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STAFF PAPER

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IASB Meeting

Project	**Availability of a refund (Amendments to IFRIC 14)**		
Paper topic	Update and next steps		
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Introduction and purpose

1. The International Accounting Standards Board (Board) proposed amendments to IFRIC 14 *IAS 19 —The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*. Those proposals, if finalised, would clarify how an entity assesses its right to a refund of a surplus in a defined benefit plan when other parties (for example, trustees) have particular rights. At a previous meeting, the Board decided to perform further work before proceeding to finalise the proposed amendments. That work would help assess whether a more principles-based approach than that currently in IFRIC 14 could be developed for an entity to assess the availability of a refund of a surplus.

2. This paper:

   (a) provides the Board with an update on the project; and

   (b) asks the Board whether it agrees with our recommendation not to finalise the proposed amendments to IFRIC 14 at this time.

Structure of the paper

3. This paper is structured as follows:

   (a) background:

      (i) existing requirements in IFRIC 14;

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(ii) the proposed amendments to IFRIC 14 and Board redeliberations;

(iii) effect of proposed paragraph 12A on defined benefit plans in the UK; and

(iv) why the Board decided to consider developing a more principles-based approach.

(b) next steps

(i) finalising the proposed amendments to IFRIC 14; or

(ii) a wider-scope project on IFRIC 14.

(c) staff recommendation.

4. This paper includes two appendices:

(a) Appendix A—Paragraphs 11–14 of IFRIC 14.

(b) Appendix B— Interaction of asset ceiling requirements and minimum funding requirements.

Background

Existing requirements in IFRIC 14

5. Paragraph 64 of IAS 19 *Employee Benefits* requires an entity to measure the net defined benefit asset at the lower of (a) the surplus in the defined benefit plan; and (b) the asset ceiling. Paragraph 8 of IAS 19 defines the asset ceiling as 'the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan'.

6. Paragraph 11 of IFRIC 14 specifies that an entity has economic benefits available in the form of a refund only if it has an unconditional right to a refund either:

(a) during the life of the plan without assuming that plan liabilities must be settled to obtain a refund;

(b) assuming gradual settlement of plan liabilities over time; or

(c) assuming full settlement of plan liabilities in a single event.

7. If an entity assumes gradual settlement of plan liabilities (paragraph 11(b) of IFRIC 14), it measures the economic benefits available in the form of a refund applying paragraph 13 of IFRIC 14. If an entity assumes full settlement of plan liabilities (paragraph 11(c) of IFRIC 14), it measures those economic benefits applying paragraph 14. The measurement of economic benefits available in the form of a refund applying paragraph 14 (assuming full settlement) could be significantly lower than that determined applying paragraph 13 (assuming gradual settlement). This is because paragraph 14 of IFRIC 14 requires an entity to include the costs to the plan of settling plan liabilities (including, for example, the cost of purchasing annuities to settle plan liabilities).

8. Appendix A to this paper reproduces paragraphs 11–14 of IFRIC 14.

The proposed amendments to IFRIC 14 and Board redeliberations

9. The proposed amendments to IFRIC 14 would clarify, among other things, an entity's right to a refund of a surplus when other parties (for example, trustees) have particular rights. The proposed amendments would clarify that:

   (a) an entity does not have a right to a refund if other parties can use the surplus to affect benefits for plan members without the entity's consent (proposed paragraph 12B of IFRIC 14). When developing the proposed amendments, the Board concluded that the other parties' rights restrict the entity's ability to use the surplus to generate future cash inflows for the entity.

   (b) an entity has a right to a refund if other parties can wind up a plan (or otherwise fully settle plan liabilities in a single event) without an entity's consent. However, in recognising and measuring this right, the entity would be unable to assume gradual settlement of plan liabilities over time (proposed paragraph 12A of IFRIC 14). When developing the proposed amendments, the Board concluded that the other parties can prevent gradual settlement if those parties can wind up the plan before all members have left it.

   In many cases, unless paragraph 11(a) of IFRIC 14 applies, this means that an entity would recognise and measure its right to a refund applying

paragraphs 11(c) and 14 of IFRIC 14 (ie assuming full settlement of plan liabilities in a single event). As discussed above in paragraph 7, this would mean including settlement costs in the measurement of the entity's right to a refund.

(c) other parties' rights to unilaterally change the asset mix within a plan—without affecting benefits for plan members—does not affect an entity's right to a refund (proposed paragraph 12C of IFRIC 14). When developing the proposed amendments, the Board concluded that, in this case, the other parties' rights relate to the future amount of plan assets and not to the entity's right to a refund.

10. The Board considered feedback on the proposed amendments and, at its December 2016 meeting, tentatively decided to finalise those proposed amendments subject to some drafting changes.

Effect of proposed paragraph 12A on defined benefit plans in the UK

11. As explained in paragraph 9(b) of this paper, proposed paragraph 12A of IFRIC 14 would clarify that an entity has a right to a refund of a surplus even if other parties can wind up a plan (or otherwise fully settle plan liabilities in a single event) without an entity's consent. However, in measuring this right, the entity would be unable to assume gradual settlement of plan liabilities over time as described in paragraph 11(b) of IFRIC 14.

12. This amendment, if finalised, would be expected to mainly affect defined benefit plans in the United Kingdom (UK)[1]. We understand that trustees generally do not have the right to legally wind-up a defined benefit plan in the UK without an entity's consent. A legal wind-up (also referred to as a Section 75 wind-up) would trigger a requirement for an entity to fund any deficit that may exist on wind-up. Nonetheless, trustees generally have the right to settle plan liabilities for individual plan members or groups of individual plan members without an entity's consent if the settlement is 'reasonable'. Although 'reasonable' is not defined, we understand that trustees can

[1] Outreach on this matter confirmed that proposed paragraph 12A would not have a significant effect in jurisdictions outside the UK.

initiate this type of partial settlement if plan members would not be worse off as a result of the settlement. We also understand that trustees generally do not need to obtain consent from plan members to initiate a settlement. Accordingly, trustees could exercise this right to settle plan liabilities for all plan members in a single event and, therefore, plans with such characteristics would be within the scope of proposed paragraph 12A. This would be the case even if the plan had insufficient funding to allow full settlement of all plan liabilities in a single event, which we understand is often the case in the current economic environment.

13. We also understand that entities with these plans have generally assumed gradual settlement of plan liabilities over time when recognising and measuring their right to a refund. However, applying proposed paragraph 12A these entities would no longer be able to make that assumption. This could result in significantly lower net defined benefit assets because of the requirement to include settlement costs in measuring the right to a refund. In some situations, an entity may also have an obligation to pay contributions under a minimum funding requirement to cover an existing shortfall in respect of services already received (MFR contribution). The reduction in the asset ceiling caused by the application of paragraph 11(c) of IFRIC 14 might also result in some portion of the MFR contribution not being recoverable once paid. If this is the case, the entity may have to recognise an additional liability for the portion of the MFR contribution that it cannot recover. Appendix B to this paper summarises the interaction of the asset ceiling requirements and the MFR contribution requirements.

Why the Board decided to explore developing a more principles-based approach

14. IFRIC 14 requires an entity to include settlement costs in measuring its right to a refund only when the entity assumes full settlement of plan liabilities in a single event. In all other situations, an entity does not include settlement costs in that measurement.

15. Proposed paragraph 12A would not change this requirement but would clarify that an entity assumes full settlement when other parties have the right to fully settle plan liabilities in a single event without the entity's consent. If, however, other parties had the right to settle only a portion of plan liabilities—or the right to settle all plan

liabilities but not in a single event—proposed paragraph 12A would not be applicable and the entity would not include settlement costs in measuring its right to a refund.

16. For example, assume a situation in which a defined benefit plan has both active and retired members[2]. If the trustees of the plan were able to settle plan liabilities for all members (active and retired) in a single event, proposed paragraph 12A would clarify that the entity includes settlement costs in measuring its right to a refund—this is because the entity would be required to assume full settlement in measuring that right. However, if the trustees were able to settle plan liabilities only for retired members (and not for active members), proposed paragraph 12A would not apply. The entity would therefore measure its right to a refund excluding settlement costs. This is despite the fact that the trustees could force the entity to settle plan liabilities for all retired members.

17. Given the bright-line nature of the existing requirements in paragraphs 11–14 of IFRIC 14, we understand that it would be possible (and potentially desirable) for entities to make non-substantive changes to plan agreements to avoid the effects of the proposed amendments. For example, an entity could amend plan agreements so that trustees would continue to have the right to settle all plan liabilities but not in a single event. Alternatively, plan agreements could be amended so that trustees would be able to settle most, but not all, plan liabilities in a single event. In these situations, the trustees would no longer have the right to settle *all* plan liabilities in a *single* event and, as a consequence, proposed paragraph 12A would not apply. The entity would continue to assume gradual settlement of plan liabilities in recognising and measuring its right to a refund. Because in the current economic environment plans often have insufficient funds to settle all plan liabilities in a single event, we understand that it might be relatively easy to get agreement on the changes necessary to avoid the effects of the proposed amendments.

18. Our work on the availability of a refund has identified that the existing requirements in paragraphs 11–14 of IFRIC 14 create a rather arbitrary line between substantively different measurements of an entity's right to a refund of a surplus—ie if other parties can settle *all* plan liabilities in a *single* event, then the measurement of an entity's

[2] In this example, we assume that the entity does not have a right to a refund during the life of the plan (ie paragraph 11(a) of IFRIC 14 does not apply).

right to a refund *includes* settlement costs; in any other situation, that measurement *excludes* settlement costs. For this reason, the Board asked us to consider whether a more principles-based approach could be developed with respect to the availability of a refund.

Next steps

Finalising the proposed amendments to IFRIC 14

19. In the light of the information presented above, we first considered whether the Board should finalise the proposed amendments to IFRIC 14.

Proposed paragraph 12A

20. With respect to the clarification proposed in paragraph 12A of IFRIC 14, we see little benefit in finalising the proposed amendment. That amendment, if finalised, would lead to consistent outcomes for defined benefit plans with the same terms and conditions. However, the ability to make non-substantive changes to those terms and conditions (as described above in paragraphs 14-18) would, in turn, reduce much of the expected benefits of that amendment.

Other aspects of the proposed amendments to IFRIC 14

21. We also see little benefit in finalising the other aspects of the proposed amendments—as described in paragraphs 9(a) and 9(c) of this paper—without also finalising proposed paragraph 12A of IFRIC 14.

22. The original submission to the IFRS Interpretations Committee (Committee) asked about the effect of other parties' rights on an entity's assessment of its right to a refund. In its discussions, the Board (and the Committee) concluded that different rights can affect an entity's assessment differently and this was reflected in the proposed amendments to IFRIC 14 (as described in paragraph 9). The proposed amendments were exposed as a package and we think the expected benefits of finalising these amendments in piecemeal fashion would not justify the costs of standard-setting. We also understand that any diversity in practice in respect of proposed paragraphs 12B and 12C are limited. This is because:

(a) proposed paragraph 12B would clarify that an entity does not have a right to a refund of a surplus if other parties can use the surplus to affect the benefits for plan members without the entity's consent. Our original outreach on this matter indicated that trustees (or other parties) do not generally have such rights.

(b) proposed paragraph 12C would clarify that other parties' rights to unilaterally change the asset mix within a plan—without affecting benefits for plan members—does not affect an entity's right to a refund of a surplus. We understand that the trustees of some plans have such rights (for example, the right to purchase annuities as part of plan assets)—however, informal outreach suggests that entities already treat such rights as proposed in paragraph 12C.

23. Accordingly, we recommend that the Board not finalise the proposed amendments to IFRIC 14.

A wider-scope project on IFRIC 14

24. Based on initial staff research, we think it is possible for the Board to develop a more principles-based approach to address the measurement of a right to a refund of a surplus, without reconsidering more broadly the measurement requirements in IAS 19. Such an approach could focus on removing the bright-line distinction between paragraph 11(b) and 11(c) of IFRIC 14 (ie when an entity assumes gradual settlement of plan liabilities over time and when it assumes full settlement of plan liabilities in a single event).

25. We think this could be done, for example, by specifying that in measuring its right to a refund, an entity assumes gradual settlement of plan liabilities over time only *to the extent* it has a right to gradually settle those plan liabilities over time. Unless paragraph 11(a) of IFRIC 14 applies, an entity would otherwise assume full settlement of any remaining plan liabilities.

26. Using the example in paragraph 16 of this paper to illustrate, if trustees have the right to settle plan liabilities for all retired members but not active members, an entity would:

   (a) assume full settlement of plan liabilities for retired members—the entity would then include settlement costs related to plan liabilities for retired members in measuring its right to a refund; and

   (b) assume gradual settlement of plan liabilities over time only for active members.

27. That said, we think developing such an approach:

   (a) would require considerable time and effort (of both the Board and stakeholders). At this stage, we have not tested the possible approach with stakeholders to assess the expected costs and benefits. We know the outcome would be lower net defined benefit assets for some plans, and possibly increased defined benefit liabilities for entities with MFR contribution obligations. There are also other aspects of the requirements in IFRIC 14 that this approach would not address but which some may view as requiring amendment at the same time (for example, differing treatments for settling plan liabilities and purchasing annuities as plan assets; IFRIC 14 has an asset impairment test but no liability adequacy test—see Appendix B for further information); and

   (b) would be broader in scope than the proposed narrow-scope amendments to IFRIC 14. We therefore think any possible amendments that might arise from such a project would require exposure for comment and would be likely to affect more defined benefit plans than were previously in the scope of the proposed amendments.

28. At this stage, we do not have enough information to assess whether such a project would be more or less of a priority for the Board than other projects currently on the Board's research pipeline. The Board has started its 2020 Agenda Consultation and expects to publish a Request for Information (RFI) in the second half of 2020. We think the 2020 Agenda Consultation provides stakeholders with an opportunity to inform the Board about whether it should undertake a project on IFRIC 14 (along the lines of that described in paragraph 24 of this paper). Accordingly, we think the

Board could consider referring to a project on IFRIC 14 as a potential project in its RFI. Such a project could focus on making the distinction between paragraph 11(b) and 11(c) of IFRIC 14 more principles-based than the existing requirements in IFRIC 14.

Staff recommendation

29. We recommend that the Board not finalise the proposed amendments to IFRIC 14.

30. We think the Board could consider referring to a project on IFRIC 14 as a potential project in the RFI to its 2020 Agenda Consultation.

Question for the Board
Does the Board agree with our recommendation not to finalise the proposed amendments to IFRIC 14?

Appendix A—Excerpts from IFRIC 14

A1. This appendix reproduces paragraphs 11–14 of IFRIC 14 for ease of reference.

The right to a refund

11 A refund is available to an entity only if the entity has an unconditional right to a refund:

(a) during the life of the plan, without assuming that the plan liabilities must be settled in order to obtain the refund (eg in some jurisdictions, the entity may have a right to a refund during the life of the plan, irrespective of whether the plan liabilities are settled); or

(b) assuming the gradual settlement of the plan liabilities over time until all members have left the plan; or

(c) assuming the full settlement of the plan liabilities in a single event (ie as a plan wind-up).

An unconditional right to a refund can exist whatever the funding level of a plan at the end of the reporting period.

12 If the entity's right to a refund of a surplus depends on the occurrence or non-occurrence of one or more uncertain future events not wholly within its control, the entity does not have an unconditional right and shall not recognise an asset.

Measurement of the economic benefit

13 An entity shall measure the economic benefit available as a refund as the amount of the surplus at the end of the reporting period (being the fair value of the plan assets less the present value of the defined benefit obligation) that the entity has a right to receive as a refund, less any associated costs. For instance, if a refund would be subject to a tax other than income tax, an entity shall measure the amount of the refund net of the tax.

14 In measuring the amount of a refund available when the plan is wound up (paragraph 11(c)), an entity shall include the costs to the plan of settling the plan liabilities and making the refund. For example, an entity shall deduct professional fees if these are paid by the plan rather than the entity, and the costs of any insurance premiums that may be required to secure the liability on wind-up.

Appendix B—Interaction of asset ceiling requirements and MFR

B1. MFR contributions do not generally affect the measurement of a defined benefit asset or liability. This is because the MFR contributions, once paid, will become plan assets and therefore the additional net liability is nil (explained in paragraph 3 of IFRIC 14). However, the requirement to make MFR contributions could give rise to a liability if the IAS 19 surplus generated by those contributions will be unavailable to the entity once paid.

B2. If the plan is in a surplus position applying IAS 19 (ie if the fair value of plan assets is more than the defined benefit obligation)—or would be once the entity has paid any MFR contribution—an entity assesses whether it can recognise an asset for its right to a refund or its right to a reduction in future contributions. To the extent the surplus arising from an MFR contribution will be unavailable after it is paid into the plan, an entity recognises a liability for that portion of the contribution—this is because that portion represents an obligation for past services received.

B3. To illustrate, assume a plan—applying IAS 19—has a surplus of CU5,000. The entity is required to make an MFR contribution of CU3,000. This contribution, once paid, would increase the surplus to CU8,000. If any portion of that additional CU3,000 would be unavailable to the entity once paid, the entity recognises an additional liability for that portion.

B4. Similarly, assume a plan has a deficit—applying IAS 19—of CU3,000. The entity would not generally consider the asset ceiling requirements in IFRIC 14 because the plan has no surplus. However, if the entity were required to make an MFR contribution of CU5,000, this contribution, once paid, would result in a surplus of CU2,000. The entity is therefore required to assess whether any portion of that anticipated surplus of CU2,000 would be unavailable to the entity once paid. If this is the case, then the entity would recognise that portion as an additional liability.

B5. However, assume a plan has a deficit—applying IAS 19—of CU3,000. The entity is required to make an MFR contribution of CU2,000. This contribution would result in a deficit of CU1,000 once paid. Because the contribution would not create a surplus, the entity is not required to consider the effect of the asset ceiling. It would not recognise any additional liability for the MFR contribution.

B6. In other words, IFRIC 14 requires an entity to determine whether an MFR contribution would be available to the entity if that MFR contribution would create or increase a surplus—ie the entity anticipates any non-recoverability of a future asset that would result from paying the MFR contribution. However, to the extent the payment of a future contribution would not create a surplus, the entity is not required to consider the effect of any restrictions on the entity's ability to reduce an existing deficit by making the MFR contribution. This is because IAS 19 and IFRIC 14 are not symmetrical in their treatment of assets and liabilities—there is an asset impairment test (the asset ceiling), but no liability adequacy test.