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IFRS Foundation: Training Material for the *IFRS® for SMEs*

Module 28 – Employee Benefits

IFRS™

IFRS Foundation: Training Material for the *IFRS® for SMEs*

including the full text of
Section 28 *Employee Benefits*
of the International Financial Reporting Standard (IFRS)
for Small and Medium-sized Entities (SMEs)
issued by the International Accounting Standards Board on 9 July 2009

with extensive explanations, self-assessment questions and case studies

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Module 28 – Employee Benefits

This training material has been prepared by IFRS Foundation education staff and has not been approved by the International Accounting Standards Board (IASB).
The accounting requirements applicable to small and medium-sized entities (SMEs) are set out in the *International Financial Reporting Standard (IFRS) for SMEs*, which was issued by the IASB in July 2009.

INTRODUCTION

This module focuses on the accounting and reporting of employee benefits in accordance with Section 28 *Employee Benefits* of the *IFRS for SMEs*. It introduces the learner to the subject, guides the learner through the official text, develops the learner's understanding of the requirements through the use of examples and indicates significant judgements that are required in accounting for employee benefits. Furthermore, the module includes questions designed to test the learner's knowledge of the requirements and case studies to develop the learner's ability to account for employee benefits in accordance with the *IFRS for SMEs*.

Learning objectives

Upon successful completion of this module you should know the financial reporting requirements for employee benefits in accordance with the *IFRS for SMEs*. Furthermore, through the completion of case studies that simulate aspects of the real world application of that knowledge, you should have enhanced your ability to account for employee benefits in accordance with the *IFRS for SMEs*. In particular you should, in the context of the *IFRS for SMEs*, be able:

- to identify four types of employee benefits accounted for in accordance with Section 28—short-term employee benefits, post-employment benefits, other long-term employee benefits and termination benefits
- to identify when and how to recognise the cost of employee benefits
- to measure employee benefits
- to present and disclose employee benefits in financial statements
- to demonstrate an understanding of the significant judgements that are required in accounting for employee benefits.

Module 28 – Employee Benefits

IFRS for SMEs

The *IFRS for SMEs* is intended to apply to the general purpose financial statements of entities that do not have public accountability (see Section 1 *Small and Medium-sized Entities*).

The *IFRS for SMEs* includes mandatory requirements and other material (non-mandatory) that is published with it.

The material that is not mandatory includes:

- a preface, which provides a general introduction to the *IFRS for SMEs* and explains its purpose, structure and authority.
- implementation guidance, which includes illustrative financial statements and a disclosure checklist.
- the Basis for Conclusions, which summarises the IASB's main considerations in reaching its conclusions in the *IFRS for SMEs*.
- the dissenting opinion of an IASB member who did not agree with the publication of the *IFRS for SMEs*.

In the *IFRS for SMEs* the Glossary is part of the mandatory requirements.

In the *IFRS for SMEs* there are appendices in Section 21 *Provisions and Contingencies*, Section 22 *Liabilities and Equity* and Section 23 *Revenue.* Those appendices are non-mandatory guidance.

Introduction to the requirements

The objective of general purpose financial statements of a small or medium-sized entity is to provide information about the entity's financial position, performance and cash flows that is useful for economic decision-making by a broad range of users who are not in a position to demand reports tailored to meet their particular information needs. The objective of Section 28 is to prescribe the accounting treatment for employee benefits (other than share-based payments that are accounted for in accordance with the requirements of Section 26 *Share-based Payment*), so that users of the financial statements can see information about an entity's employee benefits.

Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees, including directors and management. An entity shall recognise the cost of all employee benefits to which its employees have become entitled as a result of service rendered to the entity in the period as an expense, unless another section of this IFRS requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

Obligations for short-term employee benefits are measured at undiscounted amounts. Liabilities for obligations under post-employment defined benefit plans and other long-term employee benefits are measured by subtracting the fair value at the reporting date of plan assets (if any) from the present value of its obligations under defined benefit plans (or other long-term employee benefit scheme) at the reporting date. Obligations to pay termination benefits are measured at the best estimate of the expenditure that would be required to settle the obligation at the reporting date.

The section also specifies disclosures for employee benefits.

Module 28 – Employee Benefits

REQUIREMENTS AND EXAMPLES

The contents of Section 28 *Employee Benefits* of the *IFRS for SMEs* are set out below and shaded grey. Terms defined in the Glossary of the *IFRS for SMEs* are also part of the requirements. They are in **bold type** the first time they appear in the text of Section 28. The notes and examples inserted by the IFRS Foundation education staff are not shaded. Other annotations inserted by the IFRS Foundation staff are presented within square brackets in ***bold italics***. The insertions made by the staff do not form part of the *IFRS for SMEs* and have not been approved by the IASB.

Scope of this section

28.1 **Employee benefits** are all forms of consideration given by an entity in exchange for service rendered by employees, including directors and management. This section applies to all employee benefits, except for **share-based payment transactions**, which are covered by Section 26 *Share-based Payment*. Employee benefits covered by this section will be one of the following four types:

(a) short-term employee benefits, which are employee benefits (other than **termination benefits**) that are wholly due within twelve months after the end of the period in which the employees render the related service.

[Refer: paragraphs 28.4−28.8 and 28.39]

(b) **post-employment benefits**, which are employee benefits (other than termination benefits) that are payable after the completion of employment.

[Refer: paragraphs 28.9−28.28, 28.40 and 28.41]

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

[Refer: paragraphs 28.29, 28.30 and 28.42]

(d) termination benefits, which are employee benefits payable as a result of either:

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

(ii) an employee's decision to accept voluntary redundancy in exchange for those benefits.

[Refer: paragraphs 28.31−28.37, 28.43 and 28.44]

Notes

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. Furthermore, an employee may provide services to an entity on a full-time, part-time, permanent, casual or temporary basis. For the purpose of this section, employees include directors and other management personnel.

28.2 Employee benefits also include share-based payment transactions by which employees receive equity instruments (such as shares or share options) or cash or other assets of the entity in amounts that are based on the price of the entity's shares or other equity instruments of the entity. An entity shall apply Section 26 in accounting for share-based payment transactions.

General recognition principle for all employee benefits

28.3 An entity shall recognise the cost of all employee benefits to which its employees have become entitled as a result of service rendered to the entity during the **reporting period**:

(a) as a liability, after deducting amounts that have been paid either directly to the employees or as a contribution to an employee benefit fund. If the amount paid exceeds the obligation arising from service before the **reporting date**, an entity shall recognise that excess as an asset to the extent that the prepayment will lead to a reduction in future payments or a cash refund.

(b) as an expense, unless another section of this IFRS requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

Examples – general recognition principle for employee benefits

Ex 1 **On 1 January 20X2 an entity paid one of its employees CU1,000[1] for work performed in the manufacture of the entity's goods in December 20X1. All of the goods manufactured by the employee in December were sold to the entity's customers by 31 December 20X1.**

At 31 December 20X1 the entity must recognise a liability of CU1,000 (accrual of employee benefits) for the amount due to the employee. This amount would be recognised as an expense (part of cost of goods sold—see Section 13 *Inventories* paragraphs 13.5, 13.8 and 13.20).

Ex 2 **The facts are the same as in example 1 above. However, in this example, the goods manufactured in December were in the entity's inventories at 31 December 20X1.**

At 31 December 20X1 the entity must recognise a liability (accrual of employee benefits) to recognise the amount due to the employee and an asset (inventories) of CU1,000 to recognise the work performed.

Ex 3 **The facts are the same as in example 1 above. However, in this example, the employee manufactured an item of equipment for use by the entity in the manufacture of goods in future periods.**

At 31 December 20X1 the entity must recognise a liability of CU1,000 (accrual of employee benefits) to recognise the amount due to the employee. That amount is also included in the cost of the equipment (an asset) in accordance with paragraph 17.10(b) rather than included in profit or loss in the period of construction.

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[1] In this example, and in all other examples in this module, monetary amounts are denominated in 'currency units (CU)'.

Note: The amount included in the cost of the asset will be recognised in profit or loss as depreciation expense over the useful life of the asset, or as an impairment loss, or in arriving at the gain or loss on derecognition of the item of equipment (see Section 17 *Property, Plant and Equipment*). Depreciation of manufacturing equipment will generally be added to the cost of the inventories produced (see Section 13). The cost of the inventories produced will be recognised in profit or loss when the related revenue is recognised.

Short-term employee benefits

Examples

28.4 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) when 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.

Notes

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 (see paragraph 28.5).

Examples – short-term employee benefits

Ex 4 **On 31 December 20X1 a retailer paid its employees CU1,000,000 (net of CU400,000 income taxes deducted from the employees' remuneration and paid by the retailer on behalf of the employees to the tax authorities) for work performed in December 20X1. On 1 January 20X2 the entity paid to the government the CU400,000 deducted from its employees' remuneration.**

On 2 January 20X2 the retailer paid a further CU20,000 to the tax authority. This tax was levied by the tax authority directly on the retailer's December 20X1 payroll (ie the retailer cannot recover the payroll tax from its employees).

In December 20X1 the retailer incurred CU1,400,000 short-term employee benefits (ie CU1,000,000 paid to employees and CU400,000 paid on behalf of its employees to the revenue authorities).

Note: The CU20,000 payroll tax levied directly on the retailer is not an employee benefit—it is not consideration given by the entity in exchange for services rendered by its employees.

The retailer could recognise the transactions as follows:

31 December 20X1

Dr Profit or loss	CU1,400,000	
Cr Cash		CU1,000,000
Cr Liability (accrued expense)		CU400,000

To recognise the short-term employee benefits expenses incurred in December 20X1.

Dr Profit or loss	CU20,000	
Cr Liability (accrued expense)		CU20,000

To recognise the tax levied on the entity's payroll incurred in December 20X1.

1 January 20X2

Dr Liability (accrued expense)	CU400,000	
Cr Cash		CU400,000

To recognise the payment to the government of taxes collected on its behalf from the entity's employees accrued in 20X1.

2 January 20X2

Dr Liability (accrued expense)	CU20,000	
Cr Cash		CU20,000

To recognise the settlement of the tax levied on the entity's payroll accrued in 20X1.

Ex 5 **An entity's employees 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.**

The sick leave is a short-term employee benefit—the paid absence must occur within twelve months after the end of the period in which the employees render the related employee service.

Ex 6 **A profit-sharing plan requires an entity to pay a specified proportion of its profit for the year to employees who serve throughout the year.**

The profit-sharing plan is a short-term employee benefit—the profit share is due to the employees who served throughout the year at the end of the financial reporting period (ie within twelve months after the end of the period in which the employees render the related employee service).

Ex 7 **An entity provides its expatriate employees with residential accommodation that it rents from independent third parties.**

The expatriate housing scheme is a short-term employee benefit—the housing benefit is due in the period in which the employees render the related employee service.

Examples – not short-term employee benefits

Ex 8 **The facts are the same as in example 5. However, in this example, the unused sick leave may be carried forward for three calendar years. Many employees accumulate more than 10 days' unused sick leave.**

The sick leave is not a short-term employee benefit as the paid absence is not expected to occur wholly within twelve months after the end of the period in which the employees render the related employee service. The sick leave is accounted for as other long-term employee benefits (see paragraphs 28.29 and 28.30).

Ex 9 **A profit-sharing plan requires an entity to pay a specified proportion of its cumulative profit for a five-year period to employees who serve throughout the five-year period.**

The profit-sharing plan is not a short-term employee benefit—the profit share is not due wholly within twelve months after the end of the period in which the employees render the related employee service. The profit-sharing plan is accounted for as other long-term employee benefits (see paragraphs 28.29 and 28.30).

Measurement of short-term benefits generally

28.5 When an employee has rendered service to an entity during the reporting period, the entity shall measure the amounts recognised in accordance with paragraph 28.3 at the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service.

Notes

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

(a) accumulating (see paragraph 28.6); and

(b) non-accumulating (see paragraph 28.7).

Recognition and measurement—short-term compensated absences

28.6 An entity may compensate employees for absence for various reasons including annual vacation leave and sick leave. Some short-term compensated absences accumulate—they can be carried forward and used in future periods if the employee does not use the current period's entitlement in full. Examples include annual vacation leave and sick leave. An entity shall recognise the expected cost of **accumulating**

compensated absences when the employees render service that increases their entitlement to future compensated absences. The entity shall measure the expected cost of accumulating compensated absences at the undiscounted additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the end of the reporting period. The entity shall present this amount as a **current liability** at the reporting date.

Examples – accumulating paid absences

Ex 10 **An entity's employees 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 any balance brought forward from the previous year and then out of the current year's entitlement (a FIFO basis).**

The entity does not anticipate a future saving due to unused sick leave lapsing.

At 1 January 20X1 the entity's obligation for sick leave (current liability) was measured at CU2,600.

At 31 December 20X1 the entity's sick leave records were as follows:

Employee	*Wage rate (per working day in 20X1)*	*Accumulated sick leave days due on 01/01/20X1*	*Days sick leave earned in 20X1*	*Days sick leave taken in 20X1*	*Percentage wage increase effective from 01/01/20X2*
1	CU400	4.5	5	2	5%
2	CU310	2	5	3	2%
3	CU250	0	5	9	2%
4	CU180	1	5	4.5	6%

At 31 December 20X1 the entity's liability for sick leave is CU3,651 (ie CU2,100 for employee 1 + CU1,265 for employee 2 + CU286 for employee 4), calculated as follows:

- Employee 1: CU400 current wage rate per working day × 1.05 to recognise the expected increase in salary × 5 (maximum) days due at 31 December 20X1 and expected to be taken in 20X2 = CU2,100.
- Employee 2: CU310 current wage rate per working day × 1.02 to recognise the expected increase in salary × 4 days due at 31 December 20X1 and expected to be taken in 20X2 = CU1,265.
- Employee 3: CU250 current wage rate per working day × 1.02 to recognise the expected increase in salary × 0 days due at 31 December 20X1 = CU0.
- Employee 4: CU180 current wage rate per working day × 1.06 to recognise the expected increase in salary × 1.5 days due at 31 December 20X1 and expected to be taken in 20X2 = CU286.

If the entity has not charged sick leave accrued in 20X0 and taken by employees in 20X1 against the sick leave obligation then the obligation for sick leave at 31 December 20X1 could be recognised using the following journal entry:

Dr Profit or loss (or assets—see paragraph 28.3(b))	CU1,051[(a)]	
Cr Short-term paid absences (sick leave)		CU1,051

To recognise the increase in accumulating paid absences related to sick leave.

(a) CU3,651 sick leave liability as at 31 December 20X1 less CU2,600 sick leave liability as at 1 January 20X1.

Ex 11 **The facts are the same as in example 10. However, in this example, the employee receives payment from the entity for sick leave that is not taken within twelve months after the end of the period in which the employee renders the related service. The entity pays the employee for such unused sick leave on the last day of the year following the year in which the employee rendered the service.**

On 31 December 20X1 the entity pays employee 1 CU1,000 (ie CU400 wage rate per working day × 2.5 days' vested sick leave accrued in 20X0 that was unused at 31 December 20X1).

At 31 December 20X1 the entity's liability for sick leave is CU3,651 (ie CU2,100 for employee 1 + CU1,265 for employee 2 + CU286 for employee 4).

- Employee 1: CU400 wage rate per working day × 1.05 to recognise the expected increase in salary × 5 days accumulated at 31 December 20X1 expected to be taken in 20X2 = CU2,100.
- Employee 2: CU310 wage rate per working day × 1.02 to recognise the expected increase in salary × 4 days due at 31 December 20X1 expected to be taken in 20X2 = CU1,265.
- Employee 3: CU250 wage rate per working day × 1.02 to recognise the expected increase in salary × 0 days due at 31 December 20X1 expected to be taken in 20X2 = CU0.
- Employee 4: CU180 wage rate per working day × 1.06 to recognise the expected increase in salary × 1.5 days due at 31 December 20X1 expected to be taken in 20X2 = CU286.

If the entity has not charged sick leave accrued in 20X0 and taken by employees in 20X1 against the sick leave obligation then the obligation for sick leave at 31 December 20X1 could be recognised using the following journal entries:

31 December 20X1

Dr Short-term paid absences (sick leave)	CU1,000[(a)]	
Cr Cash		CU1,000

To recognise the payment to settle the obligation for sick leave not taken.

Dr Profit or loss (or assets—see paragraph 28.3(b))	CU2,051[(b)]	
Cr Short-term paid absences (sick leave)		CU2,051

To recognise the increase in accumulating paid absences related to sick leave.

[(a)] CU400 wage rate per working day × 2.5 days vested sick leave accrued in 20X0 that was unused at 31 December 20X1.

[(b)] CU3,651 sick leave liability as at 31 December 20X1 less CU1,600 (ie CU2,600 sick leave liability at 1 January 20X1 less CU1,000 settled on 31 December 20X1).

Ex 12 **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, on the basis of experience that 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.

28.7 An entity shall recognise the cost of other (non-accumulating) compensated absences when the absences occur. The entity shall measure the cost of non-accumulating compensated absences at the undiscounted amount of salaries and wages paid or payable for the period of absence.

Examples – non-accumulating paid absences

Ex 13 **The facts are the same as in example 10. However, in this example, sick leave cannot be carried forward to the next calendar year.**

At 31 December 20X1 the entity has no liability for sick leave—all unused sick leave lapses at the end of each calendar year.

Ex 14 **The facts are the same as in example 12. However, in this example, sick leave cannot be carried forward to the next calendar year.**

At 31 December 20X1 the entity has no liability for sick leave—all unused sick leave lapses at the end of each calendar year.

Ex 15 **An entity's employees are each entitled to 25 working days' holiday leave per year. Unused holiday leave vests at the end of each calendar year. Employees are paid for all vested holiday leave in the month following the end of a calendar year at the previous year's salary rates.**

At 1 January 20X1 the entity's obligation for holiday leave vested at the end of 20X0 (current liability) was measured at CU2,600.

At 31 December 20X1 the entity's holiday leave records were as follows:

Employee	*Wage rate (per working day in 20X0)*	*Vested holiday leave days on 01/01/20X1*[(a)]	*Days holiday leave taken in 20X1*	*Percentage wage increase effective from 01/01/20X1*
1	CU400	4.5	20	5%
2	CU310	2	22	2%
3	CU250	0	25	2%
4	CU180	1	10	6%

[(a)] Settled in cash on 31/01/20X1.

On 31 January 20X1 the entity pays its employees CU2,600 (ie CU1,800 for employee 1 + CU620 for employee 2 + CU180 for employee 4) for vested holiday leave.

- Employee 1: CU400 wage rate per working day × 4.5 vested non-accumulating holiday leave at 31 December 20X0 = CU1,800.
- Employee 2: CU310 wage rate per working day × 2 vested non-accumulating holiday leave at 31 December 20X0 = CU620.
- Employee 3: CU250 wage rate per working day × 0 vested non-accumulating holiday leave at 31 December 20X0 = CU0.
- Employee 4: CU180 wage rate per working day × 1 vested non-accumulating holiday leave at 31 December 20X0 = CU180.

On 31 January 20X1 the entity could account for the settlement of its obligation for holiday leave as follows:

	Dr	Cr
Dr Short-term paid absences (holiday leave)	CU2,600	
Cr Cash		CU2,600

To recognise settlement of non-accumulating paid holiday leave.

At 31 December 20X1 the entity's liability for holiday leave is CU5,911 (ie CU2,100 for employee 1 + CU949 for employee 2 + CU2,862 for employee 4).

- Employee 1: CU400 wage rate per working day × 1.05 to recognise the expected increase in salary × 5 vested non-accumulating holiday leave at 31 December 20X1 = CU2,100.
- Employee 2: CU310 wage rate per working day × 1.02 to recognise the expected increase in salary × 3 vested non-accumulating holiday leave at 31 December 20X1 = CU949.
- Employee 3: CU250 wage rate per working day × 1.02 to recognise the expected increase in salary × 0 vested non-accumulating holiday leave at 31 December 20X1 = CU0.

- Employee 4: CU180 wage rate per working day × 1.06 to recognise the expected increase in salary × 15 vested non-accumulating holiday leave at 31 December 20X1 = CU2,862.

At 31 December 20X1 the entity could account for the accrual of its obligation for holiday leave as follows:

Dr Profit or loss (or assets—see paragraph 28.3(b))	CU5,911	
Cr Short-term paid absences (holiday leave)		CU5,911

To recognise non-accumulating paid holiday leave.

Recognition—profit-sharing and bonus plans

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

(a) the entity has a present legal or **constructive obligation** to make such payments as a result of past events (this means that the entity has no realistic alternative but to make the payments), and

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

Notes

A constructive obligation is an obligation that derives from an entity's actions when:

(a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept particular responsibilities; and

(b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

Examples – profit-sharing and bonus plans

Ex 16 **A profit-sharing plan requires an entity to pay employees 5 per cent of its profit for the year before profit-sharing bonuses . For the year ended 31 December 20X1 the entity recorded a profit before profit-sharing bonuses of CU2 million. Bonuses are paid in January.**

At 31 December 20X1 the entity could account for its profit-sharing plan obligation as follows:

Dr Profit or loss (or assets—see paragraph 28.3(b))	CU100,000[a]	
Cr Profit-sharing bonuses plan		CU100,000

To recognise the profit-sharing bonuses plan liability.

[a] 5% × CU2,000,000. The amount is not discounted (see paragraph 28.5).

Ex 17 **In 20X1 an entity implemented a profit-sharing plan. The plan requires the entity to pay 3 per cent of its profit before profit-sharing bonuses for the year to employees who serve throughout the current year and who will continue to serve throughout the following year. For the year ended 31 December 20X1 the entity recorded a profit before profit-sharing bonuses of CU1 million. The entity expects to save 10 per cent of the maximum possible bonus payment through staff turnover. The bonus will be paid on 31 December 20X2.**

At 31 December 20X1 the entity could account for its profit-sharing plan obligation as follows:

Dr Profit or loss (or assets—see paragraph 28.3(b))	CU27,000[(a)]	
Cr Profit-sharing bonuses plan		CU27,000

To recognise the profit-sharing bonuses plan liability.

[(a)] 3% × CU1,000,000 = CU30,000 maximum possible bonus.
CU30,000 less 10% × CU30,000 saving due to staff turnover = CU27,000. The amount is not discounted (see paragraph 28.5).

Post-employment benefits: distinction between defined contribution plans and defined benefit plans

28.9 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 shall apply this section to all such arrangements whether or not they involve the establishment of a separate entity to receive contributions and to pay benefits. In some cases, these arrangements are imposed by law rather than by action of the entity. In some cases, these arrangements arise from actions of the entity even in the absence of a formal, documented plan.

28.10 Post-employment benefit plans are classified as either **defined contribution plans** or **defined benefit plans**, depending on their principal terms and conditions.

(a) Defined contribution plans are post-employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund) and has no legal or constructive obligation to pay further contributions or to make direct benefit payments to employees if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods. 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 insurer, together with investment returns arising from the contributions.

(b) Defined benefit plans are post-employment benefit plans other than defined contribution plans. Under defined benefit plans, the entity's obligation is to provide

the agreed benefits to current and former employees, and actuarial risk (that benefits will cost more or less than expected) and investment risk (that returns on assets set aside to fund the benefits will differ from expectations) are borne, in substance, by the entity. If actuarial or investment experience is worse than expected, the entity's obligation may be increased, and vice versa if actuarial or investment experience is better than expected.

Notes

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.

Such cases are defined benefit plans.

Multi-employer plans and state plans

28.11 Multi-employer plans and state plans are classified as defined contribution plans or defined benefit plans on the basis of the terms of the plan, including any constructive obligation that goes beyond the formal terms. However, if sufficient information is not available to use defined benefit accounting for a multi-employer plan that is a defined benefit plan, an entity shall account for the plan in accordance with paragraph 28.13 as if it was a defined contribution plan and make the disclosures required by paragraph 28.40.

Notes

One example of a defined benefit multi-employer plan is one where:

(a) the plan is financed on a pay-as-you-go basis: 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 in 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 end of the reporting period 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.

Insured benefits

28.12 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 has a legal or constructive obligation either:

(a) to pay the employee benefits directly when they become due, or

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

A constructive obligation could arise indirectly through the plan, through the mechanism for setting future premiums, or through a **related party** relationship with the insurer. If the entity retains such a legal or constructive obligation, the entity shall treat the plan as a defined benefit plan.

Post-employment benefits: defined contribution plans

Recognition and measurement

28.13 An entity shall recognise the contribution payable for a period:

(a) as a liability, after deducting any amount already paid. If contribution payments exceed the contribution due for service before the reporting date, an entity shall recognise that excess as an asset.

(b) as an expense, unless another section of this IFRS requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

Examples – defined contribution plans

Ex 18 **On 8 January 20X2 a retailer paid CU10,000 contribution to a defined contribution plan in part exchange for services performed by the entity's employees in December 20X1.**

At 31 December 20X1 the retailer must recognise CU10,000 liability (accrual of post-employment benefits for employees' defined contribution plan) and CU10,000 expense in the determination of profit or loss for the year ended 31 December 20X1.

On 31 December 20X1 the retailer could record the following journal entry:

Dr Profit or loss	CU10,000	
Cr Post-employment benefits–defined contribution		CU10,000

To recognise the accrual of the post-employment benefits expenses incurred in December.

On 8 January 20X2 the retailer could record the following journal entry:

Dr Post-employment benefits–defined contribution	CU10,000	
Cr Cash		CU10,000

To recognise the settlement of defined contribution post-employment benefits plan expense accrued in 20X1.

Ex 19 **The facts are the same as in example 18. However, in this example, the entity is a manufacturer and the goods manufactured in December were in the entity's inventories at 31 December 20X1.**

At 31 December 20X1 the manufacturer must recognise a liability (accrual of post-employment benefits for employees' defined contribution plan) and an asset (inventories) of CU10,000. The inventories will be recognised in the determination of profit or loss when impaired or sold (see paragraphs 13.19 and 13.20).

Ex 20 **Then facts are the same as in example 18. However, in this example, in December the employees manufactured an item of equipment for use by the entity in the manufacture of goods in future periods.**

At 31 December 20X1 the entity must recognise a liability (accrual of post-employment benefits for employees' defined contribution plan) and an asset (property, plant and equipment) of CU10,000. The property, plant and equipment will be recognised in the determination of profit or loss when it is depreciated (see paragraph 17.17), impaired (see paragraph 17.24) or sold (see paragraph 17.28).

Ex 21 **On 20 December 20X1 a retailer paid CU10,000 contribution to a defined contribution plan. CU7,800 of that amount is in part exchange for services performed by the entity's employees in December 20X1 and the balance of CU2,200 is in respect of services to be performed in 20X2.**

At December 20X1 the retailer must recognise an asset of CU2,200 (prepaid post-employment benefits for employees' defined contribution plan) and CU7,800 staff cost for the year ended 31 December 20X1.

Note: The staff cost is recognised either as an expense or as part of the cost of an asset in accordance with paragraph 28.3(b).

Post-employment benefits: defined benefit plans

Recognition

28.14 In applying the general recognition principle in paragraph 28.3 to defined benefit plans, an entity shall recognise:

(a) a liability for its obligations under defined benefit plans net of plan assets—its **defined benefit liability** (see paragraphs 28.15–28.23).

(b) the net change in that liability during the period as the cost of its defined benefit plans during the period (see paragraphs 28.24–28.27).

Measurement of the defined benefit liability

28.15 An entity shall measure a defined benefit liability for its obligations under defined benefit plans at the net total of the following amounts:

(a) the **present value** of its obligations under defined benefit plans (its **defined benefit obligation**) at the reporting date (paragraphs 28.16–28.22 provide guidance for measuring this obligation), minus

(b) the fair value at the reporting date of **plan assets** (if any) out of which the obligations are to be settled directly. Paragraphs 11.27–11.32 establish requirements for determining the fair values of those plan assets that are **financial assets**.

Notes

A defined benefit liability is the present value of the defined benefit obligation at the reporting date that exceeds the fair value at the reporting date of plan assets (if any) out of which the obligations are to be settled directly.

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

Plan assets are assets held by a long-term employee benefit fund and qualifying insurance policies. Qualifying insurance policies are not defined in the *IFRS for SMEs*. In the absence of guidance in the *IFRS for SMEs* an entity is permitted (but is not required) to consider the guidance in full IFRSs. IAS 19 *Employee Benefits* (as issued at 9 July 2009) defines qualifying insurance policies as an insurance policy[2] issued by an insurer that is not a related party (as defined in IAS 24 *Related Party Disclosures*) of the reporting entity, if the proceeds of the policy:

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

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

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

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

For funded defined benefit plans, when the fair value of plan assets at the reporting date exceeds the present value of the plan obligations at the reporting date, the surplus is recognised as an asset if certain conditions are met (see paragraph 28.22).

Examples – defined benefit plans

Ex 22 **A defined benefit plan provides a monthly pension of 0.2 per cent of final salary for each year of service. The pension is payable from the age of 65. At 31 December 20X1 the present value of the entity's obligations under the plan was appropriately estimated at CU200,000. Furthermore, the fair value of the plan assets out of which the obligations are to be settled directly was determined at CU180,000 as at 31 December 20X1.**

At 31 December 20X1 the entity must recognise a liability (post-employment benefits) of CU20,000 for its defined benefit plan (ie CU200,000 obligation less CU180,000 plan assets set aside to fund the defined benefit obligation).

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

Ex 23 **The facts are the same as in example 22. However, in this example, the entity's obligations for the defined benefit scheme are unfunded.**

At 31 December 20X1 the entity must recognise a liability (post-employment benefits) of CU200,000 for its defined benefit plan.

Inclusion of both vested and unvested benefits

28.16 The present value of an entity's obligations under defined benefit plans at the reporting date shall reflect the estimated amount of benefit that employees have earned in return for their service in the current and prior periods, including benefits that are not yet **vested** (see paragraph 28.26) and including the effects of benefit formulas that give employees greater benefits for later years of service. This requires the entity to determine how much benefit is attributable to the current and prior periods on the basis of the plan's benefit formula 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 influence the cost of the benefit. The actuarial assumptions shall be unbiased (neither imprudent nor excessively conservative), mutually compatible, and selected to lead to the best estimate of the future cash flows that will arise under the plan.

Notes

The rights to vested benefits, under the conditions of a retirement plan, are not conditional on continued employment.

In the context of measuring the present value of an entity's defined benefit obligation paragraph 28.16 describes actuarial assumptions as estimates about demographic variables (such as employee turnover and mortality) and financial variables (such as future increases in salaries and medical costs) that influence the cost of the benefit. IAS 19 *Employee Benefits* (as issued at 9 July 2009) of full IFRSs provides guidance about actuarial assumptions. In applying the *IFRS for SMEs* an entity is permitted (but is not required) to consider the guidance in IAS 19.

Paragraph 73 of IAS 19 specifies that 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

  (iv) claim rates under medical plans; and

(b) financial assumptions, dealing with items such as:

  (i) the discount rate;

(ii) future salary and benefit levels;

(iii) in the case of medical benefits, future medical costs, including, where material, the cost of administering claims and benefit payments; and

(iv) the expected rate of return on plan assets.

Examples – vested and unvested benefits

Ex 24 **A defined benefit plan provides a lump-sum benefit of CU100 payable immediately after leaving the entity for each year of service.**

A benefit of CU100 is attributed to each year. The present value of the defined benefit obligation is the present value of CU100, multiplied by the number of years of service up to the end of the reporting period.

Because the benefit is payable immediately when the employee leaves the entity, the present value of the defined benefit obligation reflects the date at which the employee is expected to leave. Thus, because of the effect of discounting, it is less than the amounts that would be determined if the employee left at the end of the reporting period.

Ex 25 **A plan provides a monthly pension of 0.2 per cent of final salary for each year of service. The pension is payable from the age of 65.**

An entity attributes to each year of service a benefit equal to the present value, at the expected retirement date, of a monthly pension of 0.2 per cent of the estimated final salary payable from the expected retirement date until the expected date of death. The present value of the defined benefit obligation is the present value of monthly pension payments of 0.2 per cent of final salary[(3)], multiplied by the number of years of service up to the end of the reporting period. The present value of the defined benefit obligation is discounted because pension payments begin at the age of 65.

Ex 26 **A plan pays a benefit of CU100 for each year of service. The benefits vest after ten years of service.**

A benefit of CU100 is attributed to each year. In each of the first ten years, the present value of the obligation reflects the probability that the employee may not complete ten years of service.

Ex 27 **A plan pays a lump-sum benefit of CU1,000 that vests and is paid after ten years of service. The plan provides no further benefit for subsequent service.**

A benefit of CU100 (CU1,000 divided by ten) is attributed to each of the first ten years of service. The present value of the defined benefit obligation is the present value of CU100, multiplied by the number of years of service up to the end of the reporting period. The present value of the obligation reflects the probability that the employee may not complete ten years of service. No benefit is attributed to subsequent years.

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(3) If the employee leaves the entity before his 65th birthday his final salary is the salary at the date of leaving the entity. The pension would be paid to the employee from age 65.

Ex 28 **A plan pays a lump-sum retirement benefit of CU2,000 to all employees who are still employed at the age of 55 after twenty years of continuous 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 CU100 (CU2,000 divided by 20) to each year from the age of 35 to the age of 55.

The benefit does not apply to an employee who joins after the age of 35. For all qualifying employees, the present value of the obligation reflects the probability that the employee may not complete the necessary period of service.

Ex 29 **Employees are entitled to a benefit of 3 per cent of final salary for each year of service before the age of 55.**

Benefit of 3 per cent 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.

Discounting

28.17 An entity shall measure its defined benefit obligation on a discounted **present value** basis. The entity shall determine the rate used to discount the future payments by reference to market yields at the reporting date on high quality corporate bonds. In countries with no deep market in such bonds, the entity shall use the market yields (at the reporting date) on government bonds. The currency and term of the corporate bonds or government bonds shall be consistent with the currency and estimated period of the future payments.

Notes

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.

Actuarial valuation method

28.18 If an entity is able, without undue cost or effort, to use the **projected unit credit method** to measure its defined benefit obligation and the related expense, it shall do so. If defined benefits are based on future salaries, the projected unit credit method requires an entity to measure its defined benefit obligations on a basis that reflects estimated future salary increases. Additionally, the projected unit credit method requires an entity to make various actuarial assumptions in measuring the defined benefit obligation, including discount rates, the expected rates of return on plan assets, expected rates of salary increases, employee turnover, mortality, and (for defined benefit medical plans) medical cost trend rates.

Notes

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

Example – projected unit cost method

Ex 30 **A lump-sum benefit is payable on termination of service and equal to 1 per cent of final salary for each year of service. The salary in year 1 is CU10,000 and is assumed to increase at 7 per cent (compound) each year. The discount rate used is 10 per cent per year. 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.

Year	*1*	*2*	*3*	*4*	*5*
Benefit attributed to:					
– prior years	–	131.08	262.16	393.24	524.32
– current year (1% × final salary)[(a)]	131.08	131.08	131.08	131.08	131.08
– current and prior years[(b)]	**131.08**	**262.16**	**393.24**	**524.32**	**655.40**
Opening obligation	–	**89.53**	**196.96**	**324.99**	**476.65**
Interest at 10%	–	8.95	19.70	32.50	47.67
Current service cost	89.53	98.48	108.33	119.16	131.08
Closing obligation[(c)]	**89.53**	**196.96**	**324.99**	**476.65**	**655.40**

(a) CU131 = 1% × 13,108 final annual salary (ie CU10,000 salary in year 1 × (1 + 0.07 annual increase)^{4} (ie number of periods from year 2 to year 5)).

(b) The current service cost is the present value of benefit attributed to the current year:

Year 1—CU131.08 × $1/(1.1)^4$ = CU131.08 × 0.683013 = CU89.53

Year 2— CU131.08 × $1/(1.1)^3$ = CU131.08 × 0.751315 = CU98.48

Year 3— CU131.08 × $1/(1.1)^2$ = CU131.08 × 0.826446 = CU 108.33

Year 4— CU131.08 × $1/(1.1)^1$ = CU131.08 × 0.909091= CU119.16

Year 5— CU131.08 × $1/(1.1)^0$ = CU131.08 × 1 = CU131.08.

(c) The closing obligation is the present value of benefit attributed to current and prior years.

Examples – defined benefits based on future salaries

Ex 31 **A plan provides a monthly pension of 0.2 per cent of final salary for each year of service. The pension is payable from the age of 65.**

An entity attributes to each year of service benefit equal to the present value, at the expected retirement date, of a monthly pension of 0.2 per cent of the estimated final salary payable from the expected retirement date until the expected date of death. 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 per cent of final salary, multiplied by the number of years of service up to the end of the reporting period. The current service cost and the present value of the defined benefit obligation are discounted because pension payments begin at the age of 65.

Ex 32 **Employees are entitled to a benefit of 3 per cent of final salary for each year of service before the age of 55.**

Benefit of 3 per cent 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.

28.19 If an entity is not able, without undue cost or effort, to use the projected unit credit method to measure its obligation and cost under defined benefit plans, the entity is permitted to make the following simplifications in measuring its defined benefit obligation with respect to current employees:

(a) ignore estimated future salary increases (ie assume current salaries continue until current employees are expected to begin receiving post-employment benefits);

(b) ignore future service of current employees (ie assume closure of the plan for existing as well as any new employees); and

(c) ignore possible in-service mortality of current employees between the reporting date and the date employees are expected to begin receiving post-employment benefits (ie assume all current employees will receive the post-employment benefits). However, mortality after service (ie life expectancy) will still need to be considered.

An entity that takes advantage of the foregoing measurement simplifications must nonetheless include both vested and unvested benefits in measuring its defined benefit obligation.

Notes

The simplified calculations result in a measure of the obligation similar to what is sometimes called the accumulated benefit obligation (as opposed to the projected benefit obligation).

Examples – simplified defined benefit plan calculations

Ex 33 The facts are the same as in example 30.

Year	*1*	*2*	*3*	*4*	*5*
1% × current salary (increase at 7% per year)[(a)]	100	107	114.49	122.50	131.08
Years service at end of year	1	2	3	4	5
Future value of obligation	**100**	**214**	**343.47**	**490.02**	**655.40**
Discount factor (10%)	0.683013	0.751315	0.826446	0.909091	1
Present value of obligation	**68.30**	**160.78**	**283.86**	**445.47**	**655.40**
Opening obligation	–	**68.30**	**160.78**	**283.86**	**445.47**
Interest (10%)	–	6.83	16.08	28.39	44.55
Current service cost[(b)]	68.30	80.39	94.62	111.37	131.08
Actuarial gain or loss (balancing figure)	–	5.26	12.38	21.85	34.30
Closing obligation[(c)]	**68.30**	**160.78**	**283.86**	**445.47**	**655.40**

(a) 1% × current salary in each year:

Year 1—CU10,000 × 1% = CU100

Year 2— CU10,000 × 1.07 × 1% = CU107

Year 3— CU10,000 × 1.07^2 × 1% = CU114.49

Year 4— CU10,000 × 1.07^3 × 1% = CU122.50

Year 5— CU10,000 × 1.07^4 × 1% = CU131.08.

(b) The current service cost is the present value of benefit attributed to the current year:

Year 1—CU100 × $1/(1.1)^4$ = CU100 × 0.683013 = CU68.30

Year 2— CU107 × $1/(1.1)^3$ = CU107 × 0.751315 = CU80.39

Year 3— CU114.49 × $1/(1.1)^2$ = CU114.49 × 0.826446 = CU94.62

Year 4— CU122.50 × $1/(1.1)^1$ = CU122.50 × 0.909091= CU111.37

Year 5— CU131.08 × $1/(1.1)^0$ = CU131.08 × 1 = CU131.08.

(c) The closing obligation is the present value of benefit attributed to current and prior years:

Year 1—CU100 × 1 year's service × $1/(1.1)^4$ = CU68.30

Year 2— CU107 × 2 years' service × $1/(1.1)^3$ = CU160.78

Year 3— CU114.49 × 3 years' service × $1/(1.1)^2$ = CU283.86

Year 4— CU122.50 × 4 years' service × $1/(1.1)^1$ = CU445.47

Year 5— CU131.08 × 5 years' service × $1/(1.1)^0$ = CU655.40.

Ex 34 **The facts are the same as in example 31 (ie a plan provides a monthly pension of 0.2 per cent of final salary for each year of service. The pension is payable from the age of 65).**

In accordance with measurement simplifications an entity that is not able, without undue cost or effort, to use the projected unit credit method is permitted to measure its defined benefit obligation as follows—present value of the estimated monthly pension payments calculated at 0.2 per cent of current salary multiplied by the number of years of service up to the end of the reporting period and assuming all current employees will receive the benefit.

The present value of the defined benefit obligation is discounted because pension payments begin at the age of 65.

28.20 This IFRS does not require an entity to engage an independent actuary to perform the comprehensive actuarial valuation needed to calculate its defined benefit obligation. Nor does it require that a comprehensive actuarial valuation must be done annually. In the periods between comprehensive actuarial valuations, if the principal actuarial assumptions have not changed significantly the defined benefit obligation can be measured by adjusting the prior period measurement for changes in employee demographics such as number of employees and salary levels.

Plan introductions, changes, curtailments and settlements

28.21 If a defined benefit plan has been introduced or changed in the current period, the entity shall increase or decrease its defined benefit liability to reflect the change, and shall recognise the increase (decrease) as an expense (income) in measuring profit or loss in the current period. Conversely, if a plan has been curtailed (ie benefits or group of covered employees are reduced) or settled (the employer’s obligation is completely discharged) in the current period, the defined benefit obligation shall be decreased or eliminated, and the entity shall recognise the resulting gain or loss in profit or loss in the current period.

Example – curtailment

Ex 35 **An entity discontinues one of its businesses and employees of the discontinued business 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 CU1,000 and plan assets with a fair value of CU820. The curtailment reduces the net present value of the obligation by CU100 to CU900.**

The effect of the curtailment is as follows:

	Before curtailment	*Curtailment gain*	*After curtailment*
	CU	*CU*	*CU*
Net present value of obligation	1,000	(100)	900
Fair value of plan assets	(820)	-	(820)
Net liability recognised in statement of financial position	180	(100)	80

The entity could account for the curtailment of its employee benefit obligation as follows:

Dr	Post-employment benefit (defined benefit plans) – liability	CU100	
	Cr Profit or loss		CU100

To recognise the curtailment of defined benefit plans caused by the discontinuity of a business.

Defined benefit plan asset

28.22 If the present value of the defined benefit obligation at the reporting date is less than the fair value of plan assets at that date, the plan has a surplus. An entity shall recognise a plan surplus as a defined benefit plan asset only to the extent that it is able to recover the surplus either through reduced contributions in the future or through refunds from the plan.

Examples – defined benefit plan surplus

Ex 36 **At 31 December 20X1 an entity's defined benefit plan has the following characteristics:**

Present value of the obligation	CU1,000
Fair value of plan assets	CU1,200
Excess plan assets	CU200

At 31 December 20X1 the present value of future refunds and reductions in future contributions available to the entity is CU200.

The entity must present the defined benefit plan surplus as a CU200 defined benefit plan asset in its statement of financial position at 31 December 20X1.

Ex 37 **The facts are the same as in example 36. However, in this example, at 31 December 20X1 the present value of future refunds and reductions in future contributions available to the entity is nil.**

The entity must measure the defined benefit plan surplus at nil (defined benefit plan asset) in its statement of financial position as at 31 December 20X1.

Ex 38 **The facts are the same as in example 36. However, in this example, at 31 December 20X1 the present value of future refunds and reductions in future contributions available to the entity is CU80.**

The entity must present the defined benefit plan surplus at CU80 (defined benefit plan asset) in its statement of financial position at 31 December 20X1.

Cost of a defined benefit plan

28.23 An entity shall recognise the net change in its defined benefit liability during the period, other than a change attributable to benefits paid to employees during the period or to contributions from the employer, as the cost of its defined benefit plans during the period. That cost is recognised either entirely in profit or loss as an expense or partly in profit or loss and partly as an item of other comprehensive income (see paragraph 28.24) unless another section of this IFRS requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

Examples – recognition of the cost of a defined benefit plan

Ex 39 **An entity that recognises actuarial gains and losses in profit or loss provides its employees with a monthly pension of 0.2 per cent of final salary for each year of service. The pension is payable from the age of 65. The plan is unfunded.**

At 31 December 20X1 the entity determined the carrying amount of the plan obligation at CU1,000,000 (20X0: CU900,000).

In 20X1 the entity paid pensions of CU40,000 to its past employees.

The entity must recognise an expense of CU140,000 (ie CU1,000,000 closing obligation + CU40,000 pensions paid in 20X1 less CU900,000 opening obligation) in profit or loss for the year ended 31 December 20X1.

Defined benefit plan obligation account

			01/01/20X1	Opening balance	CU900,000
20X1	Pensions paid	CU40,000			
31/12/20X1	Closing balance	CU1,000,000	20X1	Profit or loss (or assets—see paragraph 28.23)	CU140,000 [(a)]
		CU1,040,000			CU1,040,000
			01/01/20X2	Opening balance	CU1,000,000

(a) balancing figure

Ex 40 **The facts are the same as in example 39. However, in this example, the entity's obligations for the defined benefit scheme are funded. Furthermore, in 20X1 the fund paid pensions of CU40,000 to its past employees and the entity contributed CU110,000 to the fund.**

At 31 December 20X1 the entity appropriately determined the fair value of the plan assets at CU980,000 (20X0: CU890,000).

The entity must recognise an expense of CU120,000 (ie CU20,000 closing obligation + CU110,000 increased funding by the entity in 20X1 less CU10,000 opening obligation) in profit or loss for the year ended 31 December 20X1.

Funded defined benefit plan account

			01/01/20X1	Opening balance	CU10,000 [(a)]
20X1	Increase funding	CU110,000			
31/12/20X1	Closing balance	CU20,000 [(b)]	20X1	Profit or loss (or assets—see paragraph 28.23)	CU120,000 [(c)]
		CU130,000			CU130,000
			01/01/20X2	Opening balance	CU20,000

[(a)] CU900,000 obligation less CU890,000 plan assets

[(b)] CU1,000,000 obligation less CU980,000 plan assets

[(c)] balancing figure

Ex 41 **The facts are the same as in example 39. However, in this example, CU10,000 of the cost of the defined benefit plan is attributable to the cost of producing inventories in the period that were in the entity's inventories at 31 December 20X1.**

The entity must recognise a defined benefit plan expense of CU130,000 in profit or loss for the year (ie CU140,000 calculated in example 39 less CU10,000 included in the cost of inventories at 31 December 20X1).

In accordance with paragraphs 13.20 and 13.21 the CU10,000 included in the cost of inventories will be included in profit or loss when the inventories are sold or impaired.

Recognition–accounting policy election

28.24 An entity is required to recognise all actuarial gains and losses in the period in which they occur. An entity shall:

(a) recognise all actuarial gains and losses in profit or loss, or

(b) recognise all actuarial gains and losses in other comprehensive income

as an accounting policy election. The entity shall apply its chosen accounting policy consistently to all of its defined benefit plans and all of its actuarial gains and losses. Actuarial gains and losses recognised in other comprehensive income shall be presented in the statement of comprehensive income.

Notes

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.

Consistently with other changes in accounting estimates (see Section 10 *Accounting Policies, Estimates and Errors*) actuarial gains and losses are included in comprehensive income of the period in which the actuarial assumptions are changed (ie the changes in

actuarial assumptions result from events before the reporting date that resolve a past estimate (experience adjustments) or from changes in the estimated cost of employee service before the reporting date).

Example – accounting policy choice

Ex 42 **The facts are the same as in example 39 (ie the cost of the defined benefit plan for the year ended 31 December 20X1 is CU140,000). However, in this example the entity recognises all actuarial gains and losses in other comprehensive income (see paragraph 28.24(b)). CU50,000 of the cost of the defined benefit plan for the year ended 31 December 20X1 is attributable to actuarial losses.**

The entity must recognise an expense of CU140,000 (ie CU1,000,000 closing obligation + CU40,000 pensions paid in 20X1 less CU900,000 opening obligation) as follows:

- CU50,000 in other comprehensive income for the year ended 31 December 20X1 (ie the portion of the cost that is attributable to actuarial gains and losses); and
- CU90,000 in profit or loss for the year ended 31 December 20X1 (ie CU140,000 total cost less CU50,000 recognised in other comprehensive income).

Defined benefit plan obligation account

			01/01/20X1	Opening balance	CU900,000
20X1	Pensions paid	CU40,000	20X1	Other comprehensive income (actuarial losses)	CU50,000
31/12/20X1	Closing balance	CU1,000,000	20X1	Profit or loss (or assets—see paragraph 28.23)	CU90,000 [a]
		CU1,040,000			CU1,040,000
			01/01/20X2	Opening balance	CU1,000,000

[a] balancing figure

Note: Example 39 illustrates the accounting by an entity that elects to account for actuarial gains and losses in profit or loss (ie in accordance with paragraph 28.24(a)).

28.25 The net change in the defined benefit liability that is recognised as the cost of a defined benefit plan includes:

(a) the change in the defined benefit liability arising from employee service rendered during the reporting period.

(b) interest on the defined benefit obligation during the reporting period.

(c) the returns on any plan assets and the net change in the fair value of recognised reimbursement rights (see paragraph 28.28) during the reporting period.

(d) actuarial gains and losses arising in the reporting period.

(e) increases or decreases in the defined benefit liability resulting from introducing a new plan or changing an existing plan in the reporting period (see paragraph 28.21).

(f) decreases in the defined benefit liability resulting from curtailing or settling an existing plan in the reporting period (see paragraph 28.21).

Example – components of the net change in the defined benefit liability

Ex 43 **The following information is given about a funded defined benefit plan. To keep interest computations simple, all transactions are assumed to be made at the year-end. The present value of the obligation and the fair value of the plan assets were both CU1,000 at 1 January 20X1.**

	20X1	*20X2*	*20X3*
Discount rate at start of year	10.0%	9.0%	8.0%
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

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 CU50 for vested benefits and CU30 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 entity has adopted a policy of recognising actuarial gains and losses in profit or loss (see paragraph 28.24(a)).

Changes in the present value of the obligation and in the fair value of the plan assets are used to determine the amount of the actuarial gains or losses for the period as follows:

	20X1	*20X2*	*20X3*
Present value of obligation, 1 January	1,000	1,141	1,197
Interest cost	100 [(a)]	103 [(b)]	96 [(c)]
Current service cost	130	140	150
Increases resulting from changing an existing plan			
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	**1,141**	**1,197**	**1,295**
Fair value of plan assets, 1 January	1,000	1,092	1,109
Return on plan assets	152 [(d)]	97 [(e)]	64 [(f)]
Contributions	90	100	110
Benefits paid	(150)	(180)	(190)
Fair value of plan assets, 31 December	**1,092**	**1,109**	**1,093**

(a) CU1,000 present value of obligation at 31 December 20X0 × 10%.

(b) CU1,141 present value of obligation at 31 December 20X1 × 9%.

(c) CU1,197 present value of obligation at 31 December 20X2 × 8%.

(d) CU1,092 fair value of plan assets at 31 December 20X1 + CU150 benefits paid less CU90 contributions received less CU1,000 fair value of plan assets at 31 December 20X0.

(e) CU1,109 fair value of plan assets at 31 December 20X2 + CU180 benefits paid less CU100 contributions received less CU1,092 fair value of plan assets at 31 December 20X1.

(f) CU1,093 fair value of plan assets at 31 December 20X3 + CU190 benefits paid less CU110 contributions received less CU1,109 fair value of plan assets at 31 December 20X2.

The amount to be recognised in profit or loss is determined as follows:

	20X1	*20X2*	*20X3*
Current service cost	130	140	150
Interest cost	100	103	96
Return on plan assets	(152)	(97)	(64)
Actuarial (gain) loss recognised in year	61	(87)	42
Past service cost—non-vested benefits	–	30	–
Past service cost—vested benefits	–	50	–
Staff cost for the year ended 31 December 20X1—recognised as an expense in profit or loss or as part of assets (see paragraphs 28.3(b) and 28.23)	**139**	**139**	**224**

28.26 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 yet vested). Employee service before the vesting date gives rise to a constructive obligation because, at each successive reporting 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 vesting requirements. Similarly, although some post-employment benefits (such as post-employment medical benefits) become payable only if a specified event occurs when an employee is no longer employed (such as an illness), 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 – vesting conditions

See examples 26–28.

28.27 If defined benefits are reduced for amounts that will be paid to employees under government-sponsored plans, an entity shall measure its defined benefit obligations on a basis that reflects the benefits payable under the government plans, but only if:

(a) those plans were enacted before the reporting date, or

(b) 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.

Reimbursements

28.28 If an entity is virtually certain that another party will reimburse some or all of the expenditure required to settle a defined benefit obligation, the entity shall recognise its right to reimbursement as a separate asset. The entity shall measure the asset at fair value. In the statement of comprehensive income (or in the income statement, if presented), the expense relating to a defined benefit plan may be presented net of the amount recognised for a reimbursement.

Other long-term employee benefits

28.29 Other long-term employee benefits include, for example:

(a) long-term compensated absences such as long-service or sabbatical leave.

(b) 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.

(e) deferred compensation paid twelve months or more after the end of the period in which it is earned.

Examples – other long-term employee benefits

Ex 44 **An entity's employees are each entitled to five working days of paid sick leave for each year. Unused sick leave may be carried forward for three calendar years.**

The sick leave is accounted for as other long-term employee benefits. The sick leave is not a short-term employee benefit as the paid absence is not expected to occur wholly within 12 months after the end of the period in which the employees render the related employee service.

Ex 45 **A profit-sharing plan requires an entity to pay a specified proportion of its cumulative profit for a five-year period to employees who serve throughout the five-year period.**

The profit-sharing plan is accounted for as other long-term employee benefits.
The profit-sharing plan is not a short-term employee benefit as the profit share is not due wholly within 12 months after the end of the period in which the employees render the

related employee service. Even in the fifth year of the five-year period of the profit-sharing plan it is accounted for as other long-term employee benefits.

Ex 46 **An entity's expatriate employees are each entitled to 30 working days' expatriate leave for each three-year period of continuous employment with the entity. Unused expatriate leave may be carried forward for three calendar years.**

The expatriate leave is accounted for as other long-term employee benefits. It is not a short-term employee benefit as the paid absence is not expected to occur wholly within 12 months after the end of the period in which the employees render the related employee service.

28.30 An entity shall recognise a liability for other long-term employee benefits measured at the net total of the following amounts:

(a) the present value of the benefit obligation at the reporting date, minus

(b) the fair value at the reporting date of plan assets (if any) out of which the obligations are to be settled directly.

An entity shall recognise the change in the liability in accordance with paragraph 28.23.

Examples – measurement

Ex 47 **An entity's employees are each entitled to five working days of paid sick leave for each year of service. Unused sick leave may be carried forward for two calendar years. Sick leave is taken first out of any balance brought forward from the previous years and then out of the current year's entitlement (a FIFO basis).**

On average the entity expects that sick leave will be taken approximately halfway through the year.

At 31 December 20X1 the appropriate discount rates (see paragraph 28.17) are 5 per cent for a six-month period, 14 per cent for an 18-month period and 18 per cent for a 24-month period.

At 31 December 20X1 the entity's sick leave records were as follows:

Employee	*Wage rate (per working day in 20X1)*	*Accumulated sick leave days due on 31/12/20X1*	*Expected days sick leave to be taken in 20X2*	*Expected days sick leave to be taken in 20X3*	*Expected percentage wage increase effective 1 January each year*
1	CU400	9	4	4	5%
2	CU310	6	5	5	2%
3	CU250	0	8	8	2%
4	CU180	1	6	5	8%

At 31 December 20X1 the entity's liability for sick leave is CU5,121 (ie CU3,147 for employee 1 + CU1,789 for employee 2 + CU185 for employee 4), as calculated below:

- Employee 1 (expected sick leave to be taken in 20X2): CU400 20X1 wage rate per working day × 1.05 salary increase × 4 expected days' sick leave in 20X2, accumulated at 31 December 20X1 = CU1,680. CU1,680 ÷ 1.05 discount factor = CU1,600.
- Employee 1 (expected sick leave to be taken in 20X3): CU400 20X1 wage rate per working day × 1.1025 salary increase × 4 expected days' sick leave in 20X3, accumulated at 31 December 20X1 = CU1,764. CU1,764 ÷ 1.14 discount factor = CU1,547.
- Employee 2 (expected sick leave to be taken in 20X2): CU310 20X1 wage rate per working day × 1.02 salary increase × 5 expected days' sick leave in 20X2, accumulated at 31 December 20X1 = CU1,581. CU1,581 ÷ 1.05 discount factor = CU1,506.
- Employee 2 (expected sick leave to be taken in 20X3): CU310 20X1 wage rate per working day × 1.0404 salary increase × 1 expected day's sick leave in 20X3, accumulated at 31 December 20X1 = CU323. CU323 ÷ 1.14 discount factor = CU283.
- Employee 3: CU0, as the employee has no sick leave days accumulated at 31 December 20X1.
- Employee 4 (expected sick leave to be taken in 20X2): CU180 20X1 wage rate per working day × 1.08 salary increase × 1 expected day's sick leave in 20X2, accumulated at 31 December 20X1 = CU194. CU194 ÷ 1.05 discount factor = CU185.

Ex 48 **The facts are the same as in example 47. However, in this example, the employee receives payment from the entity for sick leave that is not taken within 24 months after the end of the period in which the employees render the related service.**

At 31 December 20X1 the entity's liability for sick leave is CU5,495 (ie CU3,521 for employee 1 + CU1,789 for employee 2 + CU185 for employee 4) , as calculated below:

- Employee 1 (expected sick leave to be taken in 20X2): CU400 20X1 wage rate per working day × 1.05 salary increase × 4 expected days' sick leave in 20X2, accumulated at 31 December 20X1 = CU1,680. CU1,680 ÷ 1.05 discount factor = CU1,600.
- Employee 1 (expected sick leave to be taken in 20X3): CU400 20X1 wage rate per working day × 1.1025 salary increase × 4 expected days' sick leave in 20X3, accumulated at 31 December 20X1 = CU1,764. CU1,764 ÷ 1.14 discount factor = CU1,547.
- Employee 1 (expected payout on 31 December 20X3 for sick leave not taken): CU400 20X1 wage rate per working day × 1.1025 salary increase × 1 expected day's sick leave earned in 20X1 and paid out on 31 December 20X3 = CU441. CU441 ÷ 1.18 discount factor = CU374.
- Employee 2 (expected sick leave to be taken in 20X2): CU310 20X1 wage rate per working day × 1.02 salary increase × 5 expected days' sick leave in 20X2, accumulated at 31 December 20X1 = CU1,581. CU1,581 ÷ 1.05 discount factor = CU1,506.
- Employee 2 (expected sick leave to be taken in 20X3): CU310 20X1 wage rate per working day × 1.0404 salary increase × 1 expected day's sick leave in 20X3, accumulated at 31 December 20X1 = CU323. CU323 ÷ 1.14 discount factor = CU283.

- Employee 3: CU0, as the employee has no sick leave days accumulated at 31 December 20X1.
- Employee 4 (expected sick leave to be taken in 20X2): CU180 20X1 wage rate per working day × 1.08 salary increase × 1 expected day's sick leave in 20X2, accumulated at 31 December 20X1 = CU194. CU194 ÷ 1.05 discount factor = CU185.

Termination benefits

28.31 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.

Examples – termination benefits

Ex 49 **In December 20X1 an entity made a public announcement of its commitment to a plan for the closure, on 1 March 20X2, of one of its retail outlets. By publicly announcing its decision to close the retail outlet the entity is legally obliged to pay retrenchment benefits of CU2 million to the employees of the retail outlet.**

At 31 December 20X1 the retailer has a present legal obligation to pay termination benefits of CU2 million to the employees to be retrenched upon the closure of the retail outlet.

Ex 50 **The facts are the same as in example 49. However, in this example, the entity does not have a legal obligation to pay termination benefits to the employees of the retail outlet. However, the entity agreed with its employees' labour union to make a settlement payment of CU2 million to the employees to be retrenched on closure of the retail outlet.**

At 31 December 20X1 the retailer has a present constructive obligation to pay termination benefits of CU2 million to the employees to be retrenched upon the closure of the retail outlet.

Ex 51 **In December 20X1 with a view to reducing its workforce by 10 per cent an entity made an irrevocable offer to its employees of a voluntary redundancy package. In accordance with the offer the entity will compensate the first 10 per cent of employees who accepts voluntary redundancy on or before 31 March 20X2. The compensation offered is equal to the employee's annual salary.**

At 31 December 20X1 the entity has a present obligation to pay termination benefits to the first 10 per cent of employees who accept voluntary redundancy by 31 March 20X2. The number of employees who will volunteer for the redundancy package and each of the group's salary bands are estimated (see paragraph 28.36).

Recognition

28.32 Because termination benefits do not provide an entity with future economic benefits, an entity shall recognise them as an expense in profit or loss immediately.

Examples – recognition of termination benefits

Ex 52 **The facts are the same as in example 49.**

The retailer must recognise CU2 million expense in profit or loss for the year ended 31 December 20X1. Furthermore, at 31 December 20X1 the entity must recognise a liability to pay termination benefits to the employees to be retrenched upon the closure of the retail

The retailer could recognise the transactions as follows.

31 December 20X1

Dr Profit or loss	CU2,000,000	
Cr Termination benefits		CU2,000,000

To recognise the obligation for termination benefits arising from the commitment to close a retail outlet.

Ex 53 **The facts are the same as in example 50.**

The retailer must recognise CU2 million expense in profit or loss for the year ended 31 December 20X1. Furthermore, at 31 December 20X1 the entity must recognise a liability to pay termination benefits to the employees to be retrenched upon the closure of the retail outlet.

The retailer could recognise the transactions as follows.

31 December 20X1

Dr Profit or loss	CU2,000,000	
Cr Termination benefits		CU2,000,000

To recognise the obligation for termination benefits arising from the commitment to close a retail outlet.

Ex 54 **The facts are the same as in example 51.**

The entity must recognise an expense in profit or loss for the year ended 31 December 20X1 at the best estimate of the expenditure that would be required to settle the obligation at the reporting date (ie based on the number of employees expected to accept the voluntary redundancy offer (see paragraph 28.36)). Furthermore, at 31 December 20X1 the entity must recognise a liability to pay the termination benefits to the employees.

28.33 When an entity recognises termination benefits, the entity may also have to account for a curtailment of retirement benefits *[Refer: Paragraph 28.21]* or other employee benefits.

28.34 An entity shall recognise termination benefits as a liability and an expense only when the entity is demonstrably committed either:

(a) to terminate the employment of an employee or group of employees before the normal retirement date, or

(b) to provide termination benefits as a result of an offer made in order to encourage voluntary redundancy.

28.35 An entity is demonstrably committed to a termination only when the entity has a detailed formal plan for the termination and is without realistic possibility of withdrawal from the plan.

Notes

In the absence of more detailed guidance about what constitutes a detailed formal plan (albeit in the context of a restructuring) see example 3 in the Appendix to Section 21 *Provisions and Contingencies*. In the absence of more detailed guidance about what constitutes 'without realistic possibility of withdrawal from the plan' (albeit in the context of a provision) see examples 6 and 7 in the Appendix to Section 21.

For more detailed guidance on when an entity becomes demonstrably committed to a termination an entity can (but need not do so) look to full IFRSs—paragraph 134 of IAS 19 specifies that for the entity to be demonstrably committed to a termination the detailed plan for the termination should 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.

Measurement

28.36 An entity shall measure termination benefits at the best estimate of the expenditure that would be required to settle the obligation at the reporting date. 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.

Examples – measurement of termination benefits

Ex 55 **In December 20X1 an entity made a public announcement of its commitment to a plan for the closure, on 1 March 20X2, of one of its retail outlets. By publicly announcing its decision to close the retail outlet the entity is legally obliged to pay retrenchment benefits to the employees of the retail outlet. Law in the jurisdiction in which the retail outlet is situated requires termination benefits equal to three**

months' wages to be paid to each employee made redundant. However, the entity's practice is to pay significantly more than what is legally required. In December 20X1 the entity entered into negotiations with the employees' trade union to determine the amount to be paid to the employees to be made redundant. At 31 December 20X1 management's best estimate of the amount of termination benefits to be paid on 31 March 20X2 is CU3 million.

At 31 December 20X1 the retailer has a present obligation to pay termination benefits to the employees of its retail unit to be closed. The entity must recognise that obligation as a liability and expense (in profit or loss) at CU3 milllion (ie management's best estimate of the expenditure that would be required to settle the obligation at 31 December 20X1).

Ex 56 **The facts are the same as in example 51.**

The entity must recognise an expense in profit or loss for the year ended 31 December 20X1 at the best estimate of the expenditure that would be required to settle the obligation at the reporting date (ie based on the number of employees expected to accept the voluntary redundancy offer (see paragraph 28.36)). Furthermore, at 31 December 20X1 the entity must recognise a liability to pay that termination benefits to the employees.

28.37 When termination benefits are due more than twelve months after the end of the reporting period, they shall be measured at their discounted present value.

Example – discounting

Ex 57 **The facts are the same as in example 55. However, in this example, the entity expects to pay the termination benefits on 30 June 20X3.**

An appropriate discount factor is 16 per cent for the 18-month period ending 30 June 20X3.

The entity must recognise an expense of CU2,586,207 (ie CU3,000,000 best estimate of the expenditure required to settle the obligation at the reporting date ÷ 1.16 discount factor) in profit or loss for the year ended 31 December 20X1. Furthermore, at 31 December 20X1 the entity must recognise a CU2,586,207 liability to pay termination benefits to the employees.

Group plans

28.38 If a **parent** entity provides benefits to the employees of one or more **subsidiaries** in the group, and the parent presents consolidated financial statements using either the *IFRS for SMEs* or **full IFRSs**, such subsidiaries are permitted to recognise and measure employee benefit expense on the basis of a reasonable allocation of the expense recognised for the group.

Disclosures

Disclosures about short-term employee benefits

28.39 This section does not require specific disclosures about short-term employee benefits.

Notes

The disclosure requirements of other sections of the *IFRS for SMEs* may apply to short-term employee benefits. For example, paragraph 33.6 requires disclosure of short-term employee benefits of the entity's key management personnel.

Disclosures about defined contribution plans

28.40 An entity shall disclose the amount recognised in profit or loss as an expense for defined contribution plans. If an entity treats a defined benefit multi-employer plan as a defined contribution plan because sufficient information is not available to use defined benefit accounting (see paragraph 28.11) it shall disclose the fact that it is a defined benefit plan and the reason why it is being accounted for as a defined contribution plan, along with any available information about the plan's surplus or deficit and the implications, if any, for the entity.

Example – disclosures about defined contribution plans

Ex 58 **An entity could disclose its defined contribution expense in the notes to its financial statements as follows:**

SME A

Notes to the financial statements for the year ended 31 December 20X1

Note 7 Profit before tax

The following items have been recognised as expenses (income) in determining profit before tax:

	20X1	*20X0*
	CU	*CU*
Cost of defined contribution plans	20,000	19,000
…		

Disclosures about defined benefit plans

28.41 An entity shall disclose the following information about defined benefit plans (except for any defined multi-employer benefit plans that are accounted for as a defined contribution plans in accordance with paragraph 28.11, for which the disclosures in paragraph 28.40 apply instead). If an entity has more than one defined benefit plan, these disclosures may be made in total, separately for each plan, or in such groupings as are considered to

be the most useful:

(a) a general description of the type of plan, including funding policy.

(b) the entity's accounting policy for recognising actuarial gains and losses (either in profit or loss or as an item of other comprehensive income) and the amount of actuarial gains and losses recognised during the period.

(c) a narrative explanation if the entity uses any of the simplifications in paragraph 28.19 in measuring its defined benefit obligation.

(d) the date of the most recent comprehensive actuarial valuation and, if it was not as of the reporting date, a description of the adjustments that were made to measure the defined benefit obligation at the reporting date.

(e) a reconciliation of opening and closing balances of the defined benefit obligation showing separately benefits paid and all other changes.

(f) a reconciliation of the opening and closing balances of the fair value of plan assets and of the opening and closing balances of any reimbursement right recognised as an asset, showing separately, if applicable:

  (i) contributions;

  (ii) benefits paid; and

  (iii) other changes in plan assets.

(g) the total cost relating to defined benefit plans for the period, disclosing separately the amounts

  (i) recognised in profit or loss as an expense, and

  (ii) included in the cost of an asset.

(h) for each major class of plan assets, which shall include, but is not limited to, equity instruments, debt instruments, property, and all other assets, the percentage or amount that each major class constitutes of the fair value of the total plan assets at the reporting date.

(i) the amounts included in the fair value of plan assets for:

  (i) each class of the entity's own financial instruments, and

  (ii) any property occupied by, or other assets used by, the entity.

(j) the actual return on plan assets.

(k) the principal actuarial assumptions used, including, when 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 salary increases;

  (iv) medical cost trend rates; and

  (v) any other material actuarial assumptions used.

The reconciliations in (e) and (f) above need not be presented for prior periods. A subsidiary that recognises and measures employee benefit expense on the basis of a reasonable allocation of the expense recognised for the group (see paragraph 28.38) shall, in its separate financial statements, describe its policy for making the allocation and shall make the disclosures in (a)–(k) above for the plan as a whole.

Example – disclosures about defined benefit plans

Ex 59 **An entity could disclose its defined benefit plans in its financial statements as follows:**

Extract from an entity's statement of financial position at 31 December 20X2

All amounts are presented in currency units 'CU'

	Note	*20X2*	*20X1*
ASSETS			
…			
Net defined benefit plan assets	18	-	90
…			
LIABILITIES			
…			
Net obligations under defined benefit plans	18	11,217	7,615
…			

Extract from an entity's notes to the financial statements for the year ended 31 December 20X2

All amounts are presented in currency units 'CU'

Note 1 Accounting policies

Employee benefits—defined benefit post-employment plans

The group has obligations to its employees and former employees to provide pensions in accordance with its defined benefit final salary pension schemes. The terms of the schemes oblige the group to provide employees with a pension equal to 1.5 per cent of the employee's final salary for every year of service provided. The defined benefit pension plans are partly funded by the entity through payments to separate legal entities set up for the sole purpose of paying pensions to the group's employees.

The group is also obliged to reimburse 10 per cent of its employee's post-employment medical costs if the employee has provided 20 years or more of service to the group. The group does not fund this obligation in advance.

The group measures defined benefit liabilities (assets) at the present value of its obligations under defined benefit plans at the reporting date minus the fair value at the reporting date of plan assets out of which the obligations are to be settled directly. The obligations under defined benefit plans are determined using the projected unit credit method. Actuarial gains and losses are recognised in profit or loss in the period in which they occur.

Note 18 Net obligations under defined benefit plans

	20X2	*20X1*
…		
Post-employment plans—defined benefit plans	CU11,217	CU7,525
presented as a liability	CU11,217	CU7,615
presented as an asset	–	(90)
…		

Post-employment plans—defined benefits plans

	Defined benefit pension plans		*Post-employment medical benefits*	
	20X2	*20X1*	*20X2*	*20X1*
Present value of funded obligations	22,300	18,400	–	–
Fair value of plan assets	(18,420)	(17,280)	–	–
Present value of unfunded obligations	–	–	7,337	6,405
Net liability	3,880	1,120	7,337	6,405

Amounts in the statement of financial position:

	Defined benefit pension plans		*Post-employment medical benefits*	
	20X2	*20X1*	*20X2*	*20X1*
Liabilities	3,880	1,210	7,337	6,405
Assets	–	(90)	–	–
Net liability	3,880	1,120	7,337	6,405

The most recent comprehensive actuarial valuation was performed at 31 December 20X2.

The pension plan assets include ordinary shares issued by the entity with a fair value of CU317 (20X1: CU281). Plan assets also include property occupied by the entity with a fair value of CU200 (20X1: CU185).

The amounts recognised in profit or loss are as follows:

	20X2	*20X1*
Defined-benefit pension plan expense	3,050	750
Defined-benefit post-employment medical plan expense	479	411
Total defined-benefit plan expense	3,529	1,161

Changes in the present value of the defined benefit obligation are as follows:

	Defined benefit pension plans 20X2	*Post-employment medical benefits 20X2*
Opening defined benefit obligation	18,400	6,405
Service cost	850	479
Interest cost	950	803
Actuarial losses (gains)	2,350	250
Losses (gains) on curtailments	(500)	–
Exchange differences on foreign plans	900	–
Benefits paid	(650)	(600)
Closing defined benefit obligation	22,300	7,337

Changes in the fair value of plan assets of the defined benefit pension plans are as follows:

	20X2
Opening fair value of plan assets	17,280
Actual return on plan assets	600
Assets distributed on settlements	(400)
Contributions by employer	700
Exchange differences on foreign plans	890
Benefits paid	(650)
Closing fair value of plan assets	18,420

The group expects to contribute CU900 to its defined benefit pension plans in 20X3.

The major categories of plan assets as a percentage of total plan assets are as follows:

	20X2	20X1
Jurisdiction A equities	20%	22%
Jurisdiction B equities	16%	15%
Jurisdiction C equities	10%	7%
Jurisdiction A bonds	31%	26%
Jurisdiction B bonds	13%	17%
Jurisdiction C bonds	5%	8%
Property	5%	5%

Principal actuarial assumptions at the end of the reporting period (expressed as weighted averages):

	20X2	20X1
Discount rate at 31 December	5%	6.5%
Future salary increases	5%	4%
Future pension increases	3%	2%
Proportion of employees opting for early retirement	30%	30%
Annual increase in healthcare costs	8%	8%
Future changes in maximum state healthcare benefits	3%	2%

Disclosures about other long-term benefits

28.42 For each category of other long-term benefits that an entity provides to its employees, the entity shall disclose the nature of the benefit, the amount of its obligation and the extent of **funding** at the reporting date.

Example– disclosures about other long-term benefits

Ex 60 An entity could disclose its other long-term employee benefits as follows:

Extract from an entity's statement of financial position at 31 December 20X2

All amounts are presented in currency units 'CU'

	Note	*20X2*	*20X1*
LIABILITIES			
Non-current liabilities			
Provision for employee benefits	18	40,000	35,000
…			
Current liabilities			
…			
Provision for employee benefits	18	20,000	15,000
…			

Extract from an entity's notes to the financial statements for the year ended 31 December 20X2

All amounts are presented in currency units 'CU'

Note 18 Provision for employee benefits

	20X2	*20X1*
…		
Other long-term employee benefits	10,623	9,830
…		
Total employee benefits	60,000	50,000

Other long-term employee benefits

The liability for other long-term employee benefits obligations relates to government mandated long-service payments. All full-time members of staff, excluding directors, are covered by the programme. A payment is made of 5 per cent of salary (as determined for the twelve months before the payment) at the end of each of five years of employment. The payment is made as part of the December payroll in the fifth year. The group does not fund this obligation in advance.

The accrual recognised at the year-end is determined on the basis of a present value calculation assuming a 3 per cent average annual salary increase, with employee turnover based on the group's recent experience, discounted using the current market yield for high quality corporate bonds.

At 1 January 20X2	9,830
Additional accrual in year	7,033
Payment made in year	(6,240)
At 31 December 20X2	10,623

	20X2	20X1
Current liability	6,181	5,943
Non-current liability	4,442	3,887
Total	10,623	9,830

Disclosures about termination benefits

28.43 For each category of termination benefits that an entity provides to its employees, the entity shall disclose the nature of the benefit, its accounting policy, and the amount of its obligation and the extent of funding at the reporting date.

28.44 When there is uncertainty about the number of employees who will accept an offer of termination benefits, a contingent liability exists. Section 21 *Provisions and Contingencies* requires an entity to disclose information about its contingent liabilities unless the possibility of an outflow in settlement is remote.

Example – disclosures about termination benefits

Ex 61 An entity could disclose information about its termination benefits as follows:

Extract from an entity's statement of financial position at 31 December 20X2

All amounts are presented in currency units 'CU'

	Note	20X2	20X1
LIABILITIES			
Non-current liabilities			
Provision for employee benefits	18	40,000	35,000
…			
Current liabilities			
…			
Provision for employee benefits	18	20,000	15,000
…			

Extract from an entity's notes to the financial statements
for the year ended 31 December 20X2

All amounts are presented in currency units 'CU'

Note 18 Employee benefits

	20X2	20X1
…		
Termination benefits	6,000	–
…		
Total employee benefits	60,000	50,000

Termination benefits

The liability for termination benefits relates to the offer made by the group to all employees over 55 years of age for voluntary redundancy payments. In accordance with the offer qualifying employees who accept voluntary redundancy on or before 1 June 20X3 will be paid termination benefits equal to one year's salary. The voluntary redundancy payments are to be made in July 20X3. The group does not fund this obligation in advance.

The accrual recognised at the year-end is determined on the basis of the estimated number of employees expected to apply for voluntary redundancy in each of the group's salary bands. Salary increases are not anticipated as the group awards salary increases in December of each year. Furthermore, the termination benefits are not measured at a discounted amount as settlement is due in June 20X3.

The maximum possible financial effect of the voluntary redundancy offer that has not been recognised as a liability is CU3,000, as set out in note 30 contingent liabilities.

At 1 January 20X2	–
Accrued in year	8,000
Payment made in year	(2,000)
At 31 December 20X2 (current liability)	6,000

SIGNIFICANT ESTIMATES AND OTHER JUDGEMENTS

Applying the requirements of the *IFRS for SMEs* to transactions and events often requires judgement. Information about significant judgements and key sources of estimation uncertainty are useful in assessing the financial position, performance and cash flows of an entity. Consequently, in accordance with paragraph 8.6, an entity must disclose the judgements that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements. Furthermore, in accordance with paragraph 8.7, an entity must disclose information about the key assumptions concerning the future, and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Other sections of the *IFRS for SMEs* require disclosure of information about particular judgements and estimation uncertainties.

There are five types of employee benefits:

- short-term employee benefits;
- post-employment benefits;
- other long-term employee benefits;
- termination benefits; and
- share-based payments (sometimes referred to as equity compensation benefits).

Share-based payments are accounted for in accordance with the requirements of Section 26. The four types of employee benefits accounted for in accordance with Section 28 have a common general recognition principle. However, each type of employee benefit has unique measurement requirements. Judgements that may be necessary in measuring each type of employee benefit are set under separate headings below.

Short-term employee benefits

The liability for accumulating compensated absences is measured at their expected cost (ie the additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated). In determining the amount that the entity expects to pay, the entity may need to estimate salary increases, estimate the timing of leave relative to salary increases and estimate the extent to which accumulated entitlement will expire unused. In many cases little difficulty is encountered in measuring short-term employee benefits. However, in some cases significant judgement is required in estimating salary increases, the timing of relevant events and the expiry of entitlement to unused accumulated paid absences (eg where experience is limited or trends are not expected to continue).

Post-employment benefits

Post-employment benefit plans are classified as either defined contribution plans or defined benefit plans.

Defined contribution plans

Under defined contribution plans actuarial risk (that benefits will be less than expected) and investment risk (that assets invested will be insufficient to meet expected benefits) are borne by the employee. Consequently, little difficulty is experienced in measuring an entity's liability to make contributions to a defined contribution plan.

Defined benefit plans

Under defined benefit plans actuarial risk (for funded and unfunded plans) and investment risk (for funded plans) are borne by the employer.

An entity measures its defined-benefit liability at the net total of the following amounts:

(a) the present value of the benefit obligation at the reporting date, minus

(b) the fair value at the reporting date of plan assets (if any) out of which the obligations are to be settled directly.

The presence of actuarial risk over many years to expected settlement requires significant judgements in the estimation of actuarial assumptions—an entity's best estimates of the variables that will determine the ultimate cost of providing post-employment benefits. When using the projected unit credit method actuarial assumptions include when relevant:

(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

  (iv) claim rates under medical plans; and

(b) financial assumptions, dealing with items such as:

  (i) the discount rate;

  (ii) future salary and benefit levels; and

  (iii) in the case of medical benefits, future medical costs, including, where material, the cost of administering claims and benefit payments; and

  (iv) the expected rate of return on plan assets.

Less judgement is needed when using the simplified calculations (see paragraph 28.19).

For funded plans, the entity must measure the fair value of the plan assets at each reporting date. When active markets exist for the assets held by the plan little difficulty is experienced in determining the fair value of the plan assets. However, in the absence of active markets significant judgements may be required in estimating the fair value of the plan assets. Mandatory requirements on determining the fair value of financial instruments are set out in Section 11 *Basic Financial Instruments*. In the absence of guidance for estimating the fair value of other types of assets, this guidance should be applied to other plan assets.

Other long-term employee benefits

Other long-term employee benefits are employee benefits (other than post-employment benefits and termination benefits) that are not due wholly within twelve months after the end of the period in which the employees render the related service (eg long-term compensated absences, long-service benefits, long-term disability benefits, profit-sharing and bonuses payable twelve months or more after the end of the period in which the employees render the related service and deferred compensation paid twelve months or more after the end of the period in which it is earned).

An entity measures its liability for other long-term employee benefits at the net total of the following amounts:

(a) the present value of the benefit obligation at the reporting date, minus

(b) the fair value at the reporting date of plan assets (if any) out of which the obligations are to be settled directly.

In many cases little difficulty is encountered in measuring other long-term employee benefits. However, in some cases significant judgement is required in estimating the discount rate applicable, future salary and benefits levels, the timing of relevant events and the expiry of entitlement to unutilised accumulated paid absences (eg where experience is limited or trends are not expected to continue).

For funded plans, the entity must measure the fair value of the plan assets at each reporting date. When active markets exist for the assets held by the plan little difficulty is experienced in determining the fair value of the plan assets. However, in the absence of active markets significant judgements may be required in estimating the fair value of the plan assets. Mandatory requirements on determining the fair value of financial instruments are set out in Section 11 *Basic Financial Instruments*. In the absence of guidance for estimating the fair value of other types of assets, this guidance should be applied to other plan assets.

Termination benefits

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.

An entity measures termination benefits at the best estimate of the expenditure that would be required to settle the obligation at the reporting date. In many cases little difficulty is encountered in measuring termination benefits. However, in some cases significant judgement is required (eg in the case of an offer made to encourage voluntary redundancy, the entity must estimate the number of employees expected to accept the offer). Furthermore when termination benefits are due more than twelve months after the end of the reporting period, the entity must determine the rate at which to discount the expected cash flows to their present value.

Module 28 – Employee Benefits

COMPARISON WITH FULL IFRSs

A high level overview of differences between the requirements as issued at 9 July 2009 of accounting and reporting employee benefits in accordance with the *IFRS for SMEs* (see Section 28 *Employee Benefits*) and full IFRSs (see IAS 19 *Employee Benefits*) is set out below separately for each major type of employee benefit.

Short-term employee benefits

Full IFRSs (see IAS 19 *Employee Benefits* paragraphs 8–16) and the *IFRS for SMEs* (see Section 28 *Employee Benefits* paragraphs 28.3–28.8) share the same principles for the recognition and measurement of short-term employee benefits. However, the *IFRS for SMEs* is drafted in simple language and includes less guidance on how to apply the principles.

Post-employment benefits

Defined contribution plans

Full IFRSs (see IAS 19 *Employee Benefits* paragraphs 43–45) and the *IFRS for SMEs* (see Section 28 *Employee Benefits* paragraph 28.13) as issued at 9 July 2009 share the same principles for the recognition and measurement of defined contribution plan benefits. However, the *IFRS for SMEs* is drafted in simple language and includes significantly less guidance on how to apply the principles.

Defined benefit plans

Full IFRSs (see IAS 19 *Employee Benefits* paragraphs 48–118) and the *IFRS for SMEs* (see Section 28 *Employee Benefits* paragraphs 28.3 and 28.14–28.28) as issued at 9 July 2009 share many of the same principles for the recognition and measurement of defined benefit plans. The main differences between the requirements of accounting and reporting defined benefit plans in accordance with full IFRSs and the *IFRS for SMEs* include:

- The *IFRS for SMEs* is drafted in simple language.
- IAS 19 requires an entity to recognise unvested past service cost as an expense on a straight-line basis over the average period until the benefits become vested. In accordance with the *IFRS for SMEs* an entity is required to recognise past service costs as an expense in measuring profit or loss of the period of the change (ie immediately).
- IAS 19 requires that a defined benefit obligation should always be measured using the projected unit credit actuarial method. For cost-benefit reasons, the *IFRS for SMEs* provides for some measurement simplifications that retain the basic IAS 19 principles but reduce the need for SMEs to engage external specialists. Accordingly, if information based on the projected unit credit method is not available and cannot be obtained without undue cost or effort, SMEs must apply an approach that is based on IAS 19 but does not consider future salary progression, future service or possible mortality during an employee's period of

service. This approach still takes into account life expectancy of employees after retirement age. The resulting defined benefit pension obligation reflects both vested and unvested benefits.

- The *IFRS for SMEs* clarifies that comprehensive valuations would not normally be necessary annually. In the interim periods, the valuations would be rolled forward for aggregate adjustments for employee composition and salaries, but without changing the turnover or mortality assumptions.
- Full IFRSs permit an entity to choose between various methods of recognising actuarial gains and losses. The *IFRS for SMEs* requires the simplest of the methods permitted by IAS 19 (ie immediate recognition of actuarial gains and losses when they occur).
- Full IFRSs require an entity that elects to recognise actuarial gains and losses in other comprehensive income also to recognise in other comprehensive income any adjustments arising from the asset recognition limits for plan surpluses set out in paragraph 58(b) of IAS 19. Although the *IFRS for SMEs* specifies asset recognition limits for plan surpluses (see paragraph 28.22) it does not specify that an entity that elects to recognise actuarial gains and losses in other comprehensive income must also recognise any adjustments arising from the asset recognition limits in other comprehensive income.
- Full IFRSs define actuarial gains and losses and specify their composition. In the context of measuring the present value of an entity's defined benefit obligation the *IFRS for SMEs* describes actuarial assumptions as estimates about demographic variables (such as employee turnover and mortality) and financial variables (such as future increases in salaries and medical costs) that influence the cost of the benefit.
- The disclosure requirements for defined benefit plans in Section 28 are less detailed than those specified in IAS 19.

Other long-term employee benefits

Full IFRSs (see IAS 19 *Employee Benefits* paragraphs 128–130) and the *IFRS for SMEs* (see Section 28 *Employee Benefits* paragraph 28.30) as issued at 9 July 2009 share the same principles for the recognition and measurement of other long-term employee benefits. However, the *IFRS for SMEs* is drafted in simple language and includes less guidance on how to apply the principles.

Termination benefits

Full IFRSs (see IAS 19 *Employee Benefits* paragraphs 133–140) and the *IFRS for SMEs* (see Section 28 *Employee Benefits* paragraphs 28.31–28.37) as issued at 9 July 2009 share the same principles for the recognition and measurement of termination benefits. However, the *IFRS for SMEs* is drafted in simple language and includes less guidance on how to apply the principles.

Module 28 – Employee Benefits

TEST YOUR KNOWLEDGE

Test your knowledge of the requirements for accounting and reporting employee benefits in accordance with the *IFRS for SMEs* by answering the questions below.

Once you have completed the test check your answers against those set out below this test.

Assume all amounts are material.

Mark the box next to the most correct statement.

Question 1

Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees, including directors and management. Section 28 applies to the accounting for four types of employee benefits. It does not apply to the accounting for:

☐ (a) short-term employee benefits.

☐ (b) post-employment benefits.

☐ (c) other long-term employee benefits.

☐ (d) termination benefits.

☐ (e) share-based payments.

Question 2

An entity's employees are each entitled to 20 days of paid holiday leave per calendar year. Unused holiday leave cannot be carried forward and does not vest. The entity's annual reporting date is 31 December.

The holiday leave is:

☐ (a) a short-term employee benefit.

☐ (b) a post-employment benefit.

☐ (c) an other long-term employee benefit.

☐ (d) a termination benefit.

Question 3

Consider the information in Question 2. However, in this question, unused holiday leave is paid on 31 December of each year (ie it vests at the end of each calendar year but does not accumulate).

The holiday leave is:

☐ (a) a short-term employee benefit.

☐ (b) a post-employment benefit.

☐ (c) an other long-term employee benefit.

☐ (d) a termination benefit.

Question 4

Consider the information in Question 2. However, in this question, unused holiday leave may be carried forward for one calendar year (ie it accumulates but does not vest).

The holiday leave is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a post-employment benefit.
- ☐ (c) an other long-term employee benefit.
- ☐ (d) a termination benefit.

Question 5

Consider the information in Question 2. However, in this question, unused holiday leave may be carried forward for two calendar years (ie it accumulates but does not vest).

The holiday leave is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a post-employment benefit.
- ☐ (c) an other long-term employee benefit.
- ☐ (d) a termination benefit.

Question 6

Consider the information in Question 2. However, in this question, unused holiday leave may be carried forward until the employee leaves the employment of the entity, at which time the entity will pay the employee for all unused holiday leave (ie it accumulates and vests).

The holiday leave is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a post-employment benefit.
- ☐ (c) an other long-term employee benefit.
- ☐ (d) a termination benefit.

Question 7

An entity made a public announcement of its commitment to a voluntary redundancy plan. The entity has an obligation to pay employees that choose voluntary redundancy a lump sum equal to twice their gross annual salary.

The obligation to pay employees that choose voluntary redundancy is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a post-employment benefit.
- ☐ (c) an other long-term employee benefit.
- ☐ (d) a termination benefit.

Question 8

An entity reimburses 50 per cent of past employees' post-employment medical costs if the employee provides 25 years of service, or more, to the entity.

The obligation to pay 50 per cent of qualifying past employees' post-employment medical costs is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a defined benefit post-employment benefit.
- ☐ (c) a defined contribution post-employment benefit.
- ☐ (d) an other long-term employee benefit.
- ☐ (e) a termination benefit.

Question 9

A profit-sharing plan requires an entity to pay a specified proportion of its cumulative profit for a five-year period to employees who serve throughout the five-year period.

The profit-sharing plan is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a post-employment benefit.
- ☐ (c) an other long-term employee benefit.
- ☐ (d) a termination benefit.

Question 10

A profit-sharing plan requires an entity to pay a specified proportion of its cumulative profit for the year to employees who served the entity throughout the year.

The profit-sharing plan is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a post-employment benefit.
- ☐ (c) an other long-term employee benefit.
- ☐ (d) a termination benefit.

Question 11

Which of the following best describes the simplified method of calculating a defined benefit obligation permitted by paragraph 28.19?

- ☐ (a) it measures the pension obligation on the basis of the plan formula applied to years of service to date and existing salary levels.
- ☐ (b) it measures the pension obligation on the basis of the plan formula applied to years of service to date and future salary levels.
- ☐ (c) it estimates the total benefit at retirement and then computes the level cost that will be sufficient, together with interest expected to accumulate at the assumed rate, to provide the total benefits at retirement.
- ☐ (d) it measures the pension obligation and pension cost on the basis of the shortest possible period for funding to maximise the tax deduction.

Question 12

An entity that uses the simplified method of calculating a defined benefit obligation is not permitted:

- ☐ (a) to ignore estimated future salary increases (ie assume current salaries continue until current employees are expected to begin receiving post-employment benefits).
- ☐ (b) to ignore future service of current employees (ie assume closure of the plan for existing as well as any new employees).
- ☐ (c) to ignore possible in-service mortality of current employees between the reporting date and the date employees are expected to begin receiving post-employment benefits (ie assume all current employees will receive the post-employment benefits).
- ☐ (d) to ignore possible mortality after service (ie life expectancy).

Module 28 – Employee Benefits

Answers

Q1 (e) see paragraph 28.2
Q2 (a) see paragraph 28.4(b)
Q3 (a) see paragraph 28.4(b)
Q4 (a) see paragraph 28.4(b)
Q5 (c) see paragraph 28.29
Q6 (c) see paragraph 28.29
Q7 (d) see paragraph 28.31
Q8 (b) see paragraphs 28.9 and 28.10(b)
Q9 (c) see paragraph 28.29(d)
Q10 (a) see paragraph 28.4(c)
Q11 (a) see paragraph 28.19
Q12 (d) see paragraph 28.19(c)

APPLY YOUR KNOWLEDGE

Apply your knowledge of the requirements for accounting and reporting employee benefits in accordance with the *IFRS for SMEs* by solving the case studies below.

Once you have completed the case studies check your answers against those set out below this test.

Case study 1

SME A started operations on 31 December 20X1.

Summarised information about its employees at 31 December 20X5 includes:

Employee category	*Number of employees in category*	*Salary level for the 12-month period ending 30/06/20X6*	*Percentage wage increase effective from 01/07/20X6*
A	9	CU100,000	5%
B	200	CU50,000	7%
C	300	CU25,000	9%

Annual salary increases are expected to continue at the same rates for the foreseeable future.

At 31 December 20X5 the appropriate discount factors (determined using the current market yield for high quality corporate bonds in the jurisdiction in which SME A operates) are 0.9524 for a 12-month period, 0.9009 for a 24-month period, 0.8547 for a 36-month period and 0.8 for a 48-month period.

SME A's employees work a five-day week. SME A's operations close for the six mandatory public holidays of the jurisdiction in which SME A operates. Three of the public holidays are before 30 June.

Holiday leave

SME A's employees are each entitled to 20 paid days' holiday leave per year.

Category A employees can carry forward unused holiday leave for one calendar year on a first-in, first-out (FIFO) basis. Holiday leave not taken in the prescribed period is forfeited.

Category B employees cannot carry forward unused holiday leave but are paid for all holiday leave not used in the previous calendar year. The payment is made as part of the January payroll of the following year.

Category C employees cannot carry forward unused holiday leave and are not paid for unused holiday leave.

At 31 December 20X5 the entity's holiday leave records were as follows:

Employee category	*Number of employees in category*	*Average days' holiday leave per employee unused on 31/12/20X5*
A	9	10
B	200	6
C	300	8

At 31 December 20X5 SME A expects 25 days' holiday leave accumulated at 31 December 20X5 by employees in category A to expire unused on 31 December 20X6.

SME A expects that holiday leave will on average be taken evenly throughout the year.

Long-service awards

SME A's employees are entitled to receive government mandated long-service payments from SME A calculated at 5 per cent of salary (as determined for the twelve months before the payment) at the end of each five-year period of continuous employment. The payment is made as part of the December payroll in the fifth year. SME A does not fund this obligation in advance.

Employee turnover is expected to follow average historical patterns. For ease of calculation assume that staff join and leave on 31 December. Furthermore, assume that none of the employees who joined SME A after 1 January 20X2 left or are expected to leave SME A in the foreseeable future (ie all leavers were employed on 31 December 20X1).

At 31 December 20X5 the entity's long-service award records were as follows:

Employee category	*Employee turnover on 31 December 20X5*		*Employee turnover on 31 December 20X4*		*Employee turnover on 31 December 20X3*		*Employee turnover on 31 December 20X2*		*Employed on 31/12/20X1*
	Joined	left	joined	left	joined	left	joined	left	
A	0	0	0	0	0	0	1	1	9
B	10	9	11	10	10	9	9	8	196
C	16	18	15	12	11	16	18	20	306

Pension plan

On 5 January 20X6 SME A paid a contribution of CU100,000 to a defined contribution plan in part exchange for services performed by the entity's employees in December 20X5.

Voluntary redundancy offer

In December 20X5, with a view to reducing its workforce, SME A made an irrevocable offer to its employees of a voluntary redundancy package. In accordance with the offer SME A will compensate any employee who accepts voluntary redundancy on or before 30 June 20X6. The compensation offered is equal to the employee's annualised salary for the 12-month period ending 30 June 20X6.

At 31 December 20X5 SME A's voluntary redundancy records include:

Employee category	*Number of employees who accepted voluntary redundancy by 31/12/20X5*	*Number of employees expected to accept voluntary redundancy in 20X6*
A	0	1
B	2	8
C	5	25

Calculate SME A's liability for employee benefits at 31 December 20X5.

Answer to case study 1

At 31 December 20X5 SME A's liability for employee benefits is CU2,305,228, analysed as follows:

		CU
Short-term employee benefits	see calculation below	261,421
Other long-term employee benefits	see calculation below	593,807
Post-employment benefits—defined contribution plan		100,000
Termination benefits	see calculation below	1,350,000
Provision for employee benefits		**2,305,228**

Short-term employee benefits

At 31 December 20X5 the entity's liability for holiday leave is CU261,421 (ie CU26,127 for category A employees + CU235,294 for category B employees.

Category A: 32.5 days[(a)] × CU392.16[(b)] + 32.5 days[(a)] × CU411.76[(c)] = CU26,127.

Category B: 1,200 days[(e)] × CU196.08[(f)] = CU235,294.

Category C: CU0—non-accumulating and non-vesting.

Other long-term employee benefits

At 31 December 20X5 SME A's liability for long-service awards is CU593,807.

Calculation:

Category A employees CU34,148 (ie CU31,239[(g)] + CU2,909[(h)]) +

Category B employees CU320,000 (ie CU297,534[(i)] + CU10,371[(j)] + CU7,799[(k)] + CU4,296[(l)]) +

Category C employees CU239,659 (ie CU222,321[(m)] + CU10,113[(n)] + CU4,261[(o)] + CU2,964[(p)]).

Termination benefits

Employee category	*Number of employees elected voluntary redundancy by 31/12/20X5*	*Annualised salary for the 12-month period ending 30/06/20X6*	*Termination benefits*
	(A)	*(B)*	*(C) = (A) × (B)*
A	1	CU100,000	CU100,000
B	10	CU50,000	CU500,000
C	30	CU 25,000	CU750,000
			CU1,350,000

The calculations and explanatory notes below do not form part of the answer to this case study:

(a) 9 employees × 10 days' holiday leave accumulated, on average = 90 days accumulated in total. 90 days less 25 days expected saving due to expiration = 65 days. 65 days accumulated holiday leave expected to be taken in 20X6, ie half (or 32.5 days' holiday leave) before 30 June 20X6 and 32.5 days' holiday leave after 1 July 20X6.

(b) CU100,000 annual salary ÷ 255[(d)] working days for the year = CU392.16 salary per working day from

1 January 20X6 to 30 June 20X6.

(c) CU100,000 annual salary + 5% × CU100,000 annual salary = CU105,000 expected annual salary from 1 July 20X6. CU105,000 ÷ 255[(d)] working days for the year = CU411.76 salary per working day from 1 July 20X6 to 31 December 20X6.

(d) 365 days in a year ÷ 7 days per week × 5 working days per week = 261 working days per year. 261 days less 6 public holidays per year = 255 working days for the year.

(e) 200 employees × 6 days' holiday leave vested on average = 1,200 days vested in total. 1,200 days' vested holiday leave.

(f) CU50,000 annual salary ÷ 255[(d)] working days for the year = CU196.08 salary per working day.

(g) Category A employees expected to receive long-service payments in December 20X6: Expected salary for 20X5 CU50,000 (January to June) + CU52,500 (July to December) = CU102,500. 5% × CU102,500 × 8 employees × 4/5 (4 out of 5 years' service performed to date) = CU32,800 expected payment. CU32,800 × 0.9524 discount factor = CU31,239. Note: SME A did not anticipate savings due to category A employees leaving the employment of the entity.

(h) Category A employees expected to receive long-service payments in December 20X7: Expected salary for 20X6 CU52,500 (January to June) + CU55,125 (July to December) = CU107,625. 5% × CU107,625 × 1 employee (ie started service on 31 December 20X2) × 3/5 (ie 3 out of 5 years' service performed to date) = CU3,229 expected payment. CU3,229 × 0.9009 discount factor = CU2,909. Note: SME A did not anticipate savings due to category A employees leaving the employment of the entity.

(i) Category B employees expected to receive long-service payments in December 20X6: Expected salary for 20X5 CU25,000 (January to June) + CU26,750 (July to December) = CU51,750. 5% × CU51,750 × 77%[(q)] × 196 (ie employees at 1 January 20X2) × 4/5 (4 out of 5 years' service performed to date) = CU312,405 . CU312,405 × 0.9524 discount factor = CU297,534.

(j) Category B employees expected to receive long-service payments in December 20X7: Expected salary for 20X6 CU26,750 (January to June) + CU28,623 (July to December) = CU55,373. 5% × CU55,373 × 77%[(q)] × 9 employees (ie started service on 31 December 20X2) × 3/5 (ie 3 out of 5 years' service performed to date) = CU11,512 expected payment. CU11,512 × 0.9009 discount factor = CU10,371.

(k) Category B employees expected to receive long-service payments in December 20X8: Expected salary for 20X7 CU28,623 (January to June) + CU30,626 (July to December) = CU59,249. 5% × CU59,249 × 77%[(q)] × 10 employees (ie started service on 31 December 20X3) × 2/5 (ie 2 out of 5 years' service performed to date) = CU9,124 expected payment. CU9,124 × 0.8547 discount factor = CU7,799.

(l) Category B employees expected to receive long-service payments in December 20X9: Expected salary for 20X8 CU30,626 (January to June) + CU32,770 (July to December) = CU63,396. 5% × CU63,396 × 77%[(q)] × 11 employees (ie started service on 31 December 20X4) × 1/5 (ie 1 out of 5 years' service performed to date) = CU5,370 expected payment. CU5,370 × 0.8 discount factor = CU4,296.

(m) Category C employees expected to receive long-service payments in December 20X6: Expected salary for 20X5 CU12,500 (January to June) + CU13,625 (July to December) = CU26,125. 5% × CU26,125 × 73%[(r)] × 306 (ie employees at 1 January 20X2) × 4/5 (4 out of 5 years' service performed to date) = CU233,432 . CU233,432 × 0.9524 discount factor = CU222,321.

(n) Category C employees expected to receive long-service payments in December 20X7: Expected salary for 20X6 CU13,625 (January to June) + CU14,851 (July to December) = CU28,476. 5% × CU28,476 × 73%[(r)] × 18 employees (ie started service on 31 December 20X2) × 3/5 (ie 3 out of 5 years' service performed to date) = CU11,225 expected payment. CU11,225 × 0.9009 discount factor = CU10,113.

(o) Category C employees expected to receive long-service payments in December 20X8: Expected salary for 20X7 CU14,851 (January to June) + CU16,188 (July to December) = CU31,039. 5% × CU31,039 × 73%[(r)] × 11 employees (ie started service on 31 December 20X3) × 2/5 (ie 2 out of 5 years' service performed to date) = CU4,985 expected payment. CU4,985 × 0.8547 discount factor = CU4,261.

(p) Category C employees expected to receive long-service payments in December 20X9: Expected salary for 20X8 CU16,188 (January to June) + CU17,645 (July to December) = CU33,833. 5% × CU33,833 × 73%[(r)] × 15 employees (ie started service on 31 December 20X4) × 1/5 (ie 1 out of 5 years' service performed to date) = CU3,705 expected payment. CU3,705 × 0.8 discount factor = CU2,964.

(q) SME A expects to pay approximately 77% × category B employees' long-service payments in a five-year cycle (ie a saving of 23% due to employees leaving before the long-service payment vests).

Calculation: 36 employees left in 20X2 to 20X5 (ie on average 9 per year). In the absence of evidence to the contrary, SME A assumed that 9 employees would leave in 20X6. 36 (20X2 to 20X5) + 9 (expected 20X6) = 45 employees expected to leave by 31 December 20X6. 45 ÷ 196 category B employees at 1 January 20X2 =

expected 23% saving due to staff turnover of category B employees.

(r) SME A expects to pay approximately 73% × category C employees' long-service payments in a five-year cycle (ie a saving of 27% due to employees leaving before the long-service payment vests).

Calculation: 66 employees left in 20X2 to 20X5 (ie on average 16 per year). In the absence of evidence to the contrary, SME A assumed that 16 employees would leave in 20X6. 66 (20X2 to 20X5) + 16 (expected 20X6) = 82 employees expected to leave by 31 December 20X6. 82 ÷ 306 category C employees at 1 January 20X2 = expected 27% saving due to staff turnover of category C employees.

Case study 2

To encourage employees older than 60 years to extend their employment with the entity, SME B promises its 60-year-old employees a lump-sum benefit equal to 1 per cent of final salary for each year of service they remain employed by SME B after their 60th birthday provided they remain in the employ of SME B until they are 65, at which time, in accordance with local laws, employees are required to retire. The benefit is payable to the employees on retirement.

Employee A's 60th birthday is on 1 January 20X1. Her salary for the year ended 31 December 20X1 is CU100,000.

At 31 December 20X1 SME B made the following actuarial assumptions:

- Employee A's salary should increase by 5 per cent (compound) each year.
- There is a 20 per cent probability that employee A's employment with SME B will terminate before 1 January 20X6.
- The appropriate discount rate is 10 per cent per year (determined in accordance with paragraph 28.17).

Employee A's salary for 20X2 is CU105,000.

At 31 December 20X2 SME B revised its actuarial assumptions as follows:

- Employee A's salary should increase by 15 per cent (compound) each year.
- There is a 10 per cent probability that employee A's employment with SME B will terminate before reaching retirement date of 1 January 20X6.
- The appropriate discount rate remains 10 per cent per year (determined in accordance with paragraph 28.17).

SME B does not fund its obligation to pay lump-sum benefits. It recognises actuarial gains and losses in other comprehensive income.

Part A

SME B uses the projected unit credit method to measure its defined benefit post-retirement obligation.

Calculate the amounts that SME B would recognise in profit or loss and in other comprehensive income for the year ended 31 December 20X1 and 31 December 20X2.

Part B

The facts are the same as in part A. However, in this part, assume that the employee is not required to retire at 65 and that the benefit vests and is payable on the employee's 65th birthday.

Calculate the amounts that SME B would recognise in profit or loss and in other comprehensive income for the year ended 31 December 20X1 and 31 December 20X2.

Part C
The facts are the same as in part A. However, in this part, assume that SME B is not able, without undue cost or effort, to use the projected unit credit method to measure its defined benefit obligation. It measures its defined benefit obligation using all of the simplifications permitted in paragraph 28.19.

Calculate the amounts that SME B would recognise in profit or loss and in other comprehensive income for the year ended 31 December 20X1 and 31 December 20X2.

Answer to case study 2

Part A

SME B follows an accounting policy of recognising actuarial gains and losses in other comprehensive income. All other components of the cost of the defined benefit plan are recognised in profit or loss.

For the year ended 31 December 20X1 SME A recognises a current service cost expense of CU664 in profit or loss.

Calculation:

Expected final salary = CU100,000 × $(1.05)^4$ = CU121,551.

Benefit for the current year = 1% × CU121,551 expected final salary = CU1,216.

Adjustment for vesting condition = CU1,216 less (20% × CU12,155) = CU972.

Present value = CU973 × $1/(1.1)^4$ = CU973 × 0.683013 = CU664.

For the year ended 31 December 20X2 SME A recognises an expense of CU1,146 (ie CU1,080 current service cost + CU66 interest) in profit or loss and an expense of CU350 (actuarial loss) in other comprehensive income.

Calculations:

Current service cost

Expected final salary = CU105,000 × $(1.15)^3$ = CU159,692.

Benefit for the current year = 1% × CU159,692 expected final salary = CU1,597.

Adjustment for vesting condition = CU1,597 less (10% × CU1,597) = CU1,437.

Present value = CU1,437 × $1/(1.1)^3$ = CU1,437 × 0.751315 = CU1,080.

Interest

CU664 opening obligation × 10% = CU66.

Actuarial loss

Calculation of closing obligation

Expected final salary = CU105,000 × $(1.15)^3$ = CU159,692.

Benefit for 20X1 and 20X2 = 2 × (1% × CU159,692 expected final salary) = CU3,194.

Adjustment for vesting condition = CU3,194 less (10% × CU3,194) = CU2,875.

Present value = CU2,875 × $1/(1.1)^3$ = CU2,875 × 0.751315 = CU2,160.

CU2,160 closing obligation less CU1,080 current service cost less CU66 interest less CU664 opening obligation = CU350 actuarial loss.

Notes:

The following table shows how the obligation builds up for employee A, assuming that the only change in actuarial assumptions after 20X2 was the removal of uncertainty regarding vesting at the end of 20X5.

	20X1	*20X2*	*20X3*	*20X4*	*20X5*
Benefit attributed to:					
– prior years	–	1,596.92	3,193.84	4,790.76	6,387.68
– current year (1% × final salary)	1,215.51	1,596.92	1,596.92	1,596.92	1,596.92
– current and prior years	**1,215.51**	**3,193.84**	**4,790.76**	**6,387.68**	**7,984.59**
Opening obligation	**–**	**664.17**	**2,159.63**	**3,563.38**	**5,226.29**
Interest at 10%	–	66.42	215.96	356.34	522.63
Actuarial loss (balancing figure)	–	349.23	–	–	798.44
Current service cost[(a)]	664.17	1,079.81	1,187.79	1,306.57	1,437.23
Closing obligation[(b)]	**664.17**	**2,159.63**	**3,563.38**	**5,226.29**	**7,984.59**

(a) The current service cost is the present value of benefit attributed to the current year.

(b) The closing obligation is the present value of benefit attributed to current and prior years.

Part B

The answer to Part B is the same as the answer to Part A. However, in Part B the expense would be described as ‘other long-term benefit’ instead of ‘post-employment benefit’.

Part C

For the year ended 31 December 20X1 SME A recognises a current service cost expense of CU683 in profit or loss.

Calculation:

Benefit for the current year = 1% × CU100,000 current salary = CU1,000.

Present value = CU1,000 × $1/(1.1)^4$ = CU1,000 × 0.683013 = CU683.

For the year ended 31 December 20X2 SME A recognises an expense of CU857 (ie CU789 current service cost + CU68 interest) in profit or loss and an expense of CU38 (actuarial loss) in other comprehensive income.

Calculations:

Current service cost

Benefit for the current year = 1% × CU105,000 expected final salary = CU1,050.

Present value = CU1,050 × $1/(1.1)^3$ = CU1,050 × 0.751315 = CU789.

Interest

CU683 opening obligation × 10% = CU68.

Actuarial loss

Calculation of closing obligation

Benefit for 20X1 and 20X2 = 2 years × 1% × CU105,000 expected final salary = CU2,100.

Present value = CU2,100 × $1/(1.1)^3$ = CU2,100 × 0.751315 = CU1,578.

CU1,578 closing obligation less CU789 current service cost less CU68 interest less CU683 opening obligation = CU38 actuarial loss.

Note: the following table shows how the obligation builds up for employee A, assuming that there are no changes in actuarial assumptions after 20X2.

Year	*20X1*	*20X2*	*20X3*	*20X4*	*20X5*
1% × current salary	1,000	1,050	1,207.50	1,388.63	1,596.92
Years service at end of year	1	2	3	4	5
Future value of obligation	**1,000**	**2,100**	**3,622.50**	**5,554.50**	**7,984.59**
Discount factor (10%)	0.683013	0.751315	0.826446	0.909091	1
Present value of obligation	**683.01**	**1,577.76**	**2,993.80**	**5,049.55**	**7,984.59**
Opening obligation	**–**	**683.01**	**1,577.76**	**2,993.80**	**5,049.55**
Interest (10%)	–	68.30	157.78	299.38	504.96
Current service cost[(a)]	683.01	788.88	997.93	1,262.39	1,596.92
Actuarial gain or loss (balancing figure)	–	37.57	260.33	493.98	833.16
Closing obligation[(b)]	**683.01**	**1,577.76**	**2,993.80**	**5,049.55**	**7,984.59**

Notes:

[(a)] The current service cost is the present value of benefit attributed to the current year (including the effect of salary increases with respect to prior period service).

[(b)] The closing obligation is the present value of benefit attributed to current and prior years.

Case study 3

SME C provides its employees with two types of post-employment benefit—a final salary scheme pension benefit and a medical scheme. It recognises actuarial gains and losses arising from the defined benefit plans in profit or loss.

Pension benefit

SME C's employees and former employees are provided with pensions in accordance with SME C's defined benefit final salary pension scheme. The scheme provides a monthly pension of 0.25 per cent of final salary for each year of service. The pension is payable from the age of 60. The pension plan is funded through payments to a separate legal entity set up for the sole purpose of paying pensions to its employees.

At 31 December 20X2 SME C's actuaries using the projected unit credit method measured the pension plan obligation at CU20,000 (20X1: CU17,000 and 20X0: CU16,500). The current service cost is CU900 for the year ended 31 December 20X2 (20X1: CU800) and interest cost attributable to the unwinding of the discount in the defined benefit obligation is CU860 (20X1: CU1,100).

The actual return on the pension plan assets for the year ended 31 December 20X2 is CU1,950 (20X1: CU1,900).

At 31 December 20X2 SME C determined the fair value of the pension plan assets at CU18,000 (20X1: CU16,000 and 20X0: CU14,000). The major categories of plan assets as a percentage of total plan assets are as follows:

	20X2	*20X1*
Jurisdiction A equities	25%	25%
Jurisdiction B equities	25%	18%
Jurisdiction A bonds	20%	30%
Jurisdiction B bonds	20%	17%
Jurisdiction A property	10%	10%

The plan assets include property occupied by SME C with a fair value of CU300 (20X1: CU250).

In 20X2 the pension fund paid pensions of CU750 (20X1: CU500) to past employees of SME C and SME C contributed CU800 (20X1: CU600) to the fund.

Medical scheme

SME C is also obliged to reimburse 10 per cent of its employee's post-employment medical costs if the employee has provided 25 years or more of service to the group. SME C does not fund this obligation in advance.

At 31 December 20X2 SME C's actuaries determined the carrying amount of the medical plan obligation at CU7,000 (20X1: CU6,000 and 20X0: CU5,000). The current service cost is CU490 for

the year ended 31 December 20X2 (20X1: CU430) and interest cost attributable to the unwinding of the discount in the defined benefit obligation is CU800 (20X1: CU750).

In 20X2 SME C paid CU600 (20X1: CU550) for past employee medical costs.
The principal actuarial assumptions applied by SME C at the end of the reporting period (expressed as weighted averages) are:

	20X2	*20X1*
Discount rate at 31 December	5%	6.5%
Future salary increases	5%	4%
Future pension increases	3%	2%
Annual increase in healthcare costs	8%	8%
Future changes in maximum state healthcare benefits	3%	2%

Prepare an extract from the annual financial statements of SME C for the year ended 31 December 20X2 to record the information set out above.

Answer to case study 3

Extract from SME C's group consolidated statement of financial position at 31 December 20X2:

Description	*Note*	*20X2*	*20X1*
LIABILITIES			
…			
Provision for employee benefits	18	CUXX,XXX	CUXX,XXX
…			

Extract from SME C's notes to the financial statements at 31 December 20X2:

Note 1 Accounting policies

Employee benefits—defined benefit post-employment plans

SME C has obligations to its employees and former employees to provide pensions in accordance with its defined benefit final salary pension scheme. The terms of the scheme oblige SME C to provide employees with a pension equal to 0.25 per cent of the employee's final salary for every year of service provided. The defined benefit pension plan is funded by the entity through payments to a separate legal entity set up for the sole purpose of paying pensions to its employees.

SME C is also obliged to reimburse 10 per cent of its employee's post-employment medical costs if the employee has provided 25 years or more of service to SME C. SME C does not fund this obligation in advance.

SME C measures defined benefit liabilities (assets) at the present value of its obligations under defined benefit plans at the reporting date minus the fair value at the reporting date of plan assets out of which the obligations are to be settled directly. The obligations under defined benefit plans are determined using the projected unit credit method. Actuarial gains and losses are recognised in profit or loss in the period in which they occur.

Note 18 Employee benefits

All amounts are presented in currency units 'CU''.

	20X2	*20X1*
…		
Post-employment plans—defined benefit liabilities	CU9,000	CU7,000
…		
Total liabilities for employee benefits	CUXX,XXX	CUXX,XXX

Post-employment plans—defined benefits plans

	Defined benefit pension plans		*Post-employment medical benefits*	
	20X2	*20X1*	*20X2*	*20X1*
Present value of funded obligations	20,000	17,000	-	-
Fair value of plan assets	(18,000)	(16,000)	-	-
Present value of unfunded obligations	-	-	7,000	6,000
Net liability	2,000	1,000	7,000	6,000

The most recent comprehensive actuarial valuation was performed as at 31 December 20X2.

The pension plan assets include property occupied by SME C with a fair value of CU300 (20X1: CU250).

The amounts recognised in profit or loss expense (income) are:

	Defined benefit post-employment benefits	
	20X2	*20X1*
Defined benefit pension plan	1,800 [(a)]	(900) [(b)]
Post-employment medical benefits	1,600 [(c)]	1,550 [(d)]
Post-employment benefits	**3,400**	**650**

Changes in the present value of the defined benefit obligation are as follows:

	Defined benefit pension plans 20X2	*Post-employment medical benefits 20X2*	*Total*
Defined benefit obligations at 01/01/20X2	17,000	6,000	23,000
Service cost	900	490	1,390
Interest cost	860	800	1,660
Actuarial losses (gains)	1,990 [(e)]	310 [(f)]	2,300
Benefits paid	(750)	(600)	(1,350)
Defined benefit obligations at 31/12/20X2	**20,000**	**7,000**	**27,000**

Changes in the fair value of plan assets are as follows:

	Defined benefit pension plans 20X2
Opening fair value of plan assets	16,000
Actual return on plan assets	1,950
Contributions by employer	800
Benefits paid	(750)
Closing fair value of plan assets	**18,000**

The major categories of plan assets as a percentage of total plan assets are as follows:

	20X2	*20X1*
Jurisdiction A equities	25%	25%
Jurisdiction B equities	25%	18%
Jurisdiction A bonds	20%	30%
Jurisdiction B bonds	20%	17%
Jurisdiction A property	10%	10%

Principal actuarial assumptions at the end of the reporting period (expressed as weighted averages):

	20X2	*20X1*
Discount rate at 31 December	5%	6.5%
Future salary increases	5%	4%
Future pension increases	3%	2%
Annual increase in healthcare costs	8%	8%
Future changes in maximum state healthcare benefits	3%	2%

The calculations and explanatory notes below do not form part of the answer to this case study:

(a) CU900 pension current service cost + CU860 pension interest cost + CU1,990(e) pension actuarial loss less CU1,950 pension actuarial return on plan assets = CU1,800 expense.

(b) CU800 pension current service cost + CU1,100 pension interest cost less CU900(e) pension actuarial gain less CU1,900 pension actuarial return on plan assets = CU900 income.

(c) CU490 medical plan current service cost + CU800 medical plan interest cost + CU310(f) medical plan actuarial loss = CU1,600 expense.

(d) CU430 medical plan current service cost + CU750 medical plan interest cost + CU370(e) medical plan actuarial loss = CU1,550 expense.

(e) Calculation of actuarial gains (losses) on pension plan obligation:

Funded defined benefit pension plan obligation account

20X1	Pensions paid to past employees	CU500	01/01/20X1	Opening balance	CU16,500
20X1	.: actuarial gain	CU900	20X1	Current service cost	CU800
31/12/20X1	Closing balance	CU17,000	20X1	Interest cost	CU1,100
		CU18,400			CU18,400
20X2	Pensions paid to past employees	CU750	01/01/20X2	Opening balance	CU17,000
			20X2	Current service cost	CU900
			20X2	Interest cost	CU860
31/12/20X2	Closing balance	CU20,000	20X2	.: actuarial loss	CU1,990
		CU20,750			CU20,750
			01/01/20X3	Opening balance	CU20,000

(f) Calculation of actuarial gains (losses) on medical plan obligation:

Funded defined benefit medical plan obligation account

20X1	Medical benefits paid to past employees	CU550	01/01/20X1	Opening balance	CU5,000
			20X1	Current service cost	CU430
			20X1	Interest cost	CU750
31/12/20X1	Closing balance	CU6,000	20X2	.: actuarial loss	CU370
		CU6,550			CU6,550
20X2	Medical benefits paid to past employees	CU600	01/01/20X2	Opening balance	CU6,000
			20X2	Current service cost	CU490
			20X2	Interest cost	CU800
31/12/20X2	Closing balance	CU7,000	20X2	.: actuarial loss	CU310
		CU7,600			CU7,600
			01/01/20X3	Opening balance	CU7,000