

Straight away

IFRS bulletin from PwC

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IAS 19 amendment significantly changes accounting for employee benefits

What is the issue?

The IASB has issued an amendment to IAS 19, 'Employee benefits', which makes significant changes to the recognition and measurement of defined benefit pension expense and termination benefits, and to the disclosures for all employee benefits.

The changes will affect most entities that apply IAS 19. They could significantly change a number of performance indicators and might also significantly increase the volume of disclosures.

The key changes are as follows:

- **Recognition of actuarial gains and losses (remeasurements):** 'Actuarial gains and losses' are renamed 'remeasurements' and will be recognised immediately in 'other comprehensive income' (OCI). Actuarial gains and losses will no longer be deferred using the corridor approach or recognised in profit or loss; this is likely to increase balance sheet and OCI volatility. Remeasurements recognised in OCI will not be recycled through profit or loss in subsequent periods.
- **Recognition of past service cost/curtailment:** Past-service costs will be recognised in the period of a plan amendment; unvested benefits will no longer be spread over a future-service period. A curtailment now occurs only when an entity reduces significantly the number of employees. Curtailment gains/losses are accounted for as past-service costs.

- **Measurement of pension expense:** Annual expense for a funded benefit plan will include net interest expense or income, calculated by applying the discount rate to the net defined benefit asset or liability. This will replace the finance charge and expected return on plan assets, and will increase benefit expense for most entities. There will be no change in the discount rate, which remains a high-quality corporate bond rate where there is a deep market in such bonds, and a government bond rate in other markets.
- **Presentation in the income statement:** There will be less flexibility in income statement presentation. Benefit cost will be split between (i) the cost of benefits accrued in the current period (service cost) and benefit changes (past-service cost, settlements and curtailments); and (ii) finance expense or income. This analysis can be in the income statement or in the notes.
- **Disclosure requirements:** Additional disclosures are required to present the characteristics of benefit plans, the amounts recognised in the financial statements, and the risks arising from defined benefit plans and multi-employer plans. The objectives and principles underlying disclosures are provided; these are likely to require more extensive disclosures and more judgement to determine what disclosure is required.

- **Distinction between 'short-term' and 'other long-term' benefits:** The distinction between short- and long-term benefits for measurement purposes is based on when payment is expected, not when payment can be demanded. An obligation measured as a long-term benefit could therefore be presented as a current liability when the entity expects to settle after more than one year, but does not have the unconditional ability to defer settlement for more than one year.
- **Treatment of expenses and taxes relating to employee benefit plans:** Taxes related to benefit plans should be included either in the return on assets or the calculation of the benefit obligation, depending on their nature. Investment management costs should be recognised as part of the return on assets; other costs of running a benefit plan should be recognised as period costs when incurred. This should reduce diversity in practice but might make the actuarial calculations more complex.
- **Termination benefits:** Any benefit that has a future-service obligation is not a termination benefit. This will reduce the number of arrangements that meet the definition of termination benefits. A liability for a termination benefit is recognised when the entity can no longer withdraw the offer of the termination benefit or recognises any related restructuring costs. This might delay the recognition of voluntary termination benefits.
- **Risk or cost sharing features:** The measurement of obligations should reflect the substance of arrangements where the employer's exposure is limited or where the employer can use contributions from employees to meet a deficit. This might reduce the defined benefit obligation in some situations. Determining the substance of such arrangements will require judgement and significant disclosure.

Effective date and transition

The amendment is effective for periods beginning on or after 1 January 2013. Earlier application is permitted. The amendment should be applied retrospectively in accordance with IAS 8, 'Accounting policies, changes in accounting estimates and errors', except for changes to the carrying value of assets that include employee benefit costs in the carrying amount.

Am I affected?

These changes will affect most entities that apply IAS 19. The changes could significantly change a number of performance indicators, including EBITDA, EPS and balance sheet ratios. They might also significantly increase the volume of disclosures.

What do I need to do?

Management should determine the impact of the revised standard and, in particular, any changes in benefit classification and presentation.

Management should consider the effect of the changes on any existing employee benefit arrangements and whether additional processes are needed to compile the information required to comply with the new disclosure requirements.

Management should also consider the choices that remain within IAS 19, including the possibility of early adoption, the possible effect of these changes on key performance ratios and how to communicate these effects to analysts and other users of the accounts.

If you have questions about this issue, please contact your PwC engagement partner. Engagement teams that have questions should contact their Global Accounting Consulting Services Contact.