STAFF PAPER

12–13 November 2013

IFRS Interpretations Committee Meeting

Project	**IAS 19 *Employee Benefits***
Paper topic	Cover note—Employee benefit plans with a guaranteed return on contributions or notional contributions

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Introduction

1. This paper provides an overview of the Agenda Papers on the issues related to IAS 19 *Employee Benefits* for the November 2013 meeting of the IFRS Interpretations Committee ('the Interpretations Committee').

2. At the September 2013 meeting, we updated the Interpretations Committee on the alternatives that we were considering for the measurement of benefit promises that fall within the agreed scope.

3. The Interpretations Committee tentatively decided that the approach based on IFRIC Draft Interpretation D9 *Employee Benefit Plans with a Promised Return on Contributions or Notional Contributions* published in 2004 would be the most suitable for the measurement of the employee benefit plans within the agreed scope. The Interpretations Committee also tentatively agreed to reconsider whether benefits with vesting conditions should be within the agreed scope.

4. The Interpretations Committee directed the staff to bring a detailed analysis of the D9 approach to a future meeting.

Structure of the Agenda Papers

5. In response to the request by the Interpretations Committee above, we have prepared a set of papers as follows:

   (a) **Agenda Paper 2A—Scope**

      (i) vesting conditions;

      (ii) demographic risks; and

      (iii) salary risks.

   (b) **Agenda Paper 2B—Distinction of components**

      (i) distinction between non-variable and variable components; and

      (ii) appendix A—analysis of how the proposed distinction is applied to various types of benefit promises.

   (c) **Agenda Paper 2C—Recognition and measurement**

      (i) non-variable components;

      (ii) variable components; and

      (iii) 'higher of' options.

Appendix A—Previous discussions

Scope

6. In September 2012, the Interpretations Committee tentatively decided that employee benefit plans should fall within the scope of its work if they have the following characteristics:

   (a) the plans would be classified as defined contribution plans under IAS 19 *Employee Benefits* (or would be defined contribution plans if they were funded by actual rather than notional contributions) if not for the guarantee provided by the employer on the return of the contributions made;

   (b) the contributions made to the plans can be notional contributions (ie whether the plans are funded or not should not affect the basis of accounting for these plans);

   (c) there should be a guarantee of return by the employer on the contributions (notional contributions) made;

   (d) the benefit under the plans should not be dependent on future events (for example, salary changes, vesting or demographic risk); and

   (e) the guarantee under the plan may be based on the value of one or more underlying assets.

7. The Interpretations Committee also tentatively decided that an employee post-employment benefit plan, or other employee long-term benefits, would fall within the scope of the Draft Interpretation if the employer has a legal or constructive obligation to pay further contributions, and the fund does not hold sufficient assets to cover all employee benefits relating to employee service in the current and prior periods in respect of:

   (a) a promised return on contributions, actual or notional; or

   (b) any other guarantee on contributions, actual or notional, based on the value of one or more underlying assets.

8. In July 2013, the Interpretations Committee observed that the agreed scope might be broader than it had envisaged because promises such as some current salary and career average promises would be included. However, in the light of the ongoing concerns about how to account for employee benefit plans with a guaranteed return on contributions or notional contributions, and the resulting diversity in practice, the Interpretations Committee tentatively decided to proceed with this project on the basis of the agreed scope

Measurement

9. In November 2012, the Interpretations Committee discussed how to address the measurement of the so-called 'higher of' option. The higher-of option relates to when the employee is guaranteed the higher of two or more possible outcomes. For example, the employer may promise the employee the higher of a fixed return of four per cent and the actual return on the contributions.

10. The Interpretations Committee tentatively decided that an entity should measure the higher-of option at its intrinsic value at the reporting date. It also considered the accounting and presentation for the higher-of option but did not make a decision on the issue.

11. In November 2012, the Interpretations Committee also asked the staff to prepare examples illustrating how the proposed measurement approaches would apply to different employee benefit plan designs. The staff will bring examples applying the proposed measurement approach to a future meeting.

IASB discussions before the 2008 Discussion Paper

12. In 2006, the IASB added a project to its agenda to revise IAS 19 *Employee Benefits*, including the accounting for 'cash balance' and similar plans. Consequently the Interpretations Committee (known as the IFRIC at the time) transferred its work on D9 to the IASB. At the time, D9 had already been exposed for comment and a number of issues had arisen that the Interpretations Committee had begun to discuss.

13. The evolution of the D9 approach to the fair value measurement approach ultimately published in the 2008 DP occurred over several IASB meetings from May 2006 right up to just before the DP was published in March 2008. We are not going to repeat the detail of those discussions in these papers. However we think it would be helpful if the Interpretations Committee was aware of the issues that the IASB encountered when it attempted to move ahead with the D9 approach. The Interpretations Committee would either have to address these issues, or accept them as a consequence of the approach.

14. Areas of the D9 approach that the IASB found troublesome included:

    (a) the distinction between fixed and variable returns;

    (b) difficulties in separating some benefits into a fixed element and a variable element, particularly for benefits that promise a variable return plus a fixed return and when the promise switches between different types of returns over time;

    (c) concerns that the intrinsic value of any guarantee or options (for example, 'higher of' options) would not faithfully represent the benefit promise; and

    (d) how to account for credit risk.

15. The IASB also noted the tension between the attribution requirements for defined contribution plans and defined benefit plans. Specifically, the attribution of defined contribution plans does not consider back-end loading features (such as when the percentage contribution of salary increases with service). Therefore, the IASB found it difficult to reconcile the attribution of the variable component and the fixed component of D9 plans.