

HKFRS / IFRS UPDATE 2013/08

DEFINED BENEFIT PLANS: EMPLOYEE CONTRIBUTIONS



Background

In May and September 2012, the IFRS Interpretations Committee (Interpretations Committee) received submissions seeking clarification surrounding the treatment of employee contributions to a defined benefit plan, when these contributions are set out in the formal terms of that plan. The International Accounting Standards Board (IASB) subsequently addressed this submission at their January 2013 meeting.

Currently, paragraph 93 of IAS 19 *Employee Benefits* addresses the accounting for contributions from employees (or third parties) to an entity's defined benefit plan, when the requirement for such contributions is set out in the formal terms of a defined benefit plan.

IAS 19.93 requires these contributions to be accounted for either:

- As a reduction to service cost (if they are linked to service)
- As a reduction in the remeasurement of the net defined benefit liability (asset).

IAS 19.93 also requires contributions from employees or third parties in respect of service to be attributed to periods of service as a negative benefit (in accordance with IAS 19.70).

The question raised in the submissions to the Interpretations Committee were whether these contributions from employees or third parties should instead be accounted as reduction in entity's short term benefit cost (ie netted off against "salaries paid"), rather than a reduction in the post-employment benefit cost (ie a "negative benefit").

Because the contributions made by employees or third parties were related to an entity's defined benefit plan, the IASB concluded that these contributions form part of the post-employment benefit rather than the short-term employee benefit, and therefore a reduction in entity's short term benefit cost would not be appropriate (see paragraph BC3 of the ED).

The IASB did however acknowledge various practical concerns regarding the complexity and confusion in relation to attributing this "negative benefit" to the periods of service.

In response, the IASB has issued an ED that proposes to introduce a practical expedient that would allow certain contributions from employees or third parties (only those linked solely to the employee's service rendered in the same period in which they are payable) to be recognised as a reduction in the service cost in the period the employee's services were rendered, rather being attributed to periods of service as a "negative benefit".

HKICPA is seeking views on this ED. The comment period in Hong Kong will end on 26 June 2013.

STATUS

Exposure Draft

EFFECTIVE DATE

To be confirmed

ACCOUNTING IMPACT

Limited to entities with defined benefit plans where employees and/or other third-parties make contributions to the plans

Summary

On 25 March 2013, the IASB published Exposure Draft *ED/2013/4 Defined Benefit Plans: Employee Contributions*. The ED addresses the accounting for contributions from employees or third parties to an entity's defined benefit plan, when the requirement for such contributions is set out in the formal terms of the defined benefit plan.

The proposed change would introduce narrow scope amendments to IAS 19.93 that would:

- i. Provide a practical expedient to certain contributions from employees or third parties to a defined benefit plan, but only those that are linked solely to the employee's service rendered in the same period in which they are payable
- ii. Clarify that the treatment of contributions from employees or third parties to a defined benefit plan that are not subject to the practical expedient.

(i) Practical expedient

A practical expedient has been included within IAS 19.93, and only applies to contributions from employees or third parties that are linked solely to the employee's service rendered in the same period in which they are payable.

For example, contributions from employees or third parties that are based on a fixed percentage of the employee's salary that do not depend on the employee's number of years of service to the employer, would be considered contributions linked solely to the employee's service rendered. This is because these contributions are in proportion to the salary paid, and therefore can be considered to be linked solely to the employee's service rendered in that period.

In contrast, contributions from employees or third parties where the percentage contributed increases relative to the number of years of service, would result in higher contributions being required in the latter years. These higher contributions could be considered to be linked not only to the service in the current year, but also to the service in other years. In this case, the contributions are not linked solely to the employee's service that is rendered the same period in which the contributions are payable. Therefore the practical expedient could not be applied to these contributions from employees or third parties.

(ii) Clarification - treatment of contributions not subject to the practical expedient

The IASB also acknowledged that the current wording of IAS 19 paragraph 93 (that first states that contributions from employees or third parties in respect of service are attributed to periods of service as a negative benefit in accordance with IAS 19 paragraph 70, and then states that the net benefit is attributed in accordance with paragraph 70) has caused confusion about whether the back-end loading test in paragraph 70 should be performed on the net benefit, or on the gross benefit and the negative benefit separately.

In observing how the performance of the test on the net benefit would be carried out in practice, the IASB concluded that this would result in added complexity – as, depending on how the attribution test was applied, the outcome of the test may be influenced by changes in the assumptions year-on-year.

Consequently, the ED proposes a rewording of IAS 19 paragraph 93, which would clarify that the negative benefit from contributions from employees or third parties should be attributed to periods of service in the same way that the gross benefit is attributed in accordance with IAS 19 paragraph 70, when they are not recognised as a reduction in the service cost in the same period in which they are payable (ie when the practical expedient is not applicable).

Disclosures

The ED does not propose any additional disclosures, including any disclosure of the amount by which the service cost is reduced when applying the proposed practical expedient.

In the basis for conclusions the IASB notes that in its view there are already sufficient disclosure requirements within IAS 19 which will adequately address this issue. For example, paragraph 141(f) of IAS 19 already requires the disclosure of contributions to defined benefit plans in the reconciliation for the net defined benefit liability (asset), showing separately those contributions made by the employer and those by the plan participants (ie the employees or third parties).

Effective date and transition

The effective date for the amendments, if finalised, is to be confirmed. The ED proposes retrospective application in accordance with of IAS 8 *Accounting Policies and Changes in Accounting Estimates and Errors*, with early application permitted.

Comment period

The ED has been published with a 120 day consultation period, with comments due by 25 July 2013.

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