal obligation is a matter of form rather than substance;
 - (b) a gross presentation would be an unnecessary change from current practice, which generally permits a net presentation. It would introduce excessive complexity into the Standard, for limited benefit to users, given that paragraph 120(c) already requires disclosure of the gross amounts;
 - (c) a gross approach may lead to measurement difficulties because of the interaction with the 10% corridor for the obligation.
 - (i) One possibility would be to measure the assets at fair value, with all changes in fair value recognised immediately. This might seem inconsistent with the treatment of plan assets, because changes in the fair value of plan assets are one component of the actuarial gains and losses to which the corridor is applied under IAS 19. In other words, this approach would deny entities the opportunity of offsetting gains and losses on the assets against gains and losses on the liability.
 - (ii) A second possibility would be to defer changes in the fair value of the assets to the extent that there are unrecognised actuarial gains and losses on the obligations. However, the carrying amount of the assets would then have no easily describable meaning. It would probably also require complex and arbitrary rules to match the gains and losses on the assets with gains and losses on the obligation.

- (iii) A third possibility would be to measure the assets at fair value, but to aggregate the changes in fair value with actuarial gains and losses on the liability. In other words, the assets would be treated in the same way as plan assets, except the balance sheet presentation would be gross rather than net. However, this would mean that changes in the fair value of the assets could affect the measurement of the obligation; and
- (d) a net approach might be viewed as analogous to the treatment of joint and several liabilities under paragraph 29 of IAS 37. An entity recognises a provision for the part of the obligation for which an outflow of resources embodying economic benefits is probable. The part of the obligation that is expected to be met by other parties is treated as a contingent liability.

68D. Supporters of a gross approach advocated that approach for one or more of the following reasons:

- (a) paragraph 66 above gives an explanation for presenting defined benefit obligations net of plan assets. The explanation focuses on whether offsetting is appropriate. Part (c) of the 1998 definition focuses on offsetting. This suggests that assets that satisfy parts (a) and (b) of the definition, but fail part (c) of the definition, should be treated in the same way as plan assets for recognition and measurement purposes, but should be shown gross on the face of the balance sheet without offsetting;
- (b) if offsetting is allowed when condition (c) is not met, this would seem to be equivalent to permitting a net presentation for ‘in-substance defeasance’ and other analogous cases where IAS 32 indicates explicitly that offsetting is inappropriate. The Board has rejected ‘in-substance defeasance’ for financial instruments (see IAS 39 Application Guidance, paragraph AG59) and there is no obvious reason to permit it in accounting for defined benefit plans. In these cases the entity retains an obligation that should be recognised as a liability and the entity’s right to reimbursement from the plan is a source of economic benefits that should be recognised as an asset. Offsetting would be permitted if the conditions in paragraph 3342 of IAS 32 are satisfied;
- (c) the Board decided in IAS 37 to require a gross presentation for reimbursements related to provisions, even though this was not previously general practice. There is no conceptual reason to require a different treatment for employee benefits;
- (d) although some consider that a gross approach requires an entity to recognise assets that it does not control, others believe that this view is incorrect. A gross approach requires the entity to recognise an asset representing its right to receive reimbursement from the fund that holds those assets. It does not require the entity to recognise the underlying assets of the fund;
- (e) in a plan with plan assets that meet the definition adopted in 1998, the employees’ first claim is against the fund—they have no claim against the entity if sufficient assets are in the fund. In the view of some, the fact that employees must first claim against the fund is more than just a difference in form—it changes the substance of the obligation; and

- (f) defined benefit plans might be regarded under SIC-12 *Consolidation—Special Purpose Entities*, as special purpose entities that the entity controls—and should consolidate. As the offsetting criterion in IAS 19 is consistent with offsetting criteria in other International Accounting Standards, it is relatively unimportant whether the pension plan is consolidated in cases where the obligation and the plan assets qualify for offset. If the assets are presented as a deduction from the related benefit obligations in cases where condition (c) is not met, it could become important to assess whether the entity should consolidate the plan.
- 68E. Some argued that a net approach should be permitted when an entity retains an obligation to pay the entire amount of the benefits directly, but the obligation is considered unlikely to have any substantive effect in practice. The Board concluded that it would not be practicable to establish guidance of this kind that could be applied in a consistent manner.
- 68F. The Board also considered the possibility of adopting a “linked presentation” that UK Financial Reporting Standard FRS 5 *Reporting the Substance of Transactions*, requires for non-recourse finance. Under FRS 5, the face of the balance sheet presents both the gross amount of the asset and, as a direct deduction, the related non-recourse debt. Supporters of this approach argued that it portrays the close link between related assets and liabilities without compromising general offsetting requirements. Opponents of the linked presentation argued that it creates a form of balance sheet presentation that IASB has not used previously and may cause confusion. The Board decided not to adopt the linked presentation.
- 68G. The Board concluded that a net presentation is justified where there are restrictions (including restrictions that apply on bankruptcy of the reporting entity) on the use of the assets so that the assets can be used only to pay or fund employee benefits. Accordingly, the Board decided to modify the definition of plan assets set out in paragraph 67 above by:
- (a) emphasising that the creditors of the entity should not have access to the assets held by the fund, even on bankruptcy of the reporting entity; and
 - (b) deleting condition (c), so that the existence of a legal or constructive obligation to pay the employee benefits directly does not preclude a net presentation, and modifying condition (b) to explicitly permit the fund to reimburse the entity for paying the long-term employee benefits.
- 68H. When an entity retains a direct obligation to the employees, the Board acknowledges that the net presentation is inconsistent with the derecognition requirements for financial instruments in IAS 39 and with the offsetting requirements in IAS 32. However, in the Board’s view, the restrictions on the use of the assets create a sufficiently strong link with the employee benefit obligations that a net presentation is more relevant than a gross presentation, even if the entity retains a direct obligation to the employees.

- 68I. The Board believes that such restrictions are unique to employee benefit plans and does not intend to permit this net presentation for other liabilities if the conditions in IAS 32 and IAS 39 are not met. Accordingly, condition (a) in the new definition refers to the reason for the existence of the fund. The Board believes that an arbitrary restriction of this kind is the only practical way to permit a pragmatic exception to IASC's general offsetting criteria without permitting an unacceptable extension of this exception to other cases.
- 68J. In some plans that exist in some countries, an entity is entitled to receive a reimbursement of employee benefits from a separate fund but the entity has discretion to delay receipt of the reimbursement or to claim less than the full reimbursement. Some argue that this element of discretion weakens the link between the benefits and the reimbursement so much that a net presentation is not justifiable. They believe that the definition of plan assets should exclude assets held by such funds and that a gross approach should be used in such cases. The Board concluded that the link between the benefits and the reimbursement is strong enough in such cases that a net approach is still appropriate.
- 68K. The Board's proposal for extending the definition of plan assets was set out in Exposure Draft E67 *Pension Plan Assets*, published in July 2000. The vast majority of the 39 respondents to E67 supported the proposal.
- 68L. A number of respondents to E67 proposed a further extension of the definition to include certain insurance policies that have similar economic effects to funds whose assets qualify as plan assets under the revised definition proposed in E67. Accordingly, the Board decided to extend the definition of plan assets to include certain insurance policies (now described in IAS 19 as qualifying insurance policies) that satisfy the same conditions as other plan assets. These decisions were implemented in a revised IAS 19, approved by the Board in October 2000.

Plan Assets - Measurement

69. The old IAS 19 stated that plan assets are valued at fair value, but did not define fair value. However, other International Accounting Standards define fair value as 'the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction'. This may imply that no deduction is made for the estimated costs necessary to sell the asset (in other words, it is a mid-market value, with no adjustment for transaction costs). However, some argue that a plan will eventually have to dispose of its assets in order to pay benefits. Therefore, the Board concluded in E54 that plan assets should be measured at market value. Market value was defined, as in IAS 25 *Accounting for Investments*¹, as the amount obtainable from the sale of an asset in an active market.

¹ superseded by IAS 39 *Financial Instruments: Recognition and Measurement* and IAS 40 *Investment Property*.

70. Some commentators on E54 felt that the proposal to measure plan assets at market value would not be consistent with IAS 22 *Business Combinations*¹ and with the measurement of financial assets as proposed in the discussion paper *Accounting for Financial Assets and Financial Liabilities* published by IASC's Financial Instruments Steering Committee in March 1997. Therefore, the Board decided that plan assets should be measured at fair value.
71. Some argue that concerns about volatility in reported profit should be countered by permitting or requiring entities to measure plan assets at a market-related value that reflects changes in fair value over an arbitrary period, such as five years. The Board believes that the use of market-related values would add excessive and unnecessary complexity and that the combination of the 'corridor' approach to actuarial gains and losses with deferred recognition outside the 'corridor' is sufficient to deal with concerns about volatility.
72. The old IAS 19 stated that, when fair values were estimated by discounting future cash flows, the long-term rate of return reflected the average rate of total income (interest, dividends and appreciation in value) expected to be earned on the plan assets during the time period until benefits are paid. It was not clear whether the old IAS 19 allowed a free choice between market values and discounted cash flows, or whether discounted cash flows could be used only when no market value was available. The Board decided that plan assets should be measured by techniques such as discounting expected future cash flows only when no market value is available.
73. Some believe that plan assets should be measured on the following basis, which is required by IAS 25 *Accounting for Investments*²:
- (a) long-term investments are carried in the balance sheet at either cost, revalued amounts or, in the case of marketable equity securities, the lower of cost and market value determined on a portfolio basis. The carrying amount of a long-term investment is reduced to recognise a decline other than temporary in the value of the investment; and
 - (b) current investments are carried in the balance sheet at either market value or the lower of cost and market value.
- The Board rejected this basis because it is not consistent with the basis used for measuring the related obligations.
74. The Board decided that there should not be a different basis for measuring investments that have a fixed redemption value and that match the obligations of the plan, or specific parts thereof. IAS 26 *Accounting and Reporting by Retirement Benefit Plans* permits such investments to be measured on an amortised cost basis.

¹ IAS 22 was withdrawn in 2004 and replaced with IFRS 3 *Business Combinations*.

² superseded by IAS 39 *Financial Instruments: Recognition and Measurement* and IAS 40 *Investment Property*.

75. In response to comments on E54, the Board decided that all plan administration costs (not just investment administration costs, as proposed in E54), should be deducted in determining the return on plan assets.

Reimbursements (paragraphs 104A-104D of the Standard)

- 75A. Paragraph 41 of IAS 19 states that an entity recognises its rights under an insurance policy as an asset if the policy is held by the entity itself. IAS 19 (revised 1998) did not address the measurement of these insurance policies. The entity's rights under the insurance policy might be regarded as a financial asset. However, rights and obligations arising under insurance contracts are excluded from the scope of IAS 39 *Financial Instruments: Recognition and Measurement*. Also, IAS 39 does not apply to "employers' ~~assets and liabilities~~ rights and obligations under employee benefit plans, to which IAS 19 *Employee Benefits* applies". Paragraphs 39-42 of IAS 19 discuss insured benefits in distinguishing defined contribution plans and defined benefit plans, but this discussion does not deal with measurement."
- 75B. In reviewing the definition of plan assets (see paragraphs 68A-68L above), the Board decided to review the treatment of insurance policies that an entity holds in order to fund employee benefits. Even under the revised definition adopted in 2000, the entity's rights under an insurance policy that is not a qualifying insurance policy (as defined in the 2000 revision to IAS 19) are not plan assets.
- 75C. In 2000, the Board decided to introduce recognition and measurement requirements for reimbursements under such insurance policies (see paragraphs 104A-104D). The Board based these requirements on the treatment of reimbursements under paragraphs 53-58 of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. In particular, the Standard requires an entity to recognise a right to reimbursement of post-employment benefits as a separate asset, rather than as a deduction from the related obligations. In all other respects (for example, the use of the 'corridor') the Standard requires an entity to treat such reimbursement rights in the same way as plan assets. This requirement reflects the close link between the reimbursement right and the related obligation.
- 75D. Paragraph 104 states that where plan assets include insurance policies that exactly match the amount and timing of some or all of the benefits payable under the plan, the plan's rights under those insurance policies are measured at the same amount as the related obligations. Paragraph 104D extends that conclusion to insurance policies that are assets of the entity itself.
- 75E. IAS 37 states that the amount recognised for the reimbursement should not exceed the amount of the provision. Paragraph 104A of the Standard contains no similar restriction, because the asset limit in paragraph 58 already applies to prevent the recognition of an asset that exceeds the available economic benefits.

Limit on the Recognition of an Asset (paragraphs 58-60 of the Standard)

76. In certain cases, paragraph 54 of the new IAS 19 would require an entity to recognise an asset. E54 proposed that the amount of the asset recognised should not exceed the aggregate of the present values of:
- (a) any refunds expected from the plan; and
 - (b) any expected reduction in future contributions arising from the surplus.
- In approving E54, the Board took the view that an entity should not recognise an asset at an amount that exceeds the present value of the future benefits that are expected to flow to the entity from that asset. This view is consistent with the Board's proposal that assets should not be carried at more than their recoverable amount (see E55 *Impairment of Assets*). The old IAS 19 contained no such restriction.
77. On reviewing the responses to E54, the Board concluded that the limit on the recognition of an asset should not over-ride the treatments of actuarial losses or past service cost in order not to defeat the purpose of these treatments. Consequently, the limit is likely to come into play only where:
- (a) an entity has chosen the transitional option to recognise the effect of adopting the new IAS 19 over up to five years, but has funded the obligation more quickly; or
 - (a) the plan is very mature and has a very large surplus that is more than large enough to eliminate all future contributions and cannot be returned to the entity.
78. Some commentators argued that the limit in E54 was not operable because it would require an entity to make extremely subjective forecasts of **expected** refunds or reductions in contributions. In response to these comments, the Board agreed that the limit should reflect the **available** refunds or reductions in contributions.

Asset ceiling—Amendment Adopted in May 2002

- 78A. In April 2002, the Board agreed on an amendment to the limit on the recognition of an asset (the asset ceiling) in paragraph 58 of the Standard. The objective of the amendment was to prevent gains (losses) being recognised solely as a result of the deferred recognition of past service cost and actuarial losses (gains).
- 78B. The asset ceiling is specified in paragraph 58 of IAS 19, which requires a defined benefit asset to be measured at the lower of:
- (a) the amount determined under paragraph 54; and
 - (b) the total of:
 - (i) any cumulative unrecognised net actuarial losses and past service cost; and

(ii) the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

- 78C. The problem arises when an entity defers recognition of actuarial losses or past service cost in determining the amount specified in paragraph 54 but is required to measure the defined benefit asset at the net total specified in paragraph 58(b). Paragraph 58(b)(i) could result in the entity recognising an increased asset because of actuarial losses or past service cost in the period. The increase in the asset would be reported as a gain in income. Examples illustrating the issue are given in Appendix C.
- 78D. The Board agreed that recognising gains (losses) arising from past service cost and actuarial losses (gains) is not representationally faithful. Further, the Board holds the view that this issue demonstrates that IAS 19 can give rise to serious problems. The Board intends to undertake a comprehensive review of the aspects of IAS 19 that cause concern, including the interaction of the asset ceiling and the options to defer recognition of certain gains and losses. In the meantime, the Board regards as an improvement a limited amendment to prevent their interaction giving rise to unfaithful representations of events.
- 78E. Paragraph 58A, therefore, prevents gains (losses) from being recognised solely as a result of the deferred recognition of past service cost or actuarial losses (gains).
- 78F. Some Board members and respondents to the exposure draft of this amendment suggested that the issue be dealt with by removing paragraph 58(b)(i). Paragraph 58(b)(i) is the component of the asset ceiling that gives rise to the problem: losses that are unrecognised under paragraph 54 are added to the amount that can be recognised as an asset. However, deleting paragraph 58(b)(i) effectively removes the option of deferred recognition of actuarial losses for all entities that have a defined benefit asset. Removing this option would have wide reaching implications for the deferred recognition approach in IAS 19 that can be considered fully only within the context of the comprehensive review noted above.

Curtailments and Settlements (paragraphs 109-115 of the Standard)

79. Under the old IAS 19, curtailment and settlement **gains** were recognised when the curtailment or settlement **occurred**, but **losses** were recognised when it was **probable** that the curtailment or settlement would occur. The Board concluded that management's intent to curtail or settle a defined benefit plan is not a sufficient basis to recognise a loss. The new IAS 19 requires that curtailment and settlement losses, as well as gains, should be recognised when the curtailment or settlement occurs. The guidance on the recognition of curtailments and settlements has been conformed to the proposals in E59 *Provisions, Contingent Liabilities and Contingent Assets*.

80. Under some national standards:
- (a) the gain or loss on a curtailment includes any unamortised past service cost (on the grounds that a curtailment eliminates the previously expected motivational effect of the benefit improvement), but excludes unrecognised actuarial gains or losses (on the grounds that the entity is still exposed to actuarial risk); and
 - (b) the gain or loss on a settlement includes any unrecognised actuarial gains or losses (on the grounds that the entity is no longer exposed to actuarial risk), but excludes unamortised past service cost (on the grounds that the previously expected motivational effect of the benefit improvement is still present).

The Board considers that this approach has some conceptual merit, but it leads to considerable complexity. The new IAS 19 requires that the gain or loss on a curtailment or settlement should include the related unrecognised actuarial gains and losses and past service cost. This is consistent with the old IAS 19.

Presentation and Disclosure (paragraphs 116-125 of the Standard)

81. The Board decided not to specify whether an entity should distinguish current and non-current portions of assets and liabilities arising from post-employment benefits, because such a distinction may sometimes be arbitrary.
82. Information about defined benefit plans is particularly important to users of financial statements because other information published by an entity will not allow users to estimate the nature and extent of defined benefit obligations and to assess the risks associated with those obligations. The disclosure requirements are based on the following principles:
- (a) the most important information about employee benefits is information about the uncertainty attaching to measures of employee benefit obligations and costs and about the potential consequences of such uncertainty for future cash flows;
 - (b) employee benefit arrangements are often complex, and this makes it particularly important for disclosures to be clear, concise and relevant;
 - (c) given the wide range of views on the treatment of actuarial gains and losses and past service cost, the required disclosures should highlight their impact on the income statement and the impact of any unrecognised actuarial gains and losses and unamortised past service cost on the balance sheet; and
- the benefits derived from information should exceed the cost of providing it.
83. The Board agreed the following changes to the disclosure requirements proposed in E54:
- (a) the description of a defined benefit plan need only be a general description of the type of plan: for example, flat salary pension plans should be distinguished from final salary plans and from post-employment medical plans. Further detail would not be required;

- (b) an entity should disclose the amounts, if any, included in the fair value of plan assets not only for each category of the reporting entity's own financial instruments, but also for any property occupied by, or other assets used by, the entity;
 - (c) an entity should disclose not just the expected return on plan assets, but also the actual return on plan assets;
 - (d) an entity should disclose a reconciliation of the movements in the net liability (or asset) recognised in its balance sheet; and
 - (e) an entity should disclose any amount not recognised as an asset because of the new limit in paragraph 58(b) of the Standard.
84. Some commentators on E54, especially preparers, felt that the disclosures were excessive. A particular concern expressed by several respondents was aggregation: how should an entity aggregate information about many different plans in a concise, meaningful and cost-effective way? Two disclosures that seemed to cause special concern were the analysis of the overall charge in the income statement and the actuarial assumptions. In particular, a number of commentators felt that the requirement to disclose expected rates of salary increases would cause difficulties with employees. However, the Board concluded that all the disclosures were essential.
85. The Board considered whether smaller or non-public entities could be exempted from any of the disclosure requirements. However, the Board concluded that any such exemptions would either prevent disclosure of essential information or do little to reduce the cost of the disclosures.

Benefits other than Post-Employment Benefits

Compensated Absences (paragraphs 11-16 of the Standard)

86. Some argue that an employee's entitlement to future compensated absences does not create an obligation if that entitlement is conditional on future events other than future service. However, the Board believes that an obligation arises as an employee renders service which increases the employee's entitlement (conditional or unconditional) to future compensated absences; for example, accumulating paid sick leave creates an obligation because any unused entitlement increases the employee's entitlement to sick leave in future periods. The probability that the employee will be sick in those future periods affects the measurement of that obligation, but does not determine whether that obligation exists.
87. The Board considered three alternative approaches to measuring the obligation that results from unused entitlement to accumulating compensated absences:
- (a) recognise the entire unused entitlement as a liability, on the basis that any future payments are made first out of unused entitlement and only subsequently out of entitlement that will accumulate in future periods (a FIFO approach);

- (b) recognise a liability to the extent that future payments for the employee group as a whole are expected to exceed the future payments that would have been expected in the absence of the accumulation feature (a group LIFO approach); or
- (c) recognise a liability to the extent that future payments for individual employees are expected to exceed the future payments that would have been expected in the absence of the accumulation feature (an individual LIFO approach).

These methods are illustrated by the following example.

Example

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 year. Such leave is taken first out of the current year's entitlement and then out of any balance brought forward from the previous year (a LIFO basis). At 31 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 four days of paid sick leave in 20X2 and that the remaining 8 employees will take an average of six and a half days each.

Method (a): The entity recognises a liability equal to the undiscounted amount of 200 days of sick pay (two days each, for 100 employees). It is assumed that the first 200 days of paid sick leave result from the unused entitlement.

Method (b): The entity recognises no liability because paid sick leave for the employee group as a whole is not expected to exceed the entitlement of five days each in 20X2.

Method (c): The entity recognises a liability equal to the undiscounted amount of 12 days of sick pay (one and a half days each, for 8 employees).

88. The Board selected method (c), the individual LIFO approach, because that method measures the obligation at the present value of the additional future payments that are expected to arise solely from the accumulation feature. The new IAS 19 notes that, in many cases, the resulting liability will not be material.

Death-in-service Benefits

89. E54 gave guidance on cases where death-in-service benefits are not insured externally and are not provided through a post-employment benefit plan. The Board concluded that such cases will be rare. Accordingly, the Board agreed to delete the guidance on death-in-service benefits.

Other Long-term Employee Benefits (paragraphs 126-131 of the Standard)

90. The Board decided, for simplicity, not to permit or require a ‘corridor’ approach for other long-term employee benefits, as such benefits do not present measurement difficulties to the same extent as post-employment benefits. For the same reason, the Board decided to require immediate recognition of all past service cost for such benefits and not to permit any transitional option for such benefits.

Termination Benefits (paragraphs 132-143 of the Standard)

91. Under some national standards, termination benefits are not recognised until employees have accepted the offer of the termination benefits. However, the Board decided that the communication of an offer to employees (or their representatives) creates an obligation and that obligation should be recognised as a liability if there is a detailed formal plan. The detailed formal plan both makes it probable that there will be an outflow of resources embodying economic benefits and also enables the obligation to be measured reliably.

92. Some argue that a distinction should be made between:

- (a) termination benefits resulting from an explicit contractual or legal requirement; and
- (b) termination benefits resulting from an offer to encourage voluntary redundancy.

The Board believes that such a distinction is irrelevant; an entity offers termination benefits to encourage voluntary redundancy because the entity already has a constructive obligation. The communication of an offer enables an entity to measure the obligation reliably. E54 proposed some limited flexibility to allow that communication to take place shortly after the balance sheet date. However, in response to comments on E54, and for consistency with E59 *Provisions, Contingent Liabilities and Contingent Assets*, the Board decided to remove that flexibility.

93. Termination benefits are often closely linked with curtailments and settlements and with restructuring provisions. Therefore, the Board decided that there is a need for recognition and measurement principles to be similar. The guidance on the recognition of termination benefits (and of curtailments and settlements) has been conformed to the proposals in E59 *Provisions, Contingent Liabilities and Contingent Assets*. The Board agreed to add explicit guidance (not given in E54) on the measurement of termination benefits, requiring discounting for termination benefits not payable within one year.

Equity Compensation Benefits (paragraphs 144-152 of the Standard)

94. ~~The Board decided that the new IAS 19 should not:~~
- ~~(a) include recognition and measurement requirements for equity compensation benefits, in view of the lack of international consensus on the recognition and measurement of the resulting obligations and costs; or~~
 - ~~(b) require disclosure of the fair value of employee share options, in view of the lack of international consensus on the fair value of many employee share options.¹~~

Transition and Effective Date (paragraphs 153-158 of the Standard)

95. The Board recognises that the new IAS 19 will lead to significant changes for some entities. E54 proposed to mitigate this problem by delaying the effective date of the new IAS 19 until 3 years after its approval. In response to comments on E54, the Board introduced a transitional option to amortise an increase in defined benefit liabilities over not more than five years. In consequence, the Board decided that it was not necessary to delay the effective date.
96. E54 proposed no specific transitional provisions. Consequently, an entity applying the new IAS 19 for the first time would have been required to compute the effect of the ‘corridor’ retrospectively. Some commentators felt that this would be impracticable and would not generate useful information. The Board agreed with these comments. Accordingly, the new IAS 19 confirms that, on initial adoption, an entity does not compute the effect of the ‘corridor’ retrospectively.

¹ Paragraphs 144-152 of IAS 19 were deleted by IFRS 2 *Share-based Payment*.

