Project **Post-employment benefits**

Topic **Past service cost, curtailments and settlements**

Objective

1. This paper provides:

   (a) background, including an overview of the current requirements in IAS 19 *Employee Benefits* relating to past service cost, curtailments and settlements and an overview of the proposals in the ED relating to the presentation of these items (paragraphs 4 – 15).

   (b) an overview of responses to the ED (paragraphs 16 – 26)

   (c) a staff analysis and recommendations (paragraphs 27 – 70)

   (d) additional materials to help illustrate and explain the staff analysis in Appendix A and Appendix B.

2. The staff will present a discussion of the timing of recognition of past service cost, curtailments and settlements and how the timing of recognition interacts with other related transactions, such as restructurings and termination benefits, at a future meeting.

3. In summary, the staff recommends that the Board:

   (a) amends the definition of curtailments to retain part (a) (a significant reduction in the number of employees covered by a plan) and to remove part (b) (an amendment to benefits for future service),

   (b) amends the definition of settlements to exclude curtailments and amendments that result in past service cost,

(c) amends the definition of non-routine settlements to exclude benefits envisaged in the terms of the plan,

(d) requires that past service cost and gains and losses on non-routine settlements and curtailments amendments are presented in the service cost component,

(e) requires routine settlements to be presented in the remeasurements component; and

(f) confirms the disclosure requirement proposed in the ED for past service cost, curtailments and settlements but amended to not require distinguishing between these items if they occur together and are presented in the same component.

Background

4. At the Board's October meeting, the Board tentatively confirmed the proposals in the exposure draft *Defined Benefit Plans* (the ED) that:

(a) an entity should disaggregate changes in the net defined benefit liability (asset) into service cost, finance cost and remeasurement components.

(b) the service cost component should exclude gains and losses arising from changes in the assumptions used to measure the service cost.

(c) the finance cost component should comprise net interest on the net defined benefit liability (asset), determined by applying the rate used to measure the defined benefit obligation to the net defined benefit liability (asset).

5. At the Board's November meeting, the Board tentatively decided that :

(a) an entity should present the service cost and finance cost components in profit or loss.

(b) an entity should present the remeasurements component either in profit or loss or other comprehensive income.

6. The objective of this paper is to discuss in which component an entity should include the effect of the following other changes in the net defined benefit liability or asset:

   (a) Past service cost (arising from plan amendments)

   (b) Gains and losses arising from curtailments

   (c) Gains and losses arising from settlements

Current requirements in IAS 19

7. Paragraph 97 of IAS 19 states that past service cost arises when an entity introduces a defined benefit plan that attributes benefits to past service or changes the benefits payable for past service under an existing defined benefit plan (a plan amendment). Past service cost excludes the effects of plan amendments that reduce benefits for future service, which are curtailments, as defined in IAS 19[1]. Current IAS 19 requires entities to recognize unvested past service cost on a straight line basis over the vesting period[2]. At its October meeting, the Board tentatively decided that an entity should recognize unvested past service cost immediately.

8. Paragraph 111 of IAS 19 states that a curtailment occurs when an entity either:

   (a) reduces the number of employees covered by the plan, or

   (b) amends the terms of the plan so that a significant element of future service by current employees will no longer qualify for benefits, or will qualify only for reduced benefits.

9. Paragraph 112 of IAS 19 states that a settlement occurs when an entity enters into a transaction that eliminates all future legal or constructive obligations for part or all of the benefits provided in a defined benefit plan, for example, when a lump-sum cash payment is made to, or on behalf of, plan participants in exchange for their rights to receive specified post-employment benefits.

[1] Paragraph 98 of IAS 19
[2] Paragraph 96 of IAS 19

The ED proposals

10. The ED proposed that:

    (a) gains and losses on routine and non-routine settlements are actuarial gains and losses and should be included in the remeasurement component that is presented in other comprehensive income, and

    (b) curtailments should be treated in the same way as plan amendments, with gains and losses on curtailment presented in profit or loss.

11. Gains and losses arise on settlements because of a difference between the defined benefit obligation, as remeasured at the transaction date, and the settlement price. The proposal in the ED was based on the view that a gain or loss on settlement is an experience adjustment arising in the period. Therefore, the ED proposed that gains and losses on settlement are treated in the same way as actuarial gains and losses and so would be presented in the remeasurement component.

12. In addition, the ED proposed that unvested past service cost should be recognised in the period of the plan amendment. This proposal means that gains and losses arising from curtailments are recognised in the same way as negative past service costs. This is consistent with the Board’s view that a curtailment is similar to a plan amendment because it occurs when an entity takes an action that reduces the benefits provided by the plan to employees; plan amendments are when an entity reduces benefits for past service and curtailments are when an entity reduces benefits for future service. Therefore, the ED proposed that curtailments should be treated in the same way as plan amendments, with gains and losses presented in profit or loss.

Current requirements in US GAAP

13. The requirements for curtailments and settlements can be found in the FASB Accounting Standard Codification (ASC) Subtopic 715-30 Compensation—*Retirement Benefits-Defined Benefit Plans—Pension*.

14. US GAAP defines a plan curtailment as an event that significantly reduces the expected years of future service of present employees or eliminates for a significant number of employees the accrual of defined benefits for some or all of their future services. Curtailments include:

    (a) termination of employees' services earlier than expected, which may or may not involve closing a facility or discontinuing a component of an entity.

    (b) termination or suspension of a plan so that employees do not earn additional defined benefits for future services. In the latter situation, future service may be counted toward vesting of benefits accumulated based on past service.

15. US GAAP defines a settlement as a transaction that is an irrevocable action, relieves the employer (or the plan) of primary responsibility for a pension or postretirement benefit obligation, and eliminates significant risks related to the obligation and the assets used to effect the settlement. Examples of transactions that constitute a settlement include making lump-sum cash payments to plan participants in exchange for their rights to receive specified pension benefits and purchasing nonparticipating annuity contracts to cover vested benefits.

Responses to the ED

16. Question 7 of the ED asked respondents the following:

> (a) Do you agree that gains and losses on routine and non-routine settlements are actuarial gains and losses and should therefore be included in the remeasurement component? (Paragraphs 119D and BC47) Why or why not?
>
> (b) Do you agree that curtailments should be treated in the same way as plan amendments, with gains and losses presented in profit or loss? (Paragraphs 98A, 119A(a) and BC48)
>
> (c) Should entities disclose (i) a narrative description of any plan amendments, curtailments and non-routine settlements, and (ii) their effect on the statement of comprehensive income? (Paragraphs 125C(c), 125E, BC49 and BC78)

Why or why not?

17. Overall, the majority of respondents to the ED supported the proposal:

    (a) to present gains and losses arising from curtailments in profit or loss;

    (b) to present gains and losses arising from *routine settlements* in other comprehensive income; and

    (c) to disclose details of any plan amendments, curtailments and non-routine settlements.

18. However, the majority of respondents did not support the presentation of *non-routine settlements* in other comprehensive income. The responses to the presentation proposals in the ED also raised a number of concerns with the current requirements, including:

    (a) The definitions of settlements and curtailments

    (b) The timing of recognition of gains and losses on settlements and curtailments

Responses to question 7(a) on settlements

19. Some respondents agreed with the ED proposal to present the effects of all settlements in other comprehensive income for the following reasons:

    (a) the gain or loss that results from a settlement is an experience adjustment, resulting from a difference between the assumptions that the entity has used to measure the obligation and the actual settlement cost.

    (b) the gain or loss attributable to non-routine settlement would not have predictive value and should not be mixed with the elements of profit or loss that have predictive value.

    (c) the proposal removes the distinction that currently exists between "buy-ins" and "buy-outs". A "buy-in" occurs when a plan purchases matching insurance for the defined benefit obligation, and a "buy-out" occurs when a plan transfers the defined benefit obligation to a third party (usually an insurance company). The current distinction would cease to exist because the impact of each would be presented in OCI rather than the current practice of presenting the effect of "buy-ins" in OCI and "buy-outs" in profit or loss. A "buy-in" affects OCI due to the change in fair value of plan assets triggered by the purchase of matching insurance, because paragraph 104 deems the fair value of matching insurance to be the present value of the related obligations. Others believe that a gain or loss for both a "buy-in" and a "buy-out" should be presented in profit or loss (paragraph 26(c))

(d) the effects of settlement of benefits that are in accordance with the terms of the plan (for example, terms that allow the employee to opt for either the payment of a pension or a lump sum) are an actuarial gain or loss because the measurements of the DBO would reflect estimates of the proportion of employees who would select each option.

20. Many respondents disagreed with the ED proposal to present the effects of all settlements in other comprehensive income for the following reasons:

(a) there is overlap in the definitions of settlements and curtailments and the transactions usually happen at the same time, therefore it can be difficult to allocate the gains and losses between them. Requiring different accounting treatments for non-routine settlements and curtailments will introduce practical difficulties, diversity in practice and structuring opportunities.

(b) settlements with third parties typically involve additional cost (such as a profit margin for the third party) and the effect of management's decision to incur this additional cost should be reflected in profit or loss when that transaction occurs.

(c) presenting a gain or loss on the de-recognition of a liability in OCI seems inconsistent with other standards that require a gain or loss on the de-recognition of a liability to be presented in profit or loss.

(d) if non-routine settlements are the result of an event accounted for separately in profit or loss, then the gain or loss on settlement should be presented together with that event.

(e) non-routine settlement can be interpreted as an "action" of the plan sponsor, therefore the argument that a plan amendment should be recognised in profit or loss "because [the plan amendment] occurs [where] an entity takes an action that reduces the benefits provided by the plan to employees" (ED IAS 19.BC48) is applicable for the treatment of settlement transactions as well.

Responses to Question 7(b) on curtailments

21. A majority of respondents supported the proposal to include the effect of curtailments in profit or loss. However, some respondents disagreed for the following reasons:

(a) plan amendments and curtailments occur infrequently and the resulting gains and losses do not provide users with predictive value. If a difference in predictive value is the characteristic used to determine whether an amount should be presented in profit or loss or other comprehensive income, then plan amendments and curtailments should be presented in other comprehensive income. Thus, the proposal is inconsistent with the Board's conclusion that items that provide little information about the amount and timing of future cash flows should be presented in other comprehensive income. If the Board takes "predictive value" of the respective items as the basis of its presentation decisions, this requires both past service cost and gains and losses arising from curtailments to be presented in other comprehensive income – the same as gains and losses on settlements.

22. Some respondents addressed the two parts of the definition of curtailments separately:

(a) Curtailments resulting from an entity amending the terms affecting future service are the same as a plan amendment and entities should account for them in the same way. Given the other changes proposed in the ED, particularly the elimination of deferred recognition of past service cost, these respondents would not include this type of event in the definition of a curtailment.

(b) Curtailments resulting from a significant reduction in the number of employees covered by the plan are more akin to other gains and losses and should be presented in the remeasurement component. The change in DBO arising from such an event is not a change in the benefits provided, but rather a remeasurement resulting from experience differing from the assumption of an ongoing plan. The curtailment gain or loss results from the termination of employment before the termination of employment had been expected in previous measurements of cost. It is possible, however, that this distinction may not be clear cut. There may be factors that would support the conclusion that the curtailment gain or loss associated with the termination of employment for a significant number of plan participants should be presented in profit or loss, such as the similarity between the types of effects produced when an entity reduces the number of employees covered by a plan and when an entity reduces benefits for future service.

Responses to question 7(c) on disclosure

23. Most, respondents supported the requirement to disclose a narrative description and the effect on the statement of comprehensive income of plan amendments, curtailments and non-routine settlements, albeit with the caveat that the disclosure apply only if these transactions are material to the financial statements.

24. Some suggested that, depending on what the Board decides for the purposes of presentation, it should not be necessary to distinguish these items for the purposes of disclosure if they occur simultaneously and are presented together.

25. One suggested that for individual immaterial plan amendments, curtailments and non-routine settlements occurring during the reporting period that are material collectively, the entity shall disclose in aggregate a narrative description of plan amendments, curtailments and non-routine settlements and their effect on the statement of comprehensive income (similar to paragraph B65 of IFRS 3 Business Combinations).

Other clarifications

26. Many asked for clarification of:

    (a) the definitions for routine and non-routine settlements, curtailments and plan amendments. In particular, the definition of a curtailment remains vague in cases where there is a significant reduction in workforce without obvious external factors like a restructuring or a discontinuation of a business facility.

    (b) the timing of recognition of settlements, curtailments and plan amendments. The ED amended the definition of a curtailment in paragraph 98A to eliminate the reference to a 'demonstrable commitment'. The effect of this would be to change the timing of recognizing a curtailment effect that was not linked to a restructuring from when the workforce reduction is announced to when the terminations occur.

    (c) the accounting for a "buy in". For these transactions, the company would have put in a significant lump sum to purchase insurance that matches the benefits but there will be no impact on the profit and loss under the proposed treatment (as the event is not classed as a settlement). Others noted that the proposals to present the effect of all settlements in remeasurements would remove this anomaly (paragraph 19(c)).

(d) the accounting for a settlement arising from transferring a defined benefit obligation and plan assets (if any) to a buyer in connection with the sale of part of the business.

(e) the accounting interactions between settlements, curtailments, termination benefits and restructurings since they often occur together. Respondents are concerned about distinguishing the gain or loss that arises from each transaction, about the timing of recognition of each transaction and the presentation of the gain or loss from each separately.

(f) the accounting for plans that offer a choice of payment of either pension benefits or lump sum benefits.

Staff analysis

27. Appendix A includes figures that are referred to in the following analysis that may help illustrate the interactions between past service cost, curtailments and settlements. Appendix B includes tables with comments and examples that further explain the figures in Appendix A.

28. This section considers the following:

(a) Definitions (paragraphs 30 – 55)

(b) Presentation (paragraphs 56 – 67)

(c) Disclosure (paragraphs 68 – 70)

29. The staff will present a discussion of the timing of recognition of past service cost, curtailments and settlements and how the timing of recognition interacts with other related transactions, such as restructurings and termination benefits, at a future meeting.

Definitions

30. In order to determine the proper presentation for settlements, curtailments and plan amendments it is important to understand the characteristics of the transactions and how they are related. This section considers:

    (a) Past service cost (paragraphs 31 – 33)

    (b) Curtailments (paragraphs 34 – 43)

    (c) Settlements (paragraphs 44 – 52)

    (d) Interaction with termination benefits and restructuring transactions (53 – 55)

Past service cost (Refer Figure 1 in Appendix A and Table 1 in Appendix B)

31. Past service cost (positive or negative) is defined in the ED as follows (without substantial change from current IAS 19 requirements):

    > 7 Past service cost is the change in the present value of the defined benefit obligation for employee service in prior periods, resulting from the introduction of, or changes to, long-term employee benefits.
    >
    > 97 Past service cost arises when an entity introduces a defined benefit plan that attributes benefits to past service or changes the benefits payable for past service under an existing defined benefit plan.

32. Past service cost is distinguished from actuarial gains and losses, and curtailments in Paragraph 98 of the ED (which was redrafted without substantial change from current IAS 19 requirements):

    > 98 Past service cost excludes:
    >
    > (a) the effect of differences between actual and previously assumed salary increases on the obligation to pay benefits for service in prior years (there is no past service cost because actuarial assumptions allow for projected salaries);
    >
    > (b) underestimates and overestimates of discretionary pension increases when an entity has a constructive obligation to grant such increases

(there is no past service cost because actuarial assumptions allow for such increases);

(c) estimates of benefit improvements that result from actuarial gains that have been recognised in the financial statements if the entity is obliged, by either the formal terms of a plan (or a constructive obligation that goes beyond those terms) or legislation, to use any surplus in the plan for the benefit of plan participants, even if the benefit increase has not yet been formally awarded (the resulting increase in the obligation is an actuarial loss and not past service cost, see paragraph 85(b));

(d) the increase in vested benefits when, in the absence of new or improved benefits, employees complete vesting requirements (there is no past service cost because the entity recognised the estimated cost of benefits as current service cost as the service was rendered); and

(e) the effect of plan amendments that reduce benefits for future service (a curtailment).

33. However, the distinction between plan amendments and actuarial gains and losses is not always clear cut and there are instances where plan amendments and actuarial gains and losses overlap and judgment is required (refer Figure 1).

Curtailments (Refer Figure 2 in Appendix A and Table 2 in Appendix B)

34. Curtailments were defined in the ED as follows (without substantial change from current IAS 19 requirements):

7 A curtailment is either:

(a) a significant reduction in the number of employees covered by a plan; or

(b) an amendment to the terms of a defined benefit plan so that a significant element of future service by current employees will no longer qualify for benefits, or will qualify only for reduced benefits.

35. Part (b) of the curtailments definition is the same as the definition of past service cost except it applies to plan amendments that change benefits for future service.

36. Only current and past service cost is recognised in the defined benefit obligation, however changes to benefits for future service affect the measurement of the defined benefit obligation in current IAS 19 because of:

    (a) benefits that are attributed on a straight-line basis in accordance with the attribution requirements of IAS 19. For these benefits, any change in the estimate of the total amount to be attributed affects the amounts attributed to prior periods. The amounts attributed to prior periods are past service cost.

    (b) benefits that are attributed on the basis of the benefit formula. For these benefits, changing the amounts attributed to future periods will not affect the amounts attributed to prior periods directly. However, the change to benefits for future periods may trigger a change in assumptions (such as staff turnover). It might not be clear whether changes in assumptions resulting from a plan amendment meet the definition of past service cost or actuarial gains or losses.

    (c) the recognition of unvested past service cost arising from a plan amendment over the vesting period. An entity includes any related unrecognized past service cost when determining the gain or loss on curtailment.

37. The changes to the defined benefit obligation in paragraphs 36(a) and 36(b) above fall under the definitions of past service cost or actuarial gains and losses, however the distinction between past service cost and curtailments is necessary in current IAS 19 because curtailments are recognised immediately, but past service cost is recognised over the vesting period. Because the Board has tentatively decided to require immediate recognition of unvested past service costs, the reason in paragraph 36(c) falls away and the distinction between past service cost and curtailments is no longer necessary. Therefore, past service cost will include amounts attributed to past service resulting from plan amendments to both past and future service and would be recognised immediately.

38. The first part of the definition of curtailments is more problematic, because employee turnover is an actuarial assumption, and any changes to that assumption are usually accounted for as actuarial gains and losses. One view is that the significant reduction in the number of employees covered by a plan results from employees leaving the plan before they had been expected to in previous measurements of cost, and is therefore more like an actuarial gain or loss. The other view is that the significant reduction in the number of employees covered by a plan result from the entity reducing benefits for future service by those employees to zero, and is therefore more like past service cost, since the entity is reducing the benefits offered and should be accounted for in the same way as a partial reduction of those benefits through a plan amendment.

39. The Board can consider the following approaches to the part (a) of the definition of curtailments (the significant reduction in the number of employees covered by a plan):

    (a) retain part (a) as currently defined in IAS 19, or

    (b) remove part (a) of the definition of curtailments (which, together with the result noted in paragraph 37, will result in the removal of the definition of curtailments in its entirety).

40. Supporters of the first approach argue that, because the distinction between past service cost and actuarial gains or losses is not clear cut, the definition of curtailments assists entities in determining whether a reduction in the number of employees covered by a plan is a plan amendment or an actuarial gain or loss. If a reduction is judged to be significant, then it is accounted for separately from past service cost and actuarial gains and losses as a curtailment, and if not significant it is an actuarial gain or loss. If part (a) of the definition is removed, there will be no guidance to differentiate between the closure of a plan to all employees (which is closer to a plan amendment) and increase in turnover (which is closer to an actuarial gain or loss).

41. Supporters of the second approach argue that part (a) of the curtailments definition requires entities to judge whether a reduction in the number of

employees covered by a plan is 'significant' and accounted for as a curtailment, or, if not significant, whether a reduction in the number of employees covered by a plan should be accounted for as an actuarial gain or loss or a past service cost. Removing the requirement to account for a 'significant' reduction as a curtailment will still require entities to judge whether any change in plan membership is a plan amendment or an actuarial gain or loss.

42. Some believe that a curtailment is different from an actuarial gain or loss because it results from an action of the entity, however there are other actuarial assumptions that an entity may influence but are accounted for as an actuarial gain or loss. Actuarial assumptions do not distinguish between the effect of choices made by the entity and choices made by the employee. As noted by one respondent:

> Examples of actions that an entity can take that could affect the experience of the plan but are not currently considered a plan change include whether to grant a pay increase to a participant and whether to dismiss a participant for cause. A workforce reduction decision is similar to these examples and that it is more consistent with a settlement decision than a decision to change the benefits offered by the plan.

43. The staff agrees with the views supporting the approach to retain part (a) (a significant reduction in the number of employees covered by a plan) of the definition of curtailments.

Question 1 (Refer Figure 4 in Appendix A)
Does the Board agree to retain part (a) (a significant reduction in the number of employees covered by a plan) and to remove part (b) (an amendment to benefits for future service) of the definition of curtailments? If not, does the Board agree to remove the definition of curtailments altogether?

Settlements (Refer Figure 3 in Appendix A and Table 3 in Appendix B)

44. Settlement gains or losses arise when an entity settles its employee benefit obligation with its employees, or a third party, for an amount that differs from the IAS 19 measurement. This gain or loss might reflect various amounts, such as a profit margin, an amendment to the benefits or differences between actuarial assumptions used by the entity and the counterparty in the settlement transaction.

45. The ED proposed that gains and losses on all settlements should be included as part of remeasurements. However, the ED distinguished between routine and non-routine settlements for the purposes of disclosure to provide users with information about settlements that are not in accordance with the terms of the plan. Non-routine settlements were defined in the ED as:

> 7 A *non-routine settlement* is a transaction (other than routine payment of benefits to, or on behalf of, employees) that eliminates all further legal or constructive obligations for part or all of the benefits provided under a defined benefit plan.

46. Paragraph BC78 explains that non-routine settlements exclude benefit options envisaged by the terms of the plan. If both routine and non-routine settlements are presented as part of remeasurements, it eliminates the need to differentiate between the two for presentation purposes. However, some respondents requested that the definition should be amended to clarify that non-routine settlement excludes benefits envisaged in the terms of the plan, as explained in paragraph BC78. The staff agrees with this clarification.

47. Some interpret the definition of settlements as overlapping with the definitions of past service cost and curtailments. In the event of a transaction which closes a plan and eliminates all further legal or constructive obligations, the transaction may meet the definition of past service cost, a curtailment and a settlement because the definitions are not mutually exclusive. For example, if an entity negotiates a lump sum to be paid out in connection with the closure of a defined benefit plan, one view is that the entire change in the defined benefit obligation is a settlement because the lump sum eliminates all further legal and

constructive obligations, the other view is that the effect of elimination of future pay growth and earlier payout than expected is a curtailment, and the conversion of the benefits to a lump sum is a plan amendment, with the settlement occurring when the payment is made.

48. It is not clear whether there is an overlap in the definitions (because the definitions are not defined exclusive of one another) or whether it is just difficult to distinguish the effect of a curtailment from the effect of a settlement when they occur together. However, it would be necessary for entities to be able to distinguish the gain or loss on settlement from any past service cost or gain or loss on curtailment if they are required to include amounts relating to each in different components of defined benefit cost.

49. The perceived overlap could be eliminated by either requiring any past service cost or curtailment to be determined before a related settlement, or by amending the definition of a settlement to exclude past service cost and curtailments, with both approaches achieving a similar outcome (ie in the case of a settlement and a curtailment occuring together, both approaches would result in the curtailment effect being determined first).

50. US GAAP does not distinguish between the effect of curtailments and settlements when they are recognised at the same time. Paragraphs 712-30-35-74 to 712-30-35-78 note that:

> 35-74 A settlement and a curtailment may occur separately or together.
>
> 35-75 This Subsection does not establish a proper sequence of events to follow in measuring the effects of a settlement and a curtailment that are to be recognized at the same time. Although the sequence selected can affect the determination of the aggregate gain or loss recognized, the selection of the event to be measured first (settlement or curtailment) is an arbitrary decision and neither order is demonstrably superior to the other. However, an employer shall consistently apply the same sequence of events in determining the effects of all settlements and curtailments that are to be recognized at the same time.
>
> 35-76 If benefits to be accumulated in future periods are reduced (for example, because half of a work force is dismissed or

a plant is closed) but the plan remains in existence and continues to pay benefits, to invest assets, and to receive contributions, a curtailment has occurred but not a settlement.

35-77 If an employer purchases nonparticipating annuity contracts for vested benefits and continues to provide defined benefits for future service, either in the same plan or in a successor plan, a settlement has occurred but not a curtailment.

35-78 If a plan is terminated (that is, the obligation is settled and the plan ceases to exist) and not replaced by a successor defined benefit plan, both a settlement and a curtailment have occurred (whether or not the employees continue to work for the employer). See Example 1 (paragraph 715-30-55-198) for an illustration of this situation.

51. Even if the definition of settlements is amended to exclude past service cost and curtailments, it may still be difficult to distinguish between these items if they occur together. For example, in the case of an entity negotiating a lump sum settlement of a defined benefit plan with its employees, unless the items are specifically identified it may be difficult to determine whether any gain or loss represents a profit margin, the use of different actuarial assumptions or changes in the benefits.

52. In addition, addressing the concerns respondents have regarding distinguishing past service cost and the effect of curtailments from the effect of settlements will not address concerns respondents have regarding presenting the effect of one separately from the other, since a curtailment or plan amendment gain (which would be presented in profit or loss as proposed by the ED) would not be offset by a settlement loss (which would be presented as a remeasurement in OCI as proposed by the ED). The presentation of these transactions is discussed further in paragraphs 56 – 67.

Interaction with termination benefits and restructuring transactions

53. Further layers can be added to the figures in Appendix A to illustrate the interaction of termination benefits and restructurings. It is possible for past

service cost, curtailments and settlements to occur together with either a related termination benefits and/or a restructuring. This has implications for the:

(a) timing of recognition of these items,

(b) presenting or disclosing the components separately (because they may offset each other if they occur in the same transaction), and

(c) distinguishing the effect of each for the purposes of the above.

54. The staff will present the timing of recognition of past service cost, curtailments and settlements together with the interaction with the timing of recognition of termination benefits and restructuring at the January Board meeting.

55. The staff notes that US GAAP contains limited requirements for distinguishing curtailments and termination benefits. Paragraph 712-30-35-95 notes that if a situation also involves termination benefits, the change in the projected benefit obligation due to the curtailment is the difference between the projected benefit obligation for the respective employees before their acceptance of the offer of termination benefits and the projected benefit obligation determined for those employees by applying the normal pension plan formula and assuming no future service because of their termination.

Question 2 (Refer Figure 4 in Appendix A)
Does the Board agree to amend the definition of settlements to exclude curtailments and plan amendments that result in past service cost? Does the Board agree to amend the definition of non-routine settlements to exclude benefits envisaged in the terms of the plan (routine settlements)? If not, what does the Board propose and why?

Presentation

56. This section addresses in which component of defined benefit cost past service cost and the gain or loss on curtailment and settlement should be included.

57. This section considers three alternatives:

    (a) Confirming the proposals in the ED – The ED proposed that past service cost and a gain or loss on curtailment should be included in the service cost component and a gain or loss on settlement should be included in the remeasurements component (Refer figure 5 in Appendix A).

    (b) Retaining the requirements in IAS 19 – This would require past service cost and any gain or loss on curtailment or non-routine settlement to be included in the service cost component and any gain or loss on routine settlement to be included in remeasurements. This, in effect draws a line between non-routine settlements and routine settlements (ie routine settlements are what existing IAS 19 would consider to be benefit payments in accordance with the terms of the plan) (Refer figure 6 in Appendix A).

    (c) Remeasurements approach – requiring the effect of settlements, curtailment and plan amendments to be presented in the remeasurements component.

Confirming the proposals in the ED

58. Including gains and losses on all settlements as remeasurements would not require a distinction to be made between routine and non-routine settlements (the distinction can be made for the purposes of disclosure as in the ED). However, this approach will require gains and losses on settlements to be distinguished from gains and losses on curtailments and past service cost.

59. As discussed above, the definitions of past service cost, curtailments and settlements are perceived to overlap to some degree and often occur at the same

time, therefore distinguishing the effect of each may not always be straightforward.

60. Respondents' concerns about the overlapping definitions of past service cost, curtailments and settlements could be addressed by excluding past service cost and curtailments from settlements as recommended in Question 2. If the Board agrees, the IAS 19 liability is remeasured before the transaction, any past service cost or gain or loss on curtailment is determined and then the effect of settling the resulting obligation is calculated.

61. Confirming the proposals in the ED would not address the concerns of respondents that past service cost and a gain on curtailment will be presented in profit or loss, and an offsetting loss on settlement of the obligation will be presented in OCI. However, in the case of an entity settling an obligation with its employees, requiring any past service cost and curtailment to be determined first might result in no gain or loss being recognized on settlement with the employees. This is because converting the benefit to a lump-sum payment to employees could be interpreted as amending the terms of the existing plan. However, as noted previously, it may be difficult to determine whether an amount arises due to a plan amendment (past service cost) or differences in actuarial assumptions used.

Retaining the existing requirements in IAS 19

62. Retaining the existing requirements in IAS 19 and presenting past service cost and gains and losses arising from non-routine settlements and curtailments and as part of the service cost component would not require a distinction to be made between those transactions for the purposes of presentation (however distinguishing between these amounts could be required for disclosure; refer paragraphs 68 – 70). This would also be consistent with presenting the amounts from other related transactions such as termination benefits and restructuring in profit or loss.

63. However a distinction would have to be made between routine and non-routine settlements because a gain or loss on a non-routine settlement will be presented

in the service cost component, and a gain or loss on a routine settlement will be presented in remeasurements. Respondents appeared less concerned about making this distinction than one between curtailments and settlements, perhaps because this is closest to the current accounting. The Board could clarify that a routine settlement is a payment of benefits in accordance with the terms of the plan (including when the terms provide members with benefit payment options) as recommended in Question 2.

Remeasurements approach

64. The remeasurement approach will not require a distinction to be made between past service cost, curtailments, settlements or actuarial gains and losses. The gains and losses arising from all of these transactions would be presented together in the remeasurements component.

65. Presenting the effects of plan changes in the remeasurements component can be justified on the basis that, while the amounts provide users with information about the uncertainty of future cash flow, plan changes provide less information about the amount and timing of future cash flow than current service cost. This will have the effect of limiting the service cost component to current service cost only, and would maintain the Board's conclusion that amounts with different predictive value should be presented separately. The remeasurements approach will eliminate the requirement to distinguish between past service cost, the effects of curtailments and settlements, and actuarial gains and losses for the purpose of presentation (however the distinction may be required for the purpose of disclosure).

66. However, concerns with the remeasurement approach include:

    (a) presenting the result of an entity's action as a remeasurement.

    (b) a plan change (such as a reduction in work force) might be part of a related transaction for which the gain or loss is presented in profit or loss, including:

        (i) the disposal of other assets or operating segments,

(ii) a termination benefit; or

(iii) a restructuring.

Staff recommendation (refer Figure 6 and 7 in Appendix A)

67. The staff agrees with the views of the majority of respondents and recommends that the Board retains requirements similar to current IAS 19, ie requires past service cost and gains and losses on non-routine settlements and curtailments to be presented in the service cost component and gains and losses on routine settlements to be presented in the remeasurements components.

Question 3 (refer Figure 6 and 7 in Appendix A)
Does the Board agree to require that past service cost and gains and losses on non-routine settlements and curtailments amendments are presented in the service cost component Does the Board agree to require routine settlements to be presented in the remeasurements component?

Disclosure

68. Most respondents agreed with the disclosure of any past service cost, curtailment and non-routine settlement. However some were concerned that the proposed disclosure requirements would be excessive and should be required only if material or significant to the financial statements.

69. The staff agrees with the suggestions that distinguishing between past service cost, curtailments and settlements should not be required for the purposes of disclosure if they occur simultaneously and are presented together and recommends that the Board clarify this in the proposed disclosure requirement.

70. The staff will consider further drafting suggestions when drafting the final amendment.

Question 4
Does the Board agree to confirm the disclosure requirement proposed in the ED for past service cost, curtailments and settlements but amended to not require distinguishing between these items if they occur together and are presented in the same component? If not, what does the Board propose and why?

Appendix A – Figures referred to in the staff analysis

This appendix contains figures illustrating the various changes that can affect the defined benefit obligation.

NOTE: These diagrams should to be printed in colour

A1. The purpose of the figures is to illustrate the possible overlaps and edge effects of the definitions. The distinction between the definitions of actuarial gains and past service cost, curtailments and settlements is important if these changes are required to be presented or disclosed separately.

A2. Because the figures attempt to show the interactions between numerous sets of changes in the defined benefit obligation, which could be complex to display, the figures introduce each set one at a time.

A3. This appendix includes the following figures:

Definitions

(a) Figure 1 – Overlap between actuarial gains and losses and past service cost

(b) Figure 2 – Add curtailments to Figure 1

(c) Figure 3 – Add settlements to Figure 2

(d) Figure 4 – Result of staff recommendations

Presentation

(e) Figure 5 – Add proposed presentation requirements in the ED to Figure 3

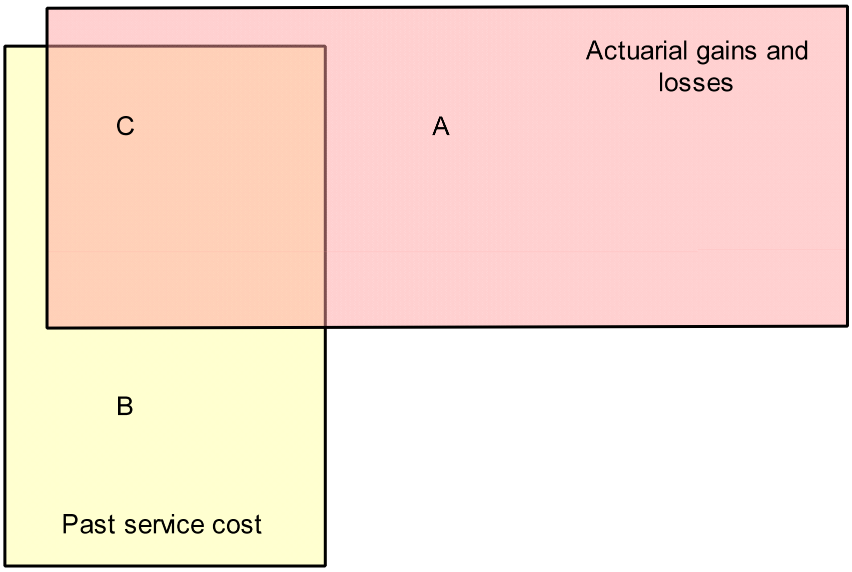
(f) Figure 6 – Add presentation requirements based on current IAS 19 to Figure 3

(g) Figure 7 – Add recommended presentation requirements to Figure 4

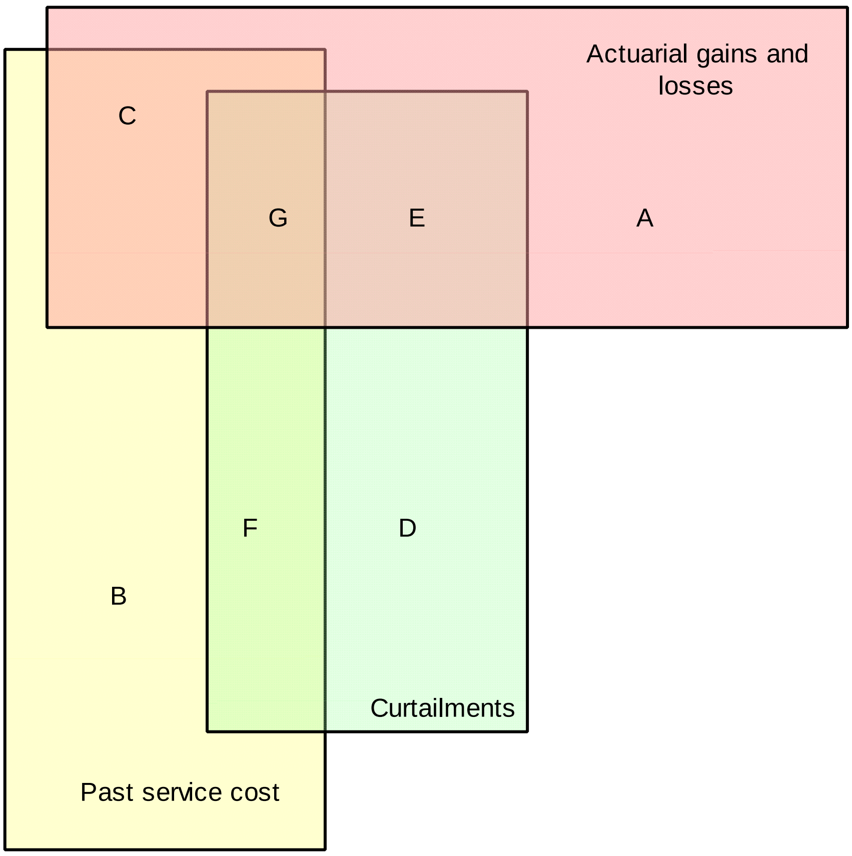
A4. Appendix B contains tables with comments and examples that further explain Figures 1 to 3.

Definitions

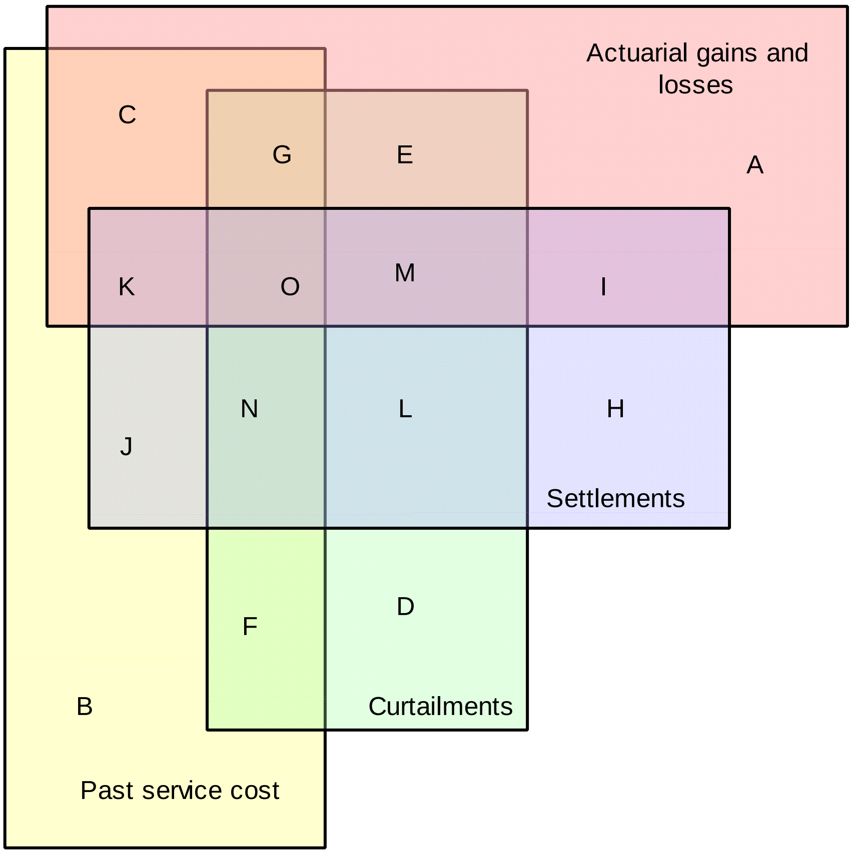
A5. Figure 1 - Overlap between actuarial gains and losses and past service cost (refer Table 1 in Appendix B)



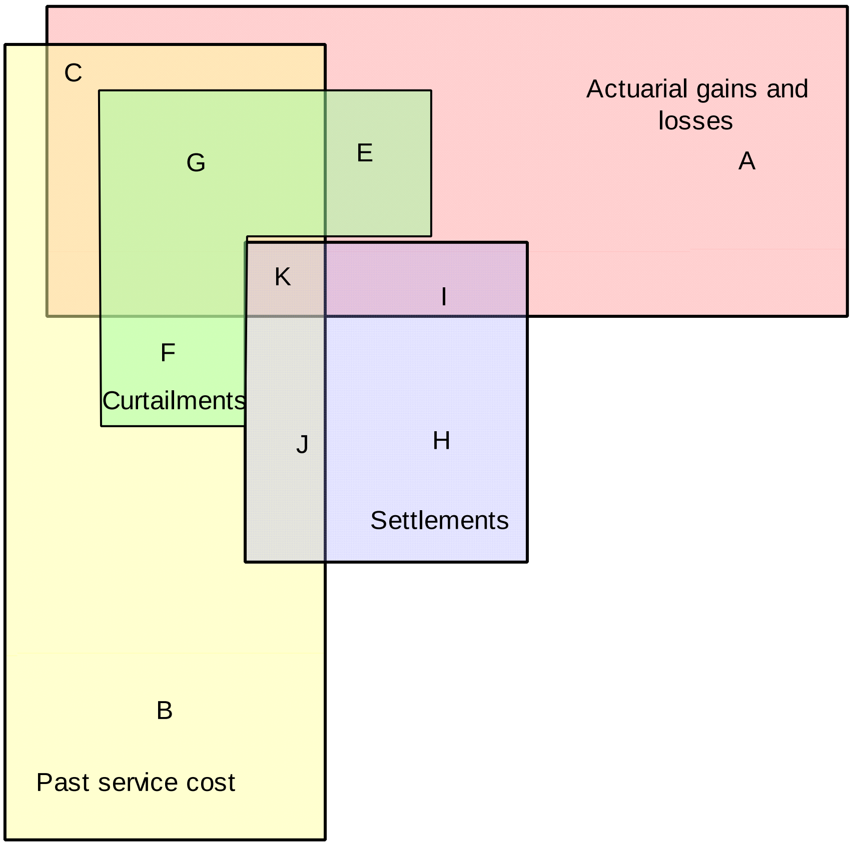
A6. Figure 2 - Add curtailments to Figure 1 (refer Table 2 in Appendix B)



A7. Figure 3 - Add settlements to Figure 2 (refer Table 3 in Appendix B)



A8. Figure 4 – Staff recommendation for definitions

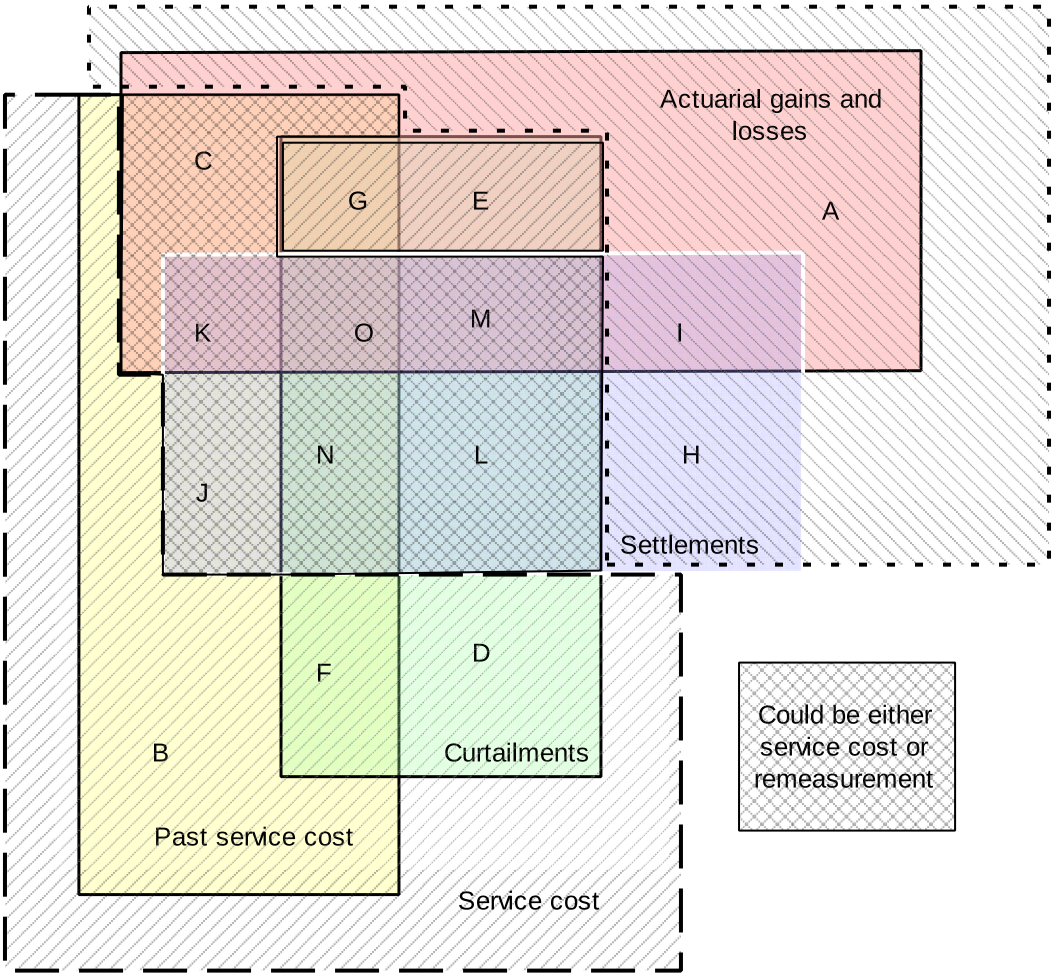


A9. Staff recommendation (paragraph 43): Remove part (b) of curtailments definition – eliminates segment D from Figures 2 and 3 relating to plan amendments to future service. Curtailments are just a subset of past service cost and actuarial gains and losses, that relate to a significant reduction in the number of employees covered by a plan.

A10. Staff recommendation (paragraph 49): Exclude plan amendments and curtailments from definition of settlements – eliminates segments L, M, N and O from Figure 3. However, segments K and J will remain because it may be difficult to distinguish between a past service cost and a gain or loss on settlement if the transactions occur at the same time.

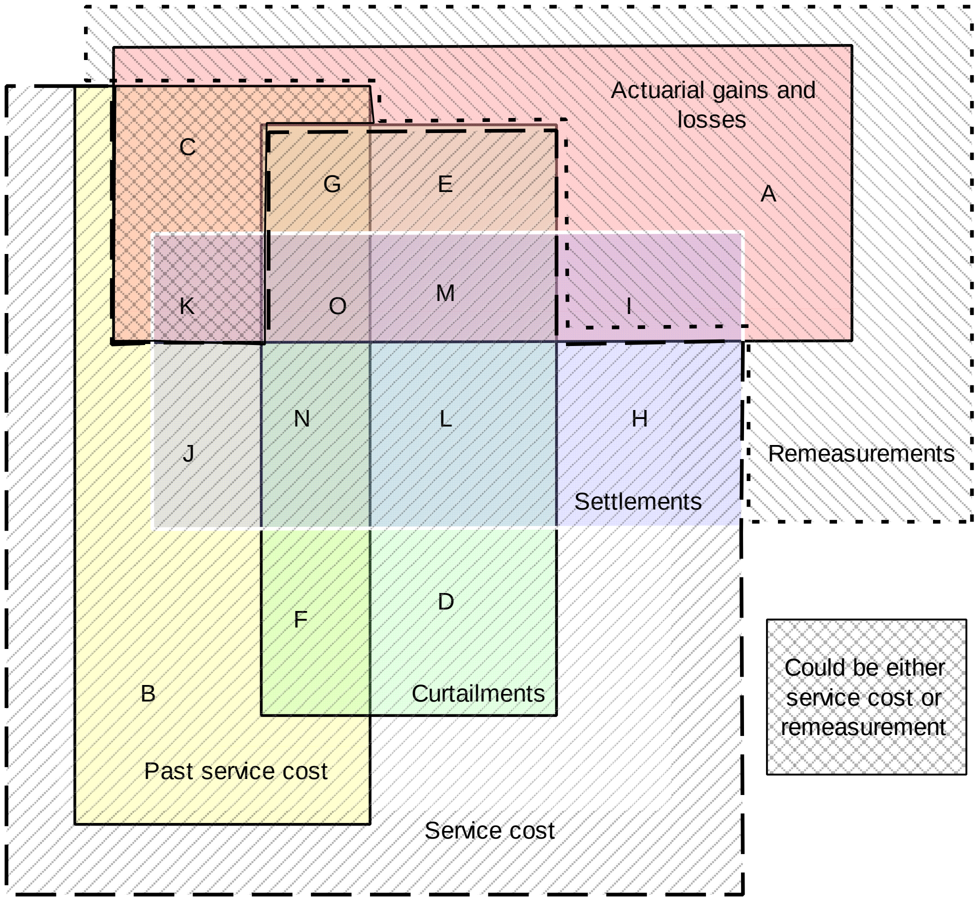
Presentation

A11. Figure 5 – Add proposed presentation requirements in the ED to Figure 3



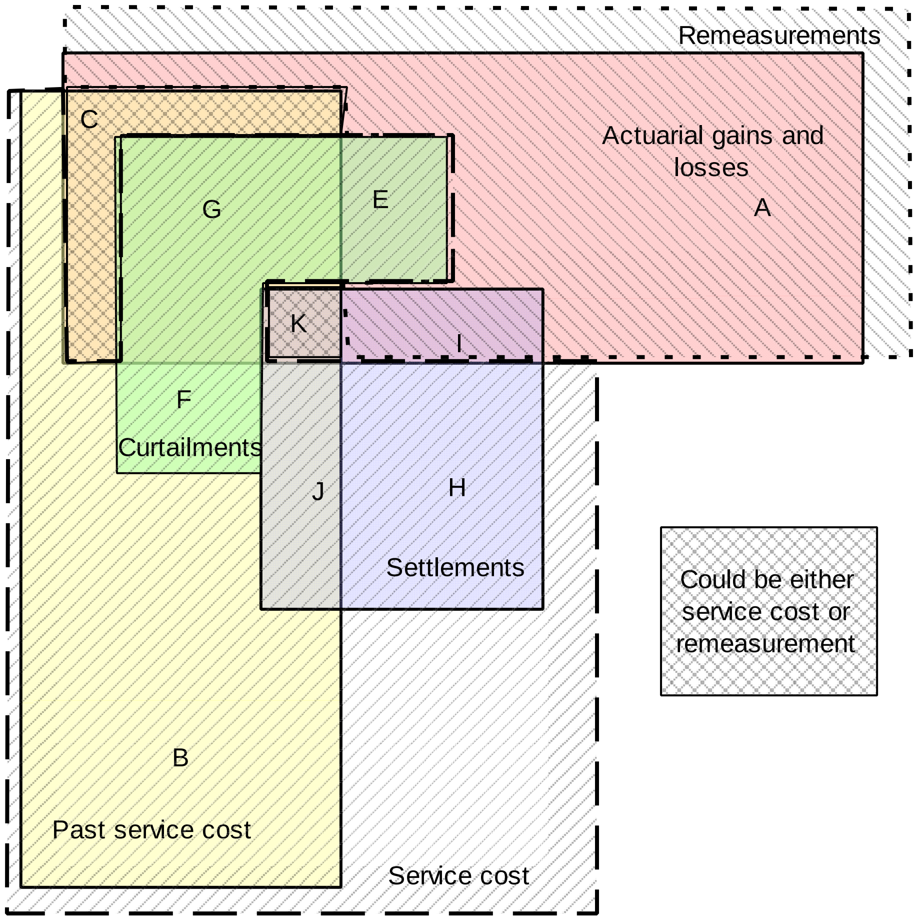
Component	**Changes included**	**Segments**
Service cost	Past service cost and curtailments	B, D, E, F, G
Remeasurements	Actuarial gains and losses and settlements	A, H, I
Service cost or remeasurements	The overlap of settlements with past service cost and curtailments (and difficulty separating when they occur together) may lead to differing interpretations for segments L,M,N,O.	C, J, K, L, M, N, O

A12. Figure 6 – Add presentation requirements based on current IAS 19 to Figure 3



Component	Changes included	Segments
Service cost	Past service cost, curtailments and *non-routine* settlements	B, D, E, F, G, H, J, L, M, N, O
Remeasurements	Actuarial gains and losses and *routine* settlements	A, I
Service cost or remeasurements	Edge effect of splitting settlements (K) - whether a settlement is routine or non-routine (ie identifying whether a gain or loss on settlement with an employee is an amendment or differences in actuarial assumptions used).	C, K

A13. Figure 7 – Add recommended presentation requirements to Figure 4



A14. Same outcome as Figure 6, ie only A and I are in remeasurements and C and K can be either remeasurements or service cost, depending on interpretation of whether a settlement is routine or non-routine.

Appendix B – Tables associated with Figures in Appendix A

A15. This appendix includes the following tables that further explain the figures in Appendix A:

(a) Table 1 – Further explanation of Figure 1 in Appendix A

(b) Table 2 – Further explanation of Figure 2 in Appendix A

(c) Table 3 – Further explanation of Figure 3 in Appendix A

A16. Table 1 – Further explanation of Figure 1 in Appendix A

Segment	**Comments**	**Example**
A	Period to period changes in actuarial assumptions used to measure the obligation	Increase in staff turnover or change in estimate of final salary
B	Plan amendments resulting in change to benefits for past service.	Reduce percentage for final salary benefit (could be reduced to nil)
C = Actuarial gains and losses ∩ past service cost	Overlap or difficulty distinguishing a transaction that results in both past service cost and actuarial gains and losses.	A reduction in the number of employees covered by a plan due to plan closure. Is this more like: (a) an increase in turnover (A)? or (b) a reduction in benefits (B)?

A17. Table 2 – Further explanation of Figure 2 in Appendix A

Segment	Comments	Example
D	Plan amendments resulting in change to benefits for future service (Part (b) of the definition of curtailments). This is not recognised because it does not affect past service cost, only future service cost.	Reduce benefits for future service.
E, F & G	Subsets of past service cost and actuarial gains and losses that represent a **significant** reduction in the number of employees covered by a plan (Part (a) of the definition of curtailments)	A **significant** reduction in the number of employees covered by a plan due to plan closure. Is this more like: (a) an increase in turnover (E)? or (b) a reduction in benefits (F)?
C	Overlap in Figure 1 (C) will remain for reduction in the number of employees covered by a plan that is **not significant**.	A **not significant** reduction in the number of employees covered by a plan due to plan closure. Is this more like: (a) an increase in turnover (A)? or (b) a reduction in benefits (B)?

A18. Table 3 – Further explanation of Figure 3

Segment	Comments	Example
H	Represents a gain or loss that is in addition to IAS 19 measurement (ie the settlement includes an amount that is not included as part of the defined benefit obligation) (Also refer L below)	Profit margin on transfer of liability to third party in a *non-routine* settlement
I = Actuarial gain or loss ∩ Settlement	Represents a settlement in accordance with the terms of the plan	A *routine* settlement
J = Past service cost ∩ Settlement	Represents a settlement accompanied with a plan amendment	A lump sum settlement of a pension (where lump sum settlement was not previously an option under the terms of the plan).
K = Settlement ∩ Actuarial gain or loss ∩ Past service cost	Represents a settlement where it is not clear whether the gain or loss is a result of a plan amendment or changes in assumptions because they occur together and it is difficult to differentiate between the various effects.	The gain or loss on a lump sum settlement with a employees could represent: (a) a risk margin (b) different actuarial assumptions being used by the employees but the benefits are the same (c) an amendment to the benefits

L = Settlement ∩ Curtailment	Represents a settlement accompanied with amendment to future service.	The settlement amount including compensation for the elimination of benefits for future service.
M = Actuarial gain or loss ∩ Settlement ∩ Curtailment	Same as I but now the plan covers significantly fewer employees than before the settlement.	Same as I but accompanied with plan closure (ie there is a reduction in the defined benefit obligation due to elimination of future service, however benefits for prior service are paid out in accordance with the terms of the plan)
N= Past service cost ∩ Settlement ∩ Curtailment	Same as J but the plan now covers significantly fewer employees than before the settlement.	Same as J but accompanied with plan closure (ie there is a reduction in the defined benefit obligation due to elimination of future service, and benefits for prior service are amended as part of the settlement)
O= Actuarial gain or loss ∩ Past service cost ∩ Settlement ∩ Curtailment	A combined transaction that includes elements of all changes.	Settlement of an entire plan for an amount that is different to the defined benefit obligation, so there will be elements of: (a) changes in benefits for past service (b) elimination of future service (c) other changes in assumptions