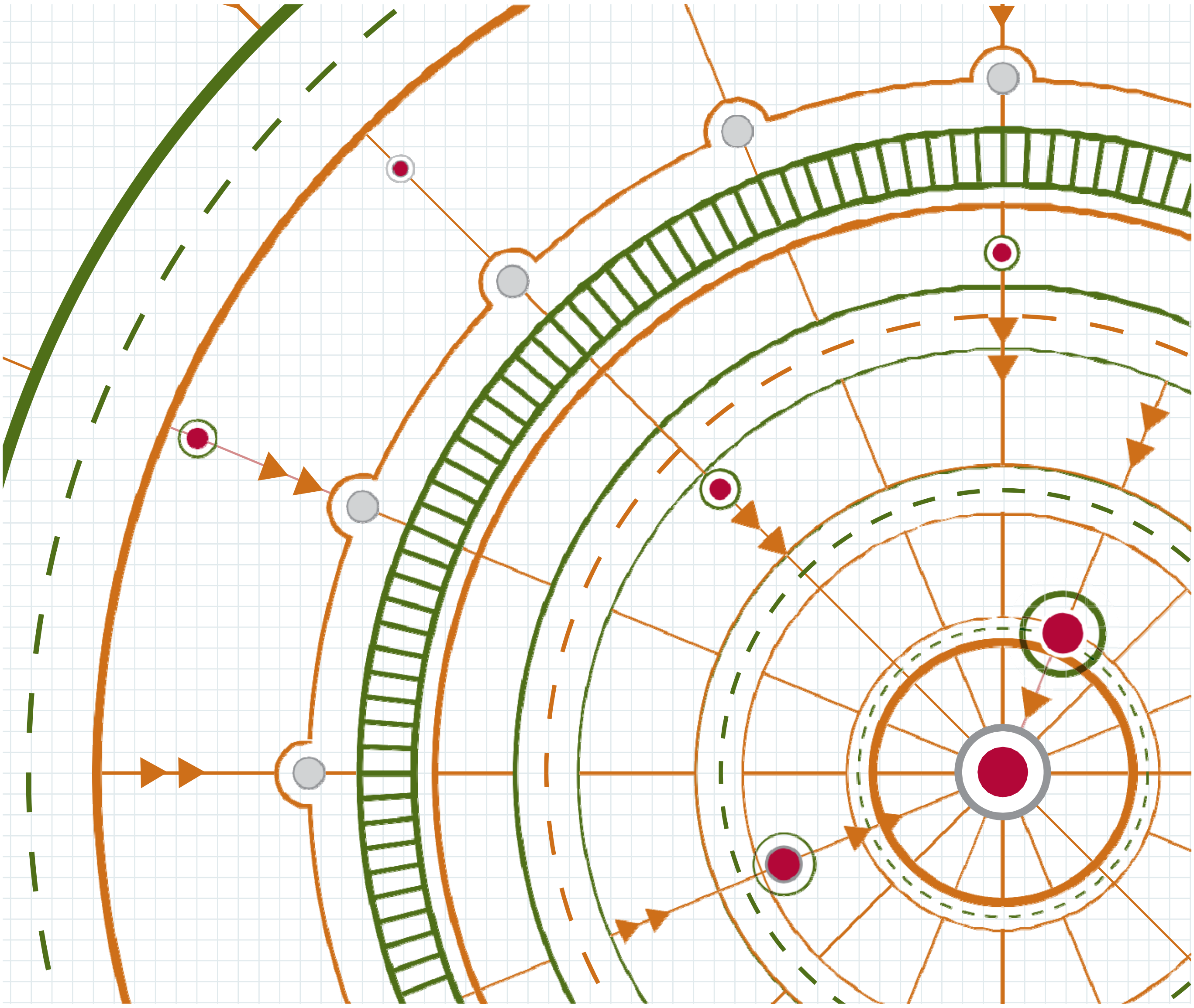
IFRS for SMEs® Standard (2015) + Q&As

IFRS® Foundation—Supporting Material for the *IFRS for SMEs* Standard

Module 28—Employee Benefits



IFRS® Foundation Supporting Material for the *IFRS for SMEs*® Standard

including the full text of
Section 28 *Employee Benefits*
of the *IFRS for SMEs* Standard
issued by the International Accounting Standards Board in October 2015

with extensive explanations, self-assessment questions and case studies

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This module has been prepared by IFRS Foundation (Foundation) education staff. It has not been approved by the International Accounting Standards Board (Board). The module is designed to assist users of the *IFRS for SMEs*® Standard (Standard) to implement and consistently apply the Standard.

Contents

Module 28—Employee Benefits

The accounting requirements applicable to small and medium-sized entities (SMEs) discussed in this module are set out in the *IFRS for SMEs* Standard, issued by the International Accounting Standards Board (Board) in October 2015.
This module has been prepared by IFRS Foundation education staff.
The contents of Section 28 *Employment Benefits* of the *IFRS for SMEs* Standard are set out in this module and shaded grey. The Glossary of terms of the *IFRS for SMEs* Standard (Glossary) is also part of the requirements. Terms defined in the Glossary are reproduced in **bold type** the first time they appear in the text of Section 28. The notes and examples inserted by the education staff are not shaded. These notes and examples do not form part of the *IFRS for SMEs* Standard and have not been approved by the Board.

INTRODUCTION

Which version of the *IFRS for SMEs*® Standard?

When the *IFRS for SMEs* Standard was first issued in July 2009, the Board said it would undertake an initial comprehensive review of the Standard to assess entities' experience of the first two years of its application and to consider the need for any amendments. To this end, in June 2012, the Board issued a Request for Information: *Comprehensive Review of the IFRS for SMEs*. An Exposure Draft proposing amendments to the *IFRS for SMEs* Standard was subsequently published in 2013, and in May 2015 the Board issued *2015 Amendments to the IFRS for SMEs* Standard.

The document published in May 2015 only included amended text, but in October 2015, the Board issued a fully revised edition of the Standard, which incorporated additional minor editorial amendments as well as the substantive May 2015 revisions. This module is based on that version.

The *IFRS for SMEs* Standard issued in October 2015 is effective for annual periods beginning on or after 1 January 2017. Earlier application was permitted, but an entity that did so was required to disclose the fact.

Any reference in this module to the *IFRS for SMEs* Standard refers to the version issued in October 2015.

This module

This module focuses on the general requirements to account for employee benefits applying Section 28 *Employee Benefits* of the *IFRS for SMEs* Standard. It introduces the subject and reproduces the official text along with explanatory notes and examples designed to enhance understanding of the requirements. The module identifies the significant judgements required in accounting for employee benefits. In addition, the module includes questions designed to test your understanding of the requirements and case studies that provide a practical opportunity to apply the requirements to account for employee benefits applying the *IFRS for SMEs* Standard.

Upon successful completion of this module, you should, within the context of the *IFRS for SMEs* Standard, be able to:

- identify four types of employee benefits accounted for applying Section 28—short-term employee benefits, post-employment benefits, other long-term employee benefits and termination benefits;

- identify when and how to recognise the cost of employee benefits;
- measure employee benefits;
- present and disclose employee benefits in financial statements; and
- demonstrate an understanding of the significant judgements that are required in accounting for employee benefits.

IFRS for SMEs Standard

The *IFRS for SMEs* Standard is intended to apply to the general purpose financial statements of entities that do not have public accountability (see Section 1 *Small and Medium-sized Entities*).

The *IFRS for SMEs* Standard is comprised of mandatory requirements and other non-mandatory material.

The non-mandatory material includes:

- a preface, which provides a general introduction to the *IFRS for SMEs* Standard and explains its purpose, structure and authority;
- implementation guidance, which includes illustrative financial statements and a table of presentation and disclosure requirements;
- the Basis for Conclusions, which summarises the Board's main considerations in reaching its conclusions in the *IFRS for SMEs* Standard issued in 2009 and, separately, in the 2015 Amendments; and
- the dissenting opinion of a Board member who did not agree with the issue of the *IFRS for SMEs* Standard in 2009 and the dissenting opinion of a Board member who did not agree with the 2015 Amendments.

In the *IFRS for SMEs* Standard, Appendix A: Effective date and transition, and Appendix B: Glossary of terms, are part of the mandatory requirements.

In the *IFRS for SMEs* Standard, there are appendices to Section 21 *Provisions and Contingencies*, Section 22 *Liabilities and Equity* and Section 23 *Revenue.* These appendices provide non-mandatory guidance.

The *IFRS for SMEs* Standard has been issued in two parts: Part A contains the preface, all the mandatory material and the appendices to Section 21, Section 22 and Section 23; and Part B contains the remainder of the material mentioned above.

Further, the SME Implementation Group (SMEIG), which assists the Board with supporting implementation of the *IFRS for SMEs* Standard, publishes implementation guidance as 'questions and answers' (Q&As). These Q&As provide non-mandatory, timely guidance on specific accounting questions raised with the SMEIG by entities implementing the *IFRS for SMEs* Standard and other interested parties. At the time of issue of this module (January 2019) the SMEIG has not issued any Q&As relevant to this module.

Module 28—Employee Benefits

Introduction to the requirements

The objective of general purpose financial statements of a small or medium-sized entity is to provide information about the entity's financial position, performance and cash flows that is useful for economic decision-making by a broad range of users who are not in a position to demand reports tailored to meet their particular information needs. Such users include, for example, owners who are not involved in managing the business, existing and potential creditors and credit rating agencies.

The objective of Section 28 is to set out the accounting treatment for employee benefits (other than share-based payments that are accounted for applying the requirements of Section 26 *Share-based Payment*), so that users of the financial statements have information about the cost of and obligations for an entity's employee benefits.

Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees, including management and directors. An entity recognises as an expense the cost of all employee benefits to which its employees have become entitled as a result of service rendered to the entity in the current or past periods, unless another section of this IFRS requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

Obligations for short-term employee benefits are measured at undiscounted amounts. Liabilities for obligations under post-employment defined benefit plans and other long-term employee benefits are measured by subtracting the fair value at the reporting date of plan assets (if any) from the present value of its obligations under defined benefit plans (or other long-term employee benefit scheme) at the reporting date. Obligations to pay termination benefits are measured at the best estimate of the expenditure that would be required to settle the obligation at the reporting date.

The section also specifies disclosures for employee benefits.

What has changed since the 2009 *IFRS for SMEs* Standard?

The 2015 Amendments made the following main changes to Section 28:

- clarifying the application of the accounting requirements in paragraph 28.23 to other long-term employee benefits (see paragraph 28.30); and
- removing the requirement to disclose the accounting policy for termination benefits (see paragraph 28.43).

The 2015 amendments also made consequential changes to paragraph 28.41(c) clarifying guidance on the undue cost or effort exemption in Section 2 *Concepts and Pervasive Principles*.

Module 28—Employee Benefits

REQUIREMENTS AND EXAMPLES

Scope of this section

28.1 **Employee benefits** are all forms of consideration given by an entity in exchange for service rendered by employees, including directors and management. This section applies to all employee benefits, except for **share-based payment transactions**, which are covered by Section 26 *Share-based Payment*. Employee benefits covered by this section will be one of the following four types:

(a) short-term employee benefits, which are employee benefits (other than **termination benefits**) that are wholly due within twelve months after the end of the period in which the employees render the related service;

(b) **post-employment benefits**, which are employee benefits (other than termination benefits) that are payable after the completion of employment;

(c) other long-term employee benefits, which are employee benefits (other than post-employment benefits and termination benefits) that are not wholly due within twelve months after the end of the period in which the employees render the related service; and

(d) termination benefits, which are employee benefits payable as a result of either:

(i) an entity's decision to terminate an employee's employment before the normal retirement date; or

(ii) an employee's decision to accept voluntary redundancy in exchange for those benefits.

Notes

Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees. It includes benefits provided to either employees or their dependants and may be settled by payments (or the provision of goods or services) directly to the employees; or to their spouses, children or other dependants; or to others, such as insurance companies. An employee may provide services to an entity on a full-time, part-time, permanent, casual or temporary basis. In this section, employees include directors and other management personnel.

28.2 Employee benefits also include share-based payment transactions by which employees receive **equity** instruments (such as shares or share options) or **cash** or other **assets** of the entity in amounts that are based on the price of the entity's shares or other equity instruments of the entity. An entity shall apply Section 26 in accounting for share-based payment transactions.

Module 28—Employee Benefits

General recognition principle for all employee benefits

28.3 An entity shall recognise the cost of all employee benefits to which its employees have become entitled as a result of service rendered to the entity during the **reporting period**:

(a) as a **liability**, after deducting amounts that have been paid either directly to the employees or as a contribution to an employee benefit fund. If the amount paid exceeds the obligation arising from service before the **reporting date**, an entity shall recognise that excess as an asset to the extent that the prepayment will lead to a reduction in future payments or a cash refund.

(b) as an **expense**, unless another section of this Standard requires the cost to be recognised as part of the cost of an asset such as **inventories** or **property, plant and equipment**.

Examples–general recognition principle for employee benefits

Ex 1 **On 1 January 20X2, an entity paid one of its employees CU1,000[1] for work performed in manufacturing the entity's goods in December 20X1. All goods manufactured by the employee in December were sold to the entity's customers by 31 December 20X1.**

At 31 December 20X1, the entity recognises a liability of CU1,000 (accrual of employee benefits) for the amount due to the employee. This amount would be recognised as an expense (part of cost of goods sold—see Section 13 *Inventories* paragraphs 13.5, 13.8 and 13.20).

Ex 2 **The facts are the same as in Example 1. However, in this example, the goods manufactured in December were in the entity's inventories at 31 December 20X1.**

At 31 December 20X1, the entity recognises a liability (accrual of employee benefits) to recognise the amount due to the employee and an asset (cost of inventories) of CU1,000 to recognise the work performed.

Ex 3 **The facts are the same as in Example 1 above. However, in this example, the employee manufactured an item of equipment for use by the entity in the manufacture of goods in future periods.**

At 31 December 20X1, the entity recognises the amount due to the employee as a liability of CU1,000 (accrual of employee benefits). That amount is also included in the cost of the equipment (an asset) applying paragraph 17.10(b) rather than included in profit or loss in the period of construction.

Note: The amount of the employee benefit included in the cost of the asset will be recognised in profit or loss as depreciation expense over the useful life of the asset, or as an impairment loss, or in arriving at the gain or loss on derecognition of the item of equipment (see Section 17 *Property, Plant and Equipment*). Depreciation of manufacturing equipment will generally be added to the cost of the inventories produced (see Section 13). The cost of the inventories produced will be recognised in profit or loss when the related revenue is recognised.

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[1] In this example, and in all other examples in this module, monetary amounts are denominated in 'currency units (CU)'.

Module 28—Employee Benefits

Short-term employee benefits

Examples

28.4 Short-term employee benefits generally include items such as:

(a) wages, salaries and social security contributions;

(b) short-term compensated absences (such as paid annual leave and paid sick leave) when the absences are expected to occur within twelve months after the end of the period in which the employees render the related employee service;

(c) profit-sharing and bonuses payable within twelve months after the end of the period in which the employees render the related service; and

(d) non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees.

Notes

Accounting for short-term employee benefits is less complicated than long-term benefits because no actuarial assumptions are required to measure the obligation or the cost. Moreover, short-term employee benefit obligations are measured at their undiscounted amounts (see paragraph 28.5).

Examples–short-term employee benefits

Ex 4 **On 31 December 20X1, a retailer paid its employees CU1,000,000 (after withholding CU400,000 of taxes deducted from the employees' remuneration and paid by the retailer on behalf of the employees to the tax authorities) for work performed in December 20X1. On 1 January 20X2, the entity paid to the government the CU400,000 deducted from its employees' remuneration.**

On 2 January 20X2, the retailer paid a further CU20,000 to the tax authority. This tax is an obligation of the retailer and is calculated based on its December 20X1 payroll.

In December 20X1 the retailer incurred CU1,400,000 in short-term employee benefits (CU1,000,000 paid to employees and CU400,000 paid on behalf of its employees to the tax authorities).

The CU20,000 payroll tax levied directly on the retailer is not an employee benefit—it is not consideration given by the entity in exchange for services rendered by its employees.

The retailer could record the following journal entry:

31 December 20X1

Dr Profit or loss	CU1,400,000	
Cr Cash		CU1,000,000
Cr Liability (accrued expense)		CU400,000

To recognise the short-term employee benefits expenses incurred in December 20X1.

Dr Profit or loss	CU20,000	
Cr Liability (accrued expense)		CU20,000

To recognise the payroll tax levied on the entity's for December 20X1.

1 January 20X2

Dr Liability (accrued expense)	CU400,000	
Cr Cash		CU400,000

To recognise the payment to the government of taxes collected on its behalf from the entity's employees accrued in 20X1.

2 January 20X2

Dr Liability (accrued expense)	CU20,000	
Cr Cash		CU20,000

To recognise the settlement of the payroll tax levied on the entity.

Ex 5 **An entity's employees are each entitled to five days of paid sick leave for each year. Unused sick leave is carried forward for one calendar year.**

The sick leave is a short-term employee benefit—the paid absence must occur within 12 months after the end of the period in which the employees render the related employee service.

Ex 6 **A profit-sharing plan requires an entity to pay a specified proportion of its profit for the year to employees who serve throughout the year. This payment must be made within 12 months after the end of the period in which the employees provide the related employee service.**

The profit-sharing plan is a short-term employee benefit—the profit share is due to the employees who served throughout the year within 12 months of the end of the financial reporting period.

Ex 7 **An entity provides its expatriate employees with housing that it rents from independent third parties.**

The expatriate housing scheme is a short-term employee benefit—the housing benefit is due in the period in which the employees render the related employee service.

Examples–not short-term employee benefits

Ex 8 **The facts are the same as in Example 5. However, in this example, unused sick leave is carried forward for three calendar years. Many employees accumulate more than 10 days' unused sick leave.**

The sick leave is not a short-term employee benefit as the paid absence is not due to be paid wholly within 12 months after the end of the period in which the employees render the related employee service. The sick leave is accounted for as other long-term employee benefits (see paragraphs 28.29 and 28.30).

Ex 9 **A profit-sharing plan requires an entity to pay a specified proportion of its cumulative profit for a five-year period to employees who serve throughout the five-year period.**

The profit-sharing plan is not a short-term employee benefit—the profit share is not due wholly within 12 months after the end of the period in which the employees render the related employee service. The profit-sharing plan is accounted for as other long-term employee benefits (see paragraphs 28.29 and 28.30).

Measurement of short-term benefits generally

28.5 When an employee has rendered service to an entity during the reporting period, the entity shall measure the amounts recognised in accordance with paragraph 28.3 at the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service.

Recognition and measurement—short-term compensated absences

28.6 An entity may compensate employees for absence for various reasons including annual vacation leave and sick leave. Some short-term compensated absences accumulate—they can be carried forward and used in future periods if the employee does not use the current period's entitlement in full. Examples include annual vacation leave and sick leave. An entity shall recognise the expected cost of **accumulating compensated absences** when the employees render service that increases their entitlement to future compensated absences. The entity shall measure the expected cost of accumulating compensated absences at the undiscounted additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the end of the reporting period. The entity shall present this amount as a current liability at the reporting date.

Notes

An entity may remunerate employees for absences for various reasons including vacation, sickness and short-term disability, maternity or paternity, jury service and military service. Entitlement to such paid absences are either accumulating (see paragraph 28.6) or non-accumulating (see paragraph 28.7).

Examples–accumulating paid absences

Ex 10 **An entity's employees are each entitled to five days of paid sick leave for each year. Unused sick leave is carried forward for one calendar year. Sick leave is taken first out of any balance brought forward from the previous year and then out of the current year's entitlement, or first-in, first-out (FIFO).**

The entity does not anticipate a future saving due to unused sick leave lapsing.

At 1 January 20X1, the entity's obligation for sick leave (current liability) was measured at CU2,600.

At 31 December 20X1, the entity's sick leave records were as follows:

Employee	*Wage rate (per working day in 20X1)*	*Accumulated sick leave days due on 01/01/20X1*	*Days sick leave earned in 20X1*	*Days sick leave taken in 20X1*	*Percentage wage increase effective from 01/01/20X2*
1	CU400	4.5	5	2	5%
2	CU310	2	5	3	2%
3	CU250	0	5	9	2%
4	CU180	1	5	4.5	6%

At 31 December 20X1, the entity's liability for sick leave is CU3,651 (CU2,100 for employee 1 + CU1,265 for employee 2 + CU286 for employee 4), calculated as follows:

- Employee 1—CU400 current wage rate per working day × 1.05 to recognise the expected increase in salary × 5 (maximum) days due at 31 December 20X1 and expected to be taken in 20X2 = CU2,100.
- Employee 2—CU310 current wage rate per working day × 1.02 to recognise the expected increase in salary × 4 days due at 31 December 20X1 and expected to be taken in 20X2 = CU1,265.
- Employee 3—CU250 current wage rate per working day × 1.02 to recognise the expected increase in salary × 0 days due at 31 December 20X1 = CU0.
- Employee 4—CU180 current wage rate per working day × 1.06 to recognise the expected increase in salary × 1.5 days due at 31 December 20X1 and expected to be taken in 20X2 = CU286.

If the entity has not charged sick leave accrued in 20X0 and taken by employees in 20X1 against the sick leave obligation, then the obligation for sick leave at 31 December 20X1 could be recognised through the following journal entry:

Dr Profit or loss (or assets—see paragraph 28.3(b))	CU1,051[(a)]	
Cr Short-term paid absences (sick leave)		CU1,051

To recognise the increase in accumulating paid absences related to sick leave.

(a) CU3,651 sick leave liability as at 31 December 20X1 less CU2,600 sick leave liability as at 1 January 20X1.

Ex 11 **The facts are the same as in Example 10. However, in this example, the employee receives payment from the entity for sick leave not taken within 12 months after the end of the period in which the employee renders the related service. The entity pays the employee for such unused sick leave on the last day of the year following the year in which the employee rendered the service.**

On 31 December 20X1, the entity pays employee 1 CU1,000 (CU400 wage rate per working day × 2.5 days vested sick leave accrued in 20X0 that was unused at 31 December 20X1).

At 31 December 20X1, the entity's liability for sick leave is CU3,651 (CU2,100 for employee 1 + CU1,265 for employee 2 + CU286 for employee 4).

If the entity has not charged sick leave accrued in 20X0 and taken by employees in 20X1 against the sick leave obligation, the obligation for sick leave at 31 December 20X1 could be recognised through the following journal entries:

31 December 20X1

Dr Short-term paid absences (sick leave)	CU1,000[(a)]	
Cr Cash		CU1,000

To recognise the payment to settle the obligation for sick leave not taken.

Dr Profit or loss (or assets—see paragraph 28.3(b))	CU2,051[(b)]	
Cr Short-term paid absences (sick leave)		CU2,051

To recognise the increase in accumulating paid absences related to sick leave.

(a) CU400 wage rate per working day × 2.5 days vested sick leave accrued in 20X0 that was unused at 31 December 20X1.

(b) CU3,651 sick leave liability as at 31 December 20X1 less CU1,600 (CU2,600 sick leave liability at 1 January 20X1 less CU1,000 settled on 31 December 20X1).

Ex 12 **An entity has 100 employees, who are each entitled to five days of paid sick leave for each year. Unused sick leave is carried forward for one calendar year. Sick leave is taken first out of the current year's entitlement and then out of any balance brought forward from the previous year—or last in, first out. At 30 December 20X1, the average unused entitlement is two days per employee. Based on experience that it projects will continue, the entity expects 92 employees to take no more than five days of paid sick leave in 20X2, and the remaining eight employees will take an average of six and a half days each.**

The entity expects to pay for 12 days of sick pay earned in the prior year, reflecting the unused entitlement accumulated at 31 December 20X1 (one and a half days each, for the eight employees expected to use more than they earned in the current year.) This is calculated as six and a half days of sick leave expected, less 20X2 sick leave entitlement of five days for each of the eight employees. Therefore, the entity recognises a liability equal to 12 days of sick pay.

28.7 An entity shall recognise the cost of other (non-accumulating) compensated absences when the absences occur. The entity shall measure the cost of non-accumulating compensated absences at the undiscounted amount of salaries and wages paid or payable for the period of absence.

Examples–non-accumulating paid absences

Ex 13 **The facts are the same as in Example 10. However, in this example, sick leave cannot be carried forward to the next calendar year.**

At 31 December 20X1, the entity has no liability for sick leave—all unused sick leave lapses at the end of each calendar year.

Ex 14 **The facts are the same as in Example 12. However, in this example, sick leave cannot be carried forward to the next calendar year.**

At 31 December 20X1, the entity has no liability for sick leave—all unused sick leave lapses at the end of each calendar year.

Ex 15 **An entity's employees are each entitled to 25 days' holiday leave per year. Unused holiday leave vests at the end of each calendar year. Employees are paid for all vested holiday leave in the month following the end of a calendar year at the previous year's salary rates.**

At 1 January 20X1, the entity's obligation for holiday leave vested at the end of 20X0 (current liability) was measured at CU2,600.

At 31 December 20X1, the entity's holiday leave records were as follows:

Employee	*Wage rate (per working day in 20X0)*	*Vested holiday leave days on 01/01/20X1*[(a)]	*Days holiday leave taken in 20X1*	*Percentage wage increase effective from 01/01/20X1*
1	CU400	4.5	20	5%
2	CU310	2	22	2%
3	CU250	0	25	2%

4	CU180	1	10	6%

[(a)] Settled in cash on 31/01/20X1.

On 31 January 20X1, the entity pays its employees CU2,600 (CU1,800 for employee 1 + CU620 for employee 2 + CU180 for employee 4) for vested holiday leave.

- Employee 1—CU400 wage rate per working day × 4.5 vested non-accumulating holiday leave at 31 December 20X0 = CU1,800.
- Employee 2—CU310 wage rate per working day × 2 vested non-accumulating holiday leave at 31 December 20X0 = CU620.
- Employee 3—CU250 wage rate per working day × 0 vested non-accumulating holiday leave at 31 December 20X0 = CU0.
- Employee 4—CU180 wage rate per working day × 1 vested non-accumulating holiday leave at 31 December 20X0 = CU180.

On 31 January 20X1, the entity could record the following journal entry for the settlement of its obligation for holiday leave:

Dr Short-term paid absences (holiday leave)	CU2,600	
Cr Cash		CU2,600

To recognise settlement of non-accumulating paid holiday leave.

At 31 December 20X1, the entity's liability for holiday leave is CU5,911 (CU2,100 for employee 1 + CU949 for employee 2 + CU2,862 for employee 4).

- Employee 1—CU400 wage rate per working day × 1.05 to recognise the expected increase in salary × 5 vested non-accumulating holiday leave at 31 December 20X1 = CU2,100.
- Employee 2—CU310 wage rate per working day × 1.02 to recognise the expected increase in salary × 3 vested non-accumulating holiday leave at 31 December 20X1 = CU949.
- Employee 3—CU250 wage rate per working day × 1.02 to recognise the expected increase in salary × 0 vested non-accumulating holiday leave at 31 December 20X1 = CU0.
- Employee 4—CU180 wage rate per working day × 1.06 to recognise the expected increase in salary × 15 vested non-accumulating holiday leave at 31 December 20X1 = CU2,862.

At 31 December 20X1, the entity could record the following journal entry for the accrual of its obligation for holiday leave:

Dr Profit or loss (or assets—see paragraph 28.3(b))	CU5,911	
Cr Short-term paid absences (holiday leave)		CU5,911

To recognise non-accumulating paid holiday leave.

Recognition—profit-sharing and bonus plans

28.8 An entity shall recognise the expected cost of profit-sharing and bonus payments only when:

(a) the entity has a present legal or constructive obligation to make such payments as a result of past events (this means that the entity has no realistic alternative but to make the payments); and

(b) a reliable estimate of the obligation can be made.

Notes

As defined in the Glossary of terms of the *IFRS for SMEs* Standard (Glossary), a constructive obligation is an obligation that derives from an entity's actions when:

(a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept particular responsibilities; and

(b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

Examples–profit-sharing and bonus plans

Ex 16 **A profit-sharing plan requires an entity to pay employees 5% of its profit for the year before profit-sharing bonuses. For the year ended 31 December 20X1 the entity had a profit before profit-sharing bonuses of CU2 million. Bonuses are paid in January.**

At 31 December 20X1, the entity could record the following journal entry for its profit-sharing plan obligation:

Dr Profit or loss (or assets—see paragraph 28.3(b))	CU100,000[(a)]	
Cr Profit-sharing bonuses plan		CU100,000

To recognise the profit-sharing bonuses plan liability.

(a) 5% × CU2,000,000. The amount is not discounted (see paragraph 28.5).

Ex 17 **In 20X1 an entity implemented a profit-sharing plan. The plan requires the entity to pay 3% of its profit before profit-sharing bonuses for the year to employees who serve throughout the current year and who will continue to serve throughout the following year. For the year ended 31 December 20X1 the entity recorded a profit before profit-sharing bonuses of CU1 million. The entity expects to save 10% of the maximum possible bonus payment through staff turnover. The bonus will be paid on 31 December 20X2.**

At 31 December 20X1, the entity could record the following journal entry for its profit-sharing plan obligation:

Dr Profit or loss (or assets—see paragraph 28.3(b))	CU27,000[(a)]	
Cr Profit-sharing bonuses plan		CU27,000

To recognise the profit-sharing bonuses plan liability.

(a) 3% × CU1,000,000 = CU30,000 maximum possible bonus.
CU30,000 less 10% × CU30,000 saving due to staff turnover = CU27,000. The amount is not discounted (see paragraph 28.5).

Post-employment benefits: distinction between defined contribution plans and defined benefit plans

28.9 Post-employment benefits include, for example:

(a) retirement benefits, such as pensions; and

(b) other post-employment benefits, such as post-employment life insurance and post-employment medical care.

Arrangements whereby an entity provides post-employment benefits are **post-employment benefit plans**. An entity shall apply this section to all such arrangements whether or not they involve the establishment of a separate entity to receive contributions and to pay benefits. In some cases, these arrangements are imposed by law instead of by action of the entity. In some cases, these arrangements arise from actions of the entity even in the absence of a formal, documented plan.

28.10 Post-employment benefit plans are classified as either **defined contribution plans** or **defined benefit plans**, depending on their principal terms and conditions:

(a) defined contribution plans are post-employment benefit plans under which an entity pays fixed contributions into a separate entity (a fund) and has no legal or constructive obligation to pay further contributions or to make direct benefit payments to employees if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods. Thus, the amount of the post-employment benefits received by the employee is determined by the amount of contributions paid by an entity (and perhaps also the employee) to a post-employment benefit plan or to an insurer, together with investment returns arising from the contributions.

(b) defined benefit plans are post-employment benefit plans other than defined contribution plans. Under defined benefit plans, the entity's obligation is to provide the agreed benefits to current and former employees, and actuarial risk (that benefits will cost more or less than expected) and investment risk (that returns on assets set aside to fund the benefits will differ from expectations) are borne, in substance, by the entity. If actuarial or investment experience is worse than expected, the entity's obligation may be increased, and vice versa if actuarial or investment experience is better than expected.

Notes

Examples of defined benefit plans—when an entity's obligation is not limited to the amount it agrees to contribute to an employee benefit fund—are when the entity has a legal or constructive obligation through:

(a) a plan benefit formula not linked solely to the amount of contributions.

(a) a guarantee, either directly or indirectly through a plan, of a specified return on contributions.

(a) informal practices that give rise to a constructive obligation. For example, a constructive obligation may arise when an entity has a history of increasing benefits for former employees to keep pace with inflation even where there is no legal obligation to do so.

Multi-employer plans and state plans

28.11 **Multi-employer plans** and state plans are classified as defined contribution plans or defined benefit plans on the basis of the terms of the plan, including any constructive obligation that goes beyond the formal terms. However, if sufficient information is not available to use defined benefit accounting for a multi-employer plan that is a defined benefit plan, an entity shall account for the plan in accordance with paragraph 28.13 as if it was a defined contribution plan and make the disclosures required by paragraph 28.40.

Notes

One example of a defined benefit multi-employer plan is one when:

(a) the plan is financed on a pay-as-you-go basis; contributions are set at a level expected to be sufficient for paying benefits falling due in a single period; and future benefits earned in the current period will be paid out of future contributions.

(b) employees' benefits are determined by the length of their service; the participating entities have no realistic means of withdrawing from the plan without paying a contribution for the benefits earned by employees up to the date of withdrawal. Such a plan creates actuarial risk for the entity; if the ultimate cost of benefits already earned at the end of the reporting period is more than expected, the entity will have to increase its contributions or persuade employees to accept a reduction in benefits. Therefore, such a plan is a defined benefit plan.

Insured benefits

28.12 An entity may pay insurance premiums to fund a post-employment benefit plan. The entity shall treat such a plan as a defined contribution plan unless the entity has a legal or constructive obligation either:

(a) to pay the employee benefits directly when they become due; or

(b) to pay further amounts if the insurer does not pay all future employee benefits relating to employee service in the current and prior periods.

A constructive obligation could arise indirectly through the plan, through the mechanism for setting future premiums, or through a **related party** relationship with the insurer. If the entity retains such a legal or constructive obligation, the entity shall treat the plan as a defined benefit plan.

Post-employment benefits: defined contribution plans

Recognition and measurement

28.13 An entity shall recognise the contribution payable for a period:

(a) as a liability, after deducting any amount already paid. If contribution payments exceed the contribution due for service before the reporting date, an entity shall recognise that excess as an asset.

(b) as an expense, unless another section of this Standard requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

Examples–defined contribution plans

Ex 18 **On 8 January 20X2, a retailer paid CU10,000 contribution to a defined contribution plan in part exchange for services performed by the entity's employees in December 20X1.**

At 31 December 20X1, the retailer must recognise CU10,000 liability (accrual of post-employment benefits for employees' defined contribution plan) and CU10,000 expense in the determination of profit or loss for the year ended 31 December 20X1.

On 31 December 20X1, the retailer could record the following journal entry:

Dr Profit or loss	CU10,000	
Cr Post-employment benefits–defined contribution payable		CU10,000

To recognise the accrual of the post-employment benefits expenses incurred in December.

On 8 January 20X2, the retailer could record the following journal entry:

Dr Post-employment benefits–defined contribution payable	CU10,000	
Cr Cash		CU10,000

To recognise the settlement of defined contribution post-employment benefits plan expense accrued in 20X1.

Ex 19 **The facts are the same as in Example 18. However, in this example, the entity is a manufacturer; the whole CU10,000 is considered direct labour; and the goods manufactured in December were in the entity's inventories at 31 December 20X1.**

At 31 December 20X1, the manufacturer must recognise a liability (accrual of post-employment benefits payable for employees' defined contribution plan) and an asset (inventories) of CU10,000. The inventories will be recognised in profit or loss when impaired or sold (see paragraphs 13.19 and 13.20).

Ex 20 **The facts are the same as in Example 18. However, in this example, the entire cost pertains to employees who manufactured an item of equipment for use by the entity in the manufacture of goods in future periods.**

At 31 December 20X1, the entity must recognise a liability (accrual of post-employment benefits for employees' defined contribution plan) and an asset (property, plant and equipment) of CU10,000. The entity recognises the cost of property, plant and equipment in profit or loss when depreciated (see paragraph 17.17), impaired (see paragraph 17.24) or sold (see paragraph 17.28).

Ex 21 **On 20 December 20X1, a retailer paid a CU10,000 contribution to a defined contribution plan. CU7,800 of that amount is, in part, in exchange for services performed by the entity's employees in December 20X1; the balance of CU2,200 is in respect of services to be performed in 20X2.**

At 31 December 20X1, the retailer must recognise an asset of CU2,200 (prepaid post-employment benefits for employees' defined contribution plan) and CU7,800 staff cost for the year ended 31 December 20X1.
The staff cost is recognised as an expense or as part of the cost of an asset, applying paragraph 28.3(b).

Post-employment benefits: defined benefit plans

Recognition

28.14 In applying the general **recognition** principle in paragraph 28.3 to defined benefit plans, an entity shall recognise:

(a) a liability for its obligations under defined benefit plans net of **plan assets**—its '**defined benefit liability**' (see paragraphs 28.15–28.23); and

(b) recognises the net change in that liability during the period as the cost of its defined benefit plans during the period (see paragraphs 28.24–28.27).

Measurement of the defined benefit liability

28.15 An entity shall measure a defined benefit liability for its obligations under defined benefit plans at the net total of the following amounts:

(a) the **present value** of its obligations under defined benefit plans (its **defined benefit obligation**) at the reporting date (paragraphs 28.16–28.22 provide guidance for measuring this obligation).

(b) minus the **fair value** at the reporting date of plan assets (if any) out of which the obligations are to be settled directly. Paragraphs 11.27–11.32 provide guidance for determining the fair values of those plan assets.

Notes

A defined benefit liability is the present value at the reporting date of the defined benefit obligation that exceeds the fair value at the reporting date of the plan assets (if any) out of which the obligations are to be settled directly.

The present value of the defined benefit obligation is the present value, without deducting any plan assets, of expected future payments required to settle the obligation resulting from employee service in the current and prior periods.

Plan assets are assets held by a long-term employee benefit fund and qualifying insurance policies. Qualifying insurance policies are not defined in the *IFRS for SMEs* Standard. In the absence of guidance in the *IFRS for SMEs* Standard, an entity is permitted (but is not required) to consider the guidance in full IFRS Standards. IAS 19 *Employee Benefits* defines qualifying insurance policies as an insurance policy[2] issued by an insurer that is not a related party (as defined in IAS 24 *Related Party Disclosures*) of the reporting entity, if the proceeds of the policy:

(a) can be used only to pay or fund employee benefits under a defined benefit plan; and

(b) are not available to the reporting entity's own creditors (even in bankruptcy) and cannot be paid to the reporting entity, unless either:

  (i) the proceeds represent surplus assets not needed for the policy to meet all the related employee benefit obligations; or

  (ii) the proceeds are returned to the reporting entity to reimburse it for employee benefits already paid.

For funded defined benefit plans, when the fair value of plan assets at the reporting date exceeds the present value of the plan obligations at the reporting date, the surplus is recognised as an asset if specific conditions are met (see paragraph 28.22).

[2] A qualifying insurance policy is not necessarily an insurance contract, as defined in IFRS 17 *Insurance Contracts*.

Examples–defined benefit plans

Ex 22 **A defined benefit plan provides a monthly pension of 0.2% of final salary for each year of service. The pension is payable from the age of 65. At 31 December 20X1, the present value of the entity's obligations under the plan was measured at CU200,000. Measuring this obligation requires making estimates of several factors including final salaries and mortality (see paragraph 28.16). Furthermore, the fair value of the plan assets out of which the obligations are to be settled directly was determined at CU180,000 as at 31 December 20X1.**

At 31 December 20X1, the entity must recognise a liability (post-employment benefits) of CU20,000 for its defined benefit plan (CU200,000 obligation less CU180,000 plan assets set aside to fund the defined benefit obligation).

Ex 23 **The facts are the same as in Example 22. However, in this example, the entity's obligations for the defined benefit scheme are unfunded.**

At 31 December 20X1, the entity must recognise a liability (post-employment benefits) of CU200,000 for its defined benefit plan.

Inclusion of both vested and unvested benefits

28.16 The present value of an entity's obligations under defined benefit plans at the reporting date shall reflect the estimated amount of benefit that employees have earned in return for their service in the current and prior periods, including benefits that are not yet **vested** (see paragraph 28.26) and including the effects of benefit formulas that give employees greater benefits for later years of service. This requires the entity to determine how much benefit is attributable to the current and prior periods on the basis of the plan's benefit formula and to make estimates (actuarial assumptions) about demographic variables (such as employee turnover and mortality) and financial variables (such as future increases in salaries and medical costs) that influence the cost of the benefit. The actuarial assumptions shall be unbiased (neither imprudent nor excessively conservative), mutually compatible and selected to lead to the best estimate of the future cash flows that will arise under the plan.

Notes

The rights to vested benefits are not conditional on continued employment, under the conditions of a retirement plan.

In the context of measuring the present value of an entity's defined benefit obligation, paragraph 28.16 describes actuarial assumptions as estimates about demographic variables (such as employee turnover and mortality) and financial variables (such as future increases in salaries and medical costs) that influence the benefit's cost. Paragraph 76 of IAS 19 provides guidance about actuarial assumptions. In applying the *IFRS for SMEs* Standard, an entity is permitted (but is not required) to consider the guidance in IAS 19.

These actuarial assumptions comprise:

(a) demographic assumptions about the future characteristics of current and former employees (and their dependants) who are eligible for benefits. Demographic assumptions deal with matters such as:

(i) mortality, both during and after employment;

(ii) rates of employee turnover, disability and early retirement;

(iii) the proportion of plan members with dependants who will be eligible for benefits; and

(iv) claim rates under medical plans; and

(b) financial assumptions, dealing with items such as:

(i) the discount rate;

(ii) future salary and benefit levels;

(iii) in the case of medical benefits, future medical costs, including, where material, the cost of administering claims and benefit payments; and

(iv) the expected rate of return on plan assets.

Examples–vested and unvested benefits

Ex 24 **A defined benefit plan provides a lump-sum benefit of CU100 for each year of service, payable immediately after the employee leaves the entity.**

A benefit of CU100 is attributed to each year. The present value of the defined benefit obligation is the present value of CU100, multiplied by the number of years of service up to the end of the reporting period.

Because the benefit is payable immediately when the employee leaves the entity, the present value of the defined benefit obligation reflects the date at which the employee is expected to leave. Thus, because of the discounting effect, the benefit is less than it would be had the employee left at the end of the reporting period.

Ex 25 **A plan provides a monthly pension of 0.2% of final salary for each year of service. The pension is payable from the age of 65.**

An entity attributes to each year of service a benefit equal to a monthly pension of 0.2% of the estimated final salary payable from the expected retirement date until the expected date of death. The present value of the defined benefit obligation is the present value of monthly pension payments of 0.2% of final salary[3], multiplied by the number of years of service up to the end of the reporting period.

Ex 26 **A plan pays a benefit of CU100 for each year of service. The benefits vest after ten years of service.**

A benefit of CU100 is attributed to each year of service. In each of the first ten years, the measurement of the obligation reflects the probability that the employee may not complete ten years of service.

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[3] If the employee leaves the entity before their 65th birthday their final salary is the salary at the date of leaving the entity. The pension would be paid to the employee from age 65.

Ex 27 **A plan pays a lump-sum benefit of CU1,000 that vests and is paid after ten years of service. The plan provides no further benefit for subsequent service.**

A benefit of CU100 (CU1,000 divided by ten) is attributed to each of the first ten years of service. The measurement of the benefit is adjusted to reflect the probability that the employee may not complete ten years of service. The present value of the defined benefit obligation is the present value of the adjusted benefit, multiplied by the number of years of service up to the end of the reporting period. No benefit is attributed to subsequent years.

Ex 28 **A plan pays a lump-sum retirement benefit of CU2,000 to all employees still employed at the age of 55 after 20 years of continuous service.**

For employees who join before the age of 35, service first leads to benefits under the plan starting from the age of 35 (because the plan requires 20 years of *continuous* service an employee could leave at the age of 30 and return at the age of 33, with no effect on the amount or timing of benefits). Those benefits are conditional on further service. Hence, for all qualifying employees, the obligation reflects the probability that the employee may not complete the necessary period of service. Also, service beyond the age of 55 will lead to no material amount of further benefits. For qualifying employees, the entity attributes benefit of CU100 (CU2,000 divided by 20) to each year from the age of 35 to the age of 55.

The benefit does not apply to an employee who joins after the age of 35 because such an employee would not complete the requirement for 20 years of continuous service by age of 55.

Ex 29 **Employees are entitled to a benefit of 3% of final salary for each year of service before the age of 55.**

A benefit of 3% of estimated final salary is attributed to each year up to the age of 55. This is the date when further service by the employee will lead to no amount of further benefits under the plan. No benefit is attributed to service after that age although the entity will recognise other costs for the period when the employee is age more than 55.

In examples 27 and 28, each period of service gives rise to an additional unit of benefit entitlement and each unit is measured separately; the obligation is the sum of the individual units. This approach is the projected unit credit method (see paragraph 28.18 for further discussion).

Discounting

28.17 An entity shall measure its defined benefit obligation on a discounted present value basis. The entity shall determine the rate used to discount the future payments by reference to market yields at the reporting date on high quality corporate bonds. In countries with no deep market in such bonds, the entity shall use the market yields (at the reporting date) on government bonds. The currency and term of the corporate bonds or government bonds shall be consistent with the currency and estimated period of the future payments.

Notes

The discount rate reflects the time value of money but not the actuarial or investment risk. Furthermore, the discount rate does not reflect the entity-specific credit risk borne by the entity's creditors.

Actuarial valuation method

28.18 If an entity is able, without undue cost or effort, to use the **projected unit credit method** to measure its defined benefit obligation and the related expense, it shall do so. If defined benefits are based on future salaries, the projected unit credit method requires an entity to measure its defined benefit obligations on a basis that reflects estimated future salary increases. Additionally, the projected unit credit method requires an entity to make various actuarial assumptions in measuring the defined benefit obligation, including discount rates, the expected rates of return on plan assets, expected rates of salary increases, employee turnover, mortality, and (for defined benefit medical plans) medical cost trend rates.

Notes

The projected unit credit method as defined in the Glossary is an actuarial valuation method in which each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation.

Example–projected unit credit method

Ex 30 **A lump-sum benefit equal to 1% of final salary for each year of service is payable on termination of service. The salary in Year 1 is CU10,000 and is assumed to increase at 7% (compound) each year. The discount rate is 10% per year. The following table shows how the obligation accumulates at the end of each of the next five years for an employee who is expected to leave at the end of Year 5, assuming actuarial assumptions don't change.**

For simplicity, this example omits the additional adjustment needed to reflect the probability that the employee may leave the entity at an earlier or later date.

Year	1	2	3	4	5
Benefit attributed to:					
– prior years	–	131.08	262.16	393.24	524.32
– current year (1% × estimated final salary)[(a)]	131.08	131.08	131.08	131.08	131.08
– current and prior years[(b)]	**131.08**	**262.16**	**393.24**	**524.32**	**655.40**
Opening obligation	–	**89.53**	**196.96**	**324.99**	**476.65**
Interest at 10%	–	8.95	19.70	32.50	47.67
Current service cost	89.53	98.48	108.33	119.16	131.08
Closing obligation[(c)]	**89.53**	**196.96**	**324.99**	**476.65**	**655.40**

(a) CU131 = 1% × 13,108 final annual salary (CU10,000 salary in year 1 × (1 + 0.07 annual increase)$^{4\ \text{(number of periods between year 1 and year 5)}}$).

(b) The current service cost is the present value of benefit attributed to the current year:
Year 1—CU131.08 × 1/(1.1)^4 = CU131.08 × 0.683013 = CU89.53
Year 2— CU131.08 × 1/(1.1)^3 = CU131.08 × 0.751315 = CU98.48
Year 3— CU131.08 × 1/(1.1)^2 = CU131.08 × 0.826446 = CU 108.33
Year 4— CU131.08 × 1/(1.1)^1 = CU131.08 × 0.909091= CU119.16
Year 5— CU131.08 × 1/(1.1)^0 = CU131.08 × 1 = CU131.08.

(c) The closing obligation is the present value of benefit attributed to current and prior years.

28.19 If an entity is not able, without undue cost or effort, to use the projected unit credit method to measure its obligation and cost under defined benefit plans, the entity is permitted to make the following simplifications in measuring its defined benefit obligation with respect to current employees:

(a) ignore estimated future salary increases (ie assume current salaries continue until current employees are expected to begin receiving post-employment benefits).

(b) ignore future service of current employees (ie assume closure of the plan for existing as well as any new employees).

(c) ignore possible in-service mortality of current employees between the reporting date and the date employees are expected to begin receiving post-employment benefits (ie assume all current employees will receive the post-employment benefits). However, mortality after service (ie life expectancy) will still need to be considered.

An entity that takes advantage of the foregoing **measurement** simplifications must nonetheless include both **vested benefits** and unvested benefits in measuring its defined benefit obligation.

Notes

If, without undue cost or effort, an entity is unable to use the projected unit credit method set out in paragraph 28.18 to measure its defined benefit obligation, the entity is permitted to apply any of the simplifications in paragraph 28.19 for measuring its defined benefit obligation. When an entity applies the simplifications, it must comply with the disclosure requirements in paragraph 28.41(c).

Examples–simplified defined benefit plan calculations

Ex 31 **The facts are the same as in Example 30. In this example the entity has used one of the simplifications in paragraph 28.19 to calculate the current service cost by ignoring future salary increases. The following table shows how the obligation accumulates at the end of each of the next five years.**

Year	1	2	3	4	5
1% × current salary (increase at 7% per year)[(a)]	100.00	107.00	114.49	122.50	131.08
Years' service at end of year	1	2	3	4	5
Future value of obligation	**100**	**214**	**343.47**	**490.00**	**655.40**
Discount factor (10%)	0.683013	0.751315	0.826446	0.909091	1.000000
Present value of obligation	**68.30**	**160.78**	**283.86**	**445.45**	**655.40**
Opening obligation	–	**68.30**	**160.78**	**283.86**	**445.45**
Interest (10%)	–	6.83	16.08	28.39	44.55
Current service cost[(b)]	68.30	80.39	94.62	111.36	131.08
Actuarial loss (balancing figure)*	–	5.26	12.38	21.84	34.32
Closing obligation[(c)]	**68.30**	**160.78**	**283.86**	**445.45**	**655.40**

(a) 1% × current salary in each year:
Year 1—CU10,000 × 1% = CU100.00
Year 2— CU10,000 × 1.07 × 1% = CU107.00
Year 3— CU10,000 × 1.07^2 × 1% = CU114.49
Year 4— CU10,000 × 1.07^3 × 1% = CU122.50
Year 5— CU10,000 × 1.07^4 × 1% = CU131.08

(b) The current service cost is the present value of benefit attributed to the current year:
Year 1—CU100 × $1/(1.1)^4$ = CU100 × 0.683013 = CU68.30
Year 2— CU107 × $1/(1.1)^3$ = CU107 × 0.751315 = CU80.39
Year 3— CU114.49 × $1/(1.1)^2$ = CU114.49 × 0.826446 = CU94.62
Year 4— CU122.50 × $1/(1.1)^1$ = CU122.50 × 0.909091= CU111.36
Year 5— CU131.08 × $1/(1.1)^0$ = CU131.08 × 1 = CU131.08

(c) The closing obligation is the present value of benefit attributed to current and prior years:
Year 1—CU100 × 1 years' service × $1/(1.1)^4$ = CU68.30
Year 2— CU107 × 2 years' service × $1/(1.1)^3$ = CU160.78
Year 3— CU114.49 × 3 years' service × $1/(1.1)^2$ = CU283.86
Year 4— CU122.50 × 4 years' service × $1/(1.1)^1$ = CU445.45
Year 5— CU131.08 × 5 years' service × $1/(1.1)^0$ = CU655.40

* The *IFRS for SMEs* Standard does not specify where the effects of the increase in salary may be recognised—whether a part of current service cost or as an actuarial loss. If the effect is recognised as an actuarial loss, depending on the accounting policy adopted, the actuarial loss (or gain) may be recognised in profit or loss or in other comprehensive income (see paragraph 28.24).

Ex 32 **The facts are the same as in Example 25 (a plan provides a monthly pension of 0.2% of final salary for each year of service. The pension is payable from the age of 65).**

An entity that is unable, without undue cost or effort, to use the projected unit credit method is permitted to measure its defined benefit obligation as the present value of the estimated monthly pension payments—calculated at 0.2% of current salary multiplied by the number of years of service to the end of the reporting period (assuming all current employees will receive the benefit). This measurement applies the simplification in paragraph 28.19(a) because it ignores estimates of future salary increases.

28.20 This Standard does not require an entity to engage an independent actuary to perform the comprehensive actuarial valuation needed to calculate its defined benefit obligation. Nor does it require that a comprehensive actuarial valuation must be done annually. In the periods between comprehensive actuarial valuations, if the principal actuarial assumptions have not changed significantly the defined benefit obligation can be measured by adjusting the prior period measurement for changes in employee demographics such as number of employees and salary levels.

Plan introductions, changes, curtailments and settlements

28.21 If a defined benefit plan has been introduced or changed in the current period, the entity shall increase or decrease its defined benefit liability to reflect the change, and shall recognise the increase (decrease) as an expense (**income**) in measuring **profit or loss** in the current period. Conversely, if a plan has been curtailed (ie benefits or group of covered employees are reduced) or settled (the employer's obligation is completely discharged) in the current period, the defined benefit obligation shall be decreased or eliminated and the entity shall recognise the resulting **gain** or loss in profit or loss in the current period.

Example–curtailment

Ex 33 **An entity discontinues one of its businesses at the beginning of its financial year and employees of the discontinued business will earn no further benefits. The discontinuation is a curtailment without a settlement. Using current actuarial assumptions (including current market interest rates and other current market prices) immediately before the curtailment, the entity has a defined benefit obligation with a net present value of CU1,000 and plan assets with a fair value of CU820. The curtailment reduces the net present value of the obligation by CU100 to CU900.**

The effect of the curtailment is as follows:

	Before curtailment CU	Curtailment gain CU	After curtailment CU
Net present value of obligation	1,000	(100)	900
Fair value of plan assets	(820)	-	(820)
Net liability recognised in statement of financial position	180	(100)	80

In the current period, the entity could record the following journal entry for the curtailment of its employee benefit obligation as follows:

Dr	Post-employment benefit (defined benefit plans) – liability	CU100	
	Cr Profit or loss		CU100

To recognise the curtailment of defined benefit plans caused by the discontinuity of a business.

Defined benefit plan asset

28.22 If the present value of the defined benefit obligation at the reporting date is less than the fair value of plan assets at that date, the plan has a surplus. An entity shall recognise a plan surplus as a defined benefit plan asset only to the extent that it is able to recover the surplus either through reduced contributions in the future or through refunds from the plan.

Examples–defined benefit plan surplus

Ex 34 **At 31 December 20X1, an entity's defined benefit plan has the following characteristics:**

Present value of the obligation	CU1,000
Fair value of plan assets	CU1,200
Excess plan assets	CU200

At 31 December 20X1, the present value of future refunds and reductions in future contributions available to the entity is CU200.

The entity must present the defined benefit plan surplus as a CU200 defined benefit plan asset in its statement of financial position at 31 December 20X1.

Ex 35 **The facts are the same as in Example 34. However, in this example, at 31 December 20X1, the present value of future refunds and of reductions in future contributions available to the entity is nil.**

The entity measures the defined benefit plan surplus at nil (defined benefit plan asset) in its statement of financial position as at 31 December 20X1.

Ex 36 **The facts are the same as in Example 34. However, in this example, at 31 December 20X1 the present value of future refunds and of reductions in future contributions available to the entity is CU80.**

The entity measures the defined benefit plan surplus at CU80 (defined benefit plan asset) in its statement of financial position at 31 December 20X1.

Cost of a defined benefit plan

28.23 An entity shall recognise the net change in its defined benefit liability during the period, other than a change attributable to benefits paid to employees during the period or to contributions from the employer, as the cost of its defined benefit plans during the period. That cost is recognised either entirely in profit or loss as an expense or partly in profit or loss and partly as an item of **other comprehensive income** (see paragraph 28.24) unless another section of this Standard requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

Examples–recognition of the cost of a defined benefit plan

Ex 37 **An entity that recognises actuarial gains and losses in profit or loss provides its employees with a monthly pension of 0.2% of final salary for each year of service. The pension is payable from the age of 65. The plan is unfunded.**

At 31 December 20X1, the entity determined the carrying amount of the plan obligation at CU1,000,000 (20X0: CU900,000).

In 20X1 the entity paid pensions of CU40,000 to its past employees.

The entity recognises an expense of CU140,000 (CU1,000,000 closing obligation + CU40,000 pensions paid in 20X1 minus CU900,000 opening obligation) in profit or loss for the year ended 31 December 20X1.

Ex 38 **The facts are the same as in Example 37. However, in this example, the entity's obligations for the defined benefit scheme are funded. Furthermore, in 20X1 the entity contributed CU110,000 to the fund.**

At 31 December 20X1, the entity measured the fair value of the plan assets at CU980,000 (20X0: CU890,000).

The entity recognises an expense of CU120,000 (CU20,000 closing obligation + CU110,000 contribution by the entity in 20X1 minus CU10,000 opening obligation) in profit or loss for the year ended 31 December 20X1.

Ex 39 **The facts are the same as in Example 37. However, in this example, CU10,000 of the cost of the defined benefit plan is attributable to the cost of producing**

inventories in the period that remained in the entity's inventories at 31 December 20X1.

The entity recognises a defined benefit plan expense of CU130,000 in profit or loss for the year (CU140,000 calculated in Example 37 minus CU10,000 included in the cost of inventories at 31 December 20X1).

Applying paragraphs 13.20 and 13.21, the CU10,000 included in the cost of inventories will be included in profit or loss when the inventories are sold or impaired.

Recognition–accounting policy election

28.24 An entity is required to recognise all actuarial gains and losses in the period in which they occur. An entity shall:

(a) recognise all actuarial gains and losses in profit or loss; or

(b) recognise all actuarial gains and losses in other comprehensive income.

as an accounting policy election. The entity shall apply its chosen accounting policy consistently to all of its defined benefit plans and all of its actuarial gains and losses. Actuarial gains and losses recognised in other comprehensive income shall be presented in the **statement of comprehensive income**.

Notes

Actuarial gains and losses are not defined in the *IFRS for SMEs* Standard. IAS 19, however, defined this. In applying the *IFRS for SMEs* Standard, an entity is permitted (but is not required) to consider the guidance in IAS 19. Actuarial gains and losses comprise:

(a) experience adjustments (the effects of differences between the previous actuarial assumptions and what has actually occurred); and

(b) the effects of changes in actuarial assumptions.

Consistent with Section 10 *Accounting Policies, Estimates and Errors*, changes in accounting estimates are not applied by restating prior periods. The *IFRS for SMEs* Standard allows actuarial gains and losses to be recognised either in profit or loss or other comprehensive income. Therefore, actuarial gains and losses are included in comprehensive income of the period in which the actuarial assumptions are changed (the changes in actuarial assumptions result from events before the reporting date that resolve a past estimate (experience adjustments) or from changes in the estimated cost of employee service before the reporting date).

Example–accounting policy choice

Ex 40 **The facts are the same as in example 39 (the cost of the defined benefit plan for the year ended 31 December 20X1 is CU140,000). However, in this example the entity recognises all actuarial gains and losses in other comprehensive income (see paragraph 28.24(b)). CU50,000 of the cost of the defined benefit plan for the year ended 31 December 20X1 is attributable to actuarial losses.**

The entity recognises cost of a defined benefit plan of CU140,000 (CU1,000,000 closing obligation + CU40,000 pensions paid in 20X1 minus CU900,000 opening obligation) as follows:

- CU50,000 in other comprehensive income for the year ended 31 December 20X1 (the portion of the cost that is attributable to actuarial gains and losses); and
- CU90,000 in profit or loss for the year ended 31 December 20X1 (CU140,000 total cost less CU50,000 recognised in other comprehensive income).

Example 39 illustrates the accounting by an entity that elects to account for actuarial gains and losses in profit or loss (applying paragraph 28.24(a)).

28.25 The net change in the defined benefit liability that is recognised as the cost of a defined benefit plan includes:

(a) the change in the defined benefit liability arising from employee service rendered during the reporting period;

(b) interest on the defined benefit obligation during the reporting period;

(c) the returns on any plan assets and the net change in the fair value of recognised reimbursement rights (see paragraph 28.28) during the reporting period;

(d) actuarial gains and losses arising in the reporting period;

(e) increases or decreases in the defined benefit liability resulting from introducing a new plan or changing an existing plan in the reporting period (see paragraph 28.21); and

(f) decreases in the defined benefit liability resulting from curtailing or settling an existing plan in the reporting period (see paragraph 28.21).

Example–components of the net change in the defined benefit liability

Ex 41 **The following information is given about a funded defined benefit plan. To keep interest computations simple, all transactions are assumed to be made at the year-end. The present value of the obligation and the fair value of the plan assets were both CU1,000 at 1 January 20X1.**

	20X1	*20X2*	*20X3*
Discount rate at start of year	10.0%	9.0%	8.0%
Current service cost	130	140	150
Benefits paid	150	180	190
Contributions paid	90	100	110
Present value of obligation at 31 December	1,141	1,197	1,295
Fair value of plan assets at 31 December	1,092	1,109	1,093

In 20X2, the plan was amended to provide additional benefits with effect from 1 January 20X2. The present value as at 1 January 20X2 of additional benefits for employee service before 1 January 20X2 was CU50 for vested benefits and CU30 for non-vested benefits. As at 1 January 20X2, the entity estimated that, on average, benefits would become vested within three years. The entity has adopted a policy of recognising actuarial gains and losses in profit or loss (see paragraph 28.24(a)).

Changes in the present value of the obligation and in the fair value of the plan assets are used to determine the amount of the actuarial gains or losses for the period as follows:

	20X1	20X2	20X3
Present value of obligation, 1 January	1,000	1,141	1,197
Interest cost	100 [(a)]	103 [(b)]	96 [(c)]
Current service cost	130	140	150
Increases resulting from changing an existing plan	–	80	–
Benefits paid	(150)	(180)	(190)
Actuarial (gain) loss on obligation (balancing figure)	61	(87)	42
Present value of obligation, 31 December	**1,141**	**1,197**	**1,295**
Fair value of plan assets, 1 January	1,000	1,092	1,109
Return on plan assets	152 [(d)]	97 [(e)]	64 [(f)]
Contributions	90	100	110
Benefits paid	(150)	(180)	(190)
Fair value of plan assets, 31 December	**1,092**	**1,109**	**1,093**

[(a)] CU1,000 present value of obligation at 31 December 20X0 × 10%.

[(b)] CU1,141 present value of obligation at 31 December 20X1 × 9%.

[(c)] CU1,197 present value of obligation at 31 December 20X2 × 8%.

[(d)] CU1,092 fair value of plan assets at 31 December 20X1 + CU150 benefits paid less CU90 contributions received less CU1,000 fair value of plan assets at 31 December 20X0.

[(e)] CU1,109 fair value of plan assets at 31 December 20X2 + CU180 benefits paid less CU100 contributions received less CU1,092 fair value of plan assets at 31 December 20X1.

[(f)] CU1,093 fair value of plan assets at 31 December 20X3 + CU190 benefits paid less CU110 contributions received less CU1,109 fair value of plan assets at 31 December 20X2.

The amount to be recognised in profit or loss is determined as follows:

	20X1	20X2	20X3
Current service cost	130	140	150
Interest cost	100	103	96
Return on plan assets	(152)	(97)	(64)
Actuarial (gain) loss recognised in year	61	(87)	42
Past service cost—non-vested benefits	–	30	–
Past service cost—vested benefits	–	50	–
Staff cost for the year ended 31 December 20X1—recognised as an expense in profit or loss or as part of assets (see paragraphs 28.3(b) and 28.23)	**139**	**139**	**224**

In most cases, the interest cost and return on plan assets need not be calculated by the entity as they are available from the actuarial valuation report.

28.26 Employee service gives rise to an obligation under a defined benefit plan even if the benefits are conditional on future employment (in other words, they are not yet vested). Employee service before the vesting date gives rise to a constructive obligation because, at each successive reporting date, the amount of future service that an employee will have to render before becoming entitled to the benefit is reduced. In measuring its defined benefit obligation, an entity considers the probability that some employees may not satisfy vesting requirements. Similarly, although some post-employment benefits (such as post-employment medical benefits) become payable only if a specified event occurs when an employee is no longer employed (such as an illness), an obligation is created when the employee renders service that will provide entitlement to the benefit if the specified event occurs. The probability that the specified event will occur affects the measurement of the obligation, but does not determine whether the obligation exists.

Examples–vesting conditions

See examples 26–28.

28.27 If defined benefits are reduced for amounts that will be paid to employees under government-sponsored plans, an entity shall measure its defined benefit obligations on a basis that reflects the benefits payable under the government plans, but only if:

(a) those plans were enacted before the reporting date; or

(b) past history, or other reliable evidence, indicates that those state benefits will change in some predictable manner, for example, in line with future changes in general price levels or general salary levels.

Reimbursements

28.28 If an entity is virtually certain that another party will reimburse some or all of the expenditure required to settle a defined benefit obligation, the entity shall recognise its right to reimbursement as a separate asset. The entity shall measure the asset at fair value. In the statement of comprehensive income (or in the **income statement**, if presented), the expense relating to a defined benefit plan may be presented net of the amount recognised for a reimbursement.

Other long-term employee benefits

28.29 Other long-term employee benefits generally include, for example:

(a) long-term compensated absences such as long-service or sabbatical leave;

(b) long-service benefits;

(c) long-term disability benefits;

(d) profit-sharing and bonuses payable twelve months or more after the end of the period in which the employees render the related service; and

(e) deferred compensation paid twelve months or more after the end of the period in which it is earned.

Examples–other long-term employee benefits

Ex 42 **An entity's employees are each entitled to five days of paid sick leave for each year. Unused sick leave may be carried forward for three calendar years.**

The sick leave is accounted for as other long-term employee benefits. The sick leave is not a short-term employee benefit because the paid absence is not expected to occur wholly within 12 months after the end of the period in which the employees render the related employee service because unused sick leave is carried forward.

Ex 43 **A profit-sharing plan requires an entity to pay a specified proportion of its cumulative profit for a five-year period to employees who provide service throughout the five-year period.**

The profit-sharing plan is accounted for as other long-term employee benefits. The profit-sharing plan is not a short-term employee benefit because the payment for the share of profits is not due wholly within 12 months after the end of the period in which the employees render the related employee service. The entity considers each year of the five-year service requirement separately rather than considering the payment due date compared to the end of the five-year service period.

Ex 44 **An entity's expatriate employees are each entitled to 30 days' expatriate leave for each three-year period of continuous employment with the entity. Unused expatriate leave may be carried forward for three calendar years.**

The expatriate leave is accounted for as other long-term employee benefits. The expatriate leave is not a short-term employee benefit, because the paid absence is not expected to occur wholly within 12 months after the end of the period in which the employees render the related employee service that earns the entitlement. The entity considers each year of the three-year service requirement separately rather than considering the payment due date compared to the end of the three-year service period.

28.30 An entity shall recognise a liability for other long-term employee benefits measured at the net total of the following amounts:

(a) the present value of the benefit obligation at the reporting date; minus

(b) the fair value at the reporting date of plan assets (if any) out of which the obligations are to be settled directly.

An entity shall recognise the net change in the liability during the period, other than a change attributable to benefits paid to employees during the period or to contributions from the employer, as the cost of its other long-term employee benefits during the period. That cost is recognised entirely in profit or loss as an expense unless another section of this Standard requires it to be recognised as part of the cost of an asset, such as inventories or property, plant and equipment.

Examples–measurement

Ex 45 An entity's employees are each entitled to five days of paid sick leave for each year of service. Unused sick leave may be carried forward for two calendar years. Sick leave is taken first out of any balance brought forward from the previous years and then out of the current year's entitlement (FIFO).

The entity expects that, on average, the five days of sick leave will be taken by approximately halfway through the year.

At 31 December 20X1, the appropriate discount rates (see paragraph 28.17) are 5 % for a six-month period, 14% for an 18-month period and 18% for a 24-month period.

At 31 December 20X1, the entity's sick leave records were as follows:

Employee	*Wage rate (per working day in 20X1)*	*Accumulated sick leave days due on 31/12/20X1*	*Expected days sick leave to be taken in 20X2*	*Expected days sick leave to be taken in 20X3*	*Expected percentage wage increase effective 1 January each year*
1	CU400	9	4	4	5%
2	CU310	6	5	5	2%
3	CU250	0	8	8	2%
4	CU180	1	6	5	8%

At 31 December 20X1, the entity's liability for sick leave is CU5,087(CU3,089 for employee 1 (CU1,640 and CU1,449 for sick leaves expected to be taken in 20X2 and 20X3, respectively) + CU1,808 for employee 2 (CU1,543 and CU265 for sick leaves expected to be taken in 20X2 and 20X3, respectively) + CU190 for employee 4), as calculated below:

- Employee 1 (expected sick leave to be taken in 20X2)—CU400 20X1 wage rate per working day × 1.05 salary increase × 4 expected days' sick leave in 20X2, accumulated at 31 December 20X1 = CU1,680. CU1,680 ÷ discount factor of 5% over 6 months = CU1,640.
- Employee 1 (expected sick leave to be taken in 20X3)—CU400 20X1 wage rate per working day × 1.1025 salary increase × 4 expected days' sick leave in 20X3, accumulated at 31 December 20X1 = CU1,764. CU1,764 ÷ discount factor of 14% over 18 months = CU1,449.
- Employee 2 (expected sick leave to be taken in 20X2)—CU310 20X1 wage rate per working day × 1.02 salary increase × 5 expected days' sick leave in 20X2, accumulated at 31 December 20X1 = CU1,581. CU1,581 ÷ discount factor of 5% over 6 months = CU1,543.
- Employee 2 (expected sick leave to be taken in 20X3)—CU310 20X1 wage rate per working day × 1.0404 salary increase × 1 expected day's sick leave in 20X3, accumulated at 31 December 20X1 = CU323. CU323 ÷ discount factor of 14% over 18 months = CU265.
- Employee 3—CU0, because the employee has no sick leave days accumulated at 31 December 20X1.

- Employee 4 (expected sick leave to be taken in 20X2)—CU180 20X1 wage rate per working day × 1.08 salary increase × 1 expected day's sick leave in 20X2, accumulated at 31 December 20X1 = CU194. CU194 ÷ discount factor of 5% over 6 months = CU190.

Ex 46 **The facts are the same as in Example 45. However, in this example, the employee receives payment from the entity for sick leave not taken within 24 months after the end of the period in which the employees render the related service.**

At 31 December 20X1, the entity's liability for sick leave is CU5,404 (CU3,406 for employee 1 + CU1,808 for employee 2 + CU190 for employee 4), as calculated below:

- Employee 1 (expected sick leave to be taken in 20X2)—CU400 20X1 wage rate per working day × 1.05 salary increase × 4 expected days' sick leave in 20X2, accumulated at 31 December 20X1 = CU1,680. CU1,680 ÷ discount factor of 5% over 6 months = CU1,640.
- Employee 1 (expected sick leave to be taken in 20X3)—CU400 20X1 wage rate per working day × 1.1025 salary increase × 4 expected days' sick leave in 20X3, accumulated at 31 December 20X1 = CU1,764. CU1,764 ÷ discount factor of 14% over 18 months = CU1,449.
- Employee 1 (expected payout on 31 December 20X3 for sick leave not taken)—CU400 20X1 wage rate per working day × 1.1025 salary increase × 1 expected day's sick leave earned in 20X1 and paid out on 31 December 20X3 = CU441. CU441 ÷ discount factor of 18% over 24 months = CU317.
- Employee 2 (expected sick leave to be taken in 20X2)—CU310 20X1 wage rate per working day × 1.02 salary increase × 5 expected days' sick leave in 20X2, accumulated at 31 December 20X1 = CU1,581. CU1,581 ÷ discount factor of 5% over 6 months = CU1,543.
- Employee 2 (expected sick leave to be taken in 20X3)—CU310 20X1 wage rate per working day × 1.0404 salary increase × 1 expected day's sick leave in 20X3, accumulated at 31 December 20X1 = CU323. CU323 ÷ discount factor of 14% over 18 months = CU265.
- Employee 3—CU0, because the employee has no sick leave days accumulated at 31 December 20X1.
- Employee 4 (expected sick leave to be taken in 20X2)—CU180 20X1 wage rate per working day × 1.08 salary increase × 1 expected day's sick leave in 20X2, accumulated at 31 December 20X1 = CU194. CU194 ÷ discount factor of 5% over 6 months = CU190.

Termination benefits

28.31 An entity may be committed, by legislation, by contractual or other agreements with employees or their representatives or by a constructive obligation based on business practice, custom or a desire to act equitably, to make payments (or provide other benefits) to employees when it terminates their employment. Such payments are termination benefits.

Examples–termination benefits

Ex 47 **On 1 December 20X1, an entity made a public announcement of its commitment to a plan for closing one of its retail outlets on 1 March 20X2. On 15 December 20X1, the entity commenced the process and started communicating with the affected employees. By publicly announcing its decision and commencing the closing of the retail outlet, the entity, has a constructive obligation to pay termination benefits of CU2 million to the employees.**

The entity determines that it would have to pay termination benefits of CU2 million if it terminates employees of one of its retail outlets. At 31 December 20X1, the retailer has a present legal obligation to pay termination benefits of CU2 million to the employees upon closing the retail outlet.

Ex 48 **The facts are the same as in Example 47. However, in this example, the entity does not have a legal obligation to pay termination benefits to the employees of the retail outlet. However, prior to 31 December 20X1 the entity agreed with its employees' labour union to make a settlement payment of CU2 million to the affected employees.**

At 31 December 20X1, the retailer has a present obligation to pay termination benefits of CU2 million to the employees upon the closure of the retail outlet.

Ex 49 **In December 20X1, with a view to reducing its workforce by 10%, an entity made its employees an irrevocable offer of voluntary redundancy. In accordance with the offer, the entity will compensate the first 10% of employees who accept voluntary redundancy on or before 31 March 20X2. The compensation offered is equal to the employee's annual salary.**

Because the offer is irrevocable at 31 December 20X1, the entity has a present obligation to pay termination benefits to the first 10% of employees who accept voluntary redundancy by 31 March 20X2. The entity estimates the number of employees who will volunteer for the redundancy package (see paragraph 28.36).

Recognition

28.32 Because termination benefits do not provide an entity with future economic benefits, an entity shall recognise them as an expense in profit or loss immediately.

28.33 When an entity recognises termination benefits, the entity may also have to account for a curtailment of retirement benefits or other employee benefits.

28.34 An entity shall recognise termination benefits as a liability and an expense only when the entity is demonstrably committed either:

(a) to terminate the employment of an employee or group of employees before the normal retirement date; or

(b) to provide termination benefits as a result of an offer made in order to encourage voluntary redundancy.

28.35 An entity is demonstrably committed to a termination only when the entity has a detailed formal plan for the termination and is without realistic possibility of withdrawal from the plan.

Notes

In the absence of more detailed guidance about what constitutes a detailed formal plan see Example 3 in the Appendix to Section 21 *Provisions and Contingencies* (in the context of a restructuring). In the absence of more detailed guidance about what constitutes 'without realistic possibility of withdrawal from the plan' see examples 6 and 7 in the Appendix to Section 21 (in the context of a provision).

For more detailed guidance on when an entity becomes demonstrably committed to a termination, an entity can look to full IFRS Standards (but it is not a requirement). IAS 19, paragraph 167 discussed that an entity can no longer withdraw the offer when the entity has communicated to the affected employees a plan of termination meeting all of the following criteria:

(a) actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made.

(b) the plan identifies the number of employees whose employment is to be terminated, their job classifications or functions and their locations (but the plan need not identify each individual employee) and the expected completion date.

(c) the plan establishes the termination benefits that employees will receive in sufficient detail that employees can determine the type and amount of benefits they will receive when their employment is terminated.

Examples–recognition of termination benefits

Ex 50 **The facts are the same as in Example 47.**

The retailer recognises a CU2 million expense in profit or loss for the year ended 31 December 20X1. Furthermore, at 31 December 20X1 the entity must recognise a liability to pay termination benefits to the employees to be terminated upon the closure of the retail outlet.

The retailer could record the following journal entry:

31 December 20X1

Dr Profit or loss	CU2,000,000	
Cr Termination benefits		CU2,000,000

To recognise the obligation for termination benefits arising from the commitment to close a retail outlet.

Ex 51 **The facts are the same as in Example 48.**

The retailer recognises a CU2 million expense in profit or loss for the year ended 31 December 20X1. Furthermore, at 31 December 20X1, the entity must recognise a liability to pay termination benefits to the employees to be terminated upon the closure of the retail outlet.

The retailer could record the following journal entry:

31 December 20X1

Dr Profit or loss	CU2,000,000	
Cr Termination benefits		CU2,000,000

To recognise the obligation for termination benefits arising from the commitment to close a retail outlet.

Ex 52 **The facts are the same as in Example 49.**

The entity recognises an expense in profit or loss for the year ended 31 December 20X1 at the best estimate of the expenditure that would be required to settle the obligation at the reporting date (based on the number and compensation of employees expected to accept the voluntary redundancy offer (see paragraph 28.36)). Furthermore, at 31 December 20X1, the entity must recognise a liability to pay the termination benefits to the employees.

Measurement

28.36 An entity shall measure termination benefits at the best estimate of the expenditure that would be required to settle the obligation at the reporting date. In the case of an offer made to encourage voluntary redundancy, the measurement of termination benefits shall be based on the number of employees expected to accept the offer.

Examples–measurement of termination benefits

Ex 53 **In December 20X1 an entity made a public announcement of its commitment to a plan for closing of one of its retail outlets on 1 March 20X2. On 15 December 20X1, the entity commenced the process and started communicating with the affected employees. Because it publicly announced its decision to close the retail outlet and commenced the process, the entity has a constructive obligation to pay termination benefits to the employees. Law in the retail outlet's jurisdiction requires the entity to pay termination benefits equal to three months' wages to each employee made redundant. However, the entity's practice is to pay significantly more than the amount legally required. In December 20X1 the entity entered negotiations with the employees' trade union to determine the amount to pay the employees that will be made redundant. At 31 December 20X1, management's best estimate of the termination benefits to be paid on 31 March 20X2 is CU3 million.**

At 31 December 20X1, the retailer has a present obligation to pay termination benefits to the employees of the retail unit to be closed. The entity must recognise that obligation as a liability and expense (in profit or loss) at CU3 million (management's best estimate of the expenditure required to settle the obligation at 31 December 20X1).

Ex 54 **The facts are the same as in Example 49.**

The entity must recognise an expense in profit or loss for the year ended 31 December 20X1 at the best estimate of the expenditure required to settle the obligation at the reporting date (based on the number of employees expected to accept the voluntary redundancy offer (see paragraph 28.36)). Furthermore, at 31 December 20X1, the entity must recognise a liability to pay employees those termination benefits.

28.37 When termination benefits are due more than twelve months after the end of the reporting period, they shall be measured at their discounted present value.

Example–discounting

Ex 55 **The facts are the same as in Example 53. However, in this example, the entity expects to pay the termination benefits on 30 June 20X3.**

An appropriate discount factor is 16% for the 18-month period ending 30 June 20X3.

The entity must recognise an expense of CU2,401,233 (CU3,000,000 best estimate of the expenditure required to settle the obligation at the reporting date ÷ discount factor of 16% over 18 months) in profit or loss for the year ended 31 December 20X1. Furthermore, at 31 December 20X1, the entity must recognise a CU2,401,233 liability to pay termination benefits to the employees.

Group plans

28.38 If a **parent** entity provides benefits to the employees of one or more **subsidiaries** in the **group**, and the parent presents **consolidated financial statements** using either the *IFRS for SMEs* or **full IFRS**, such subsidiaries are permitted to recognise and measure employee benefit expense on the basis of a reasonable allocation of the expense recognised for the group.

Disclosures

Disclosures about short-term employee benefits

28.39 This section does not require specific disclosures about short-term employee benefits.

Notes

The disclosure requirements of other sections of the *IFRS for SMEs* Standard may apply to short-term employee benefits. For example, paragraph 33.6 requires disclosure of all employee benefits of the entity's key management personnel.

Disclosures about defined contribution plans

28.40 An entity shall disclose the amount recognised in profit or loss as an expense for defined contribution plans. If an entity treats a defined benefit multi-employer plan as a defined contribution plan because sufficient information is not available to use defined benefit accounting (see paragraph 28.11) it shall disclose the fact that it is a defined benefit plan and the reason why it is being accounted for as a defined contribution plan, along with any available information about the plan's surplus or deficit and the implications, if any, for the entity.

Example–disclosures about defined contribution plans

Ex 56 **The disclosures that an entity would make about its defined contribution expense in the notes to its financial statements would be:**

SME A
Notes to the financial statements for the year ended 31 December 20X1

Note 7 Salaries and other employee benefits

This consists of:

	20X1	*20X0*
	CU	*CU*
Cost of defined contribution plans	20,000	19,000

…

Disclosures about defined benefit plans

28.41 An entity shall disclose the following information about defined benefit plans (except for any defined multi-employer benefit plans that are accounted for as a defined contribution plans in accordance with paragraph 28.11, for which the disclosures in paragraph 28.40 apply instead). If an entity has more than one defined benefit plan, these disclosures may be made in total, separately for each plan, or in such groupings as are considered to be the most useful:

(a) a general description of the type of plan, including **funding** policy;

(b) the entity's accounting policy for recognising actuarial gains and losses (either in profit or loss or as an item of other comprehensive income) and the amount of actuarial gains and losses recognised during the period;

(c) if the entity uses any of the simplifications in paragraph 28.19 in measuring its defined benefit obligation, it shall disclose that fact and the reasons why using the projected unit credit method to measure its obligation and cost under defined benefit plans would involve undue cost or effort;

(d) the date of the most recent comprehensive actuarial valuation and, if it was not as of the reporting date, a description of the adjustments that were made to measure the defined benefit obligation at the reporting date;

(e) a reconciliation of opening and closing balances of the defined benefit obligation showing separately benefits paid and all other changes;

(f) a reconciliation of the opening and closing balances of the fair value of plan assets and of the opening and closing balances of any reimbursement right recognised as an asset, showing separately, if applicable:

(i) contributions;

(ii) benefits paid; and

(iii) other changes in plan assets.

(g) the total cost relating to defined benefit plans for the period, disclosing separately the amounts:

(i) recognised in profit or loss as an expense; and

(ii) included in the cost of an asset.

(h) for each major class of plan assets, which shall include, but is not limited to, equity instruments, debt instruments, property, and all other assets, the percentage or amount that each major class constitutes of the fair value of the total plan assets at the reporting date;

(i) the amounts included in the fair value of plan assets for:

(i) each class of the entity's own **financial instruments**; and

(ii) any property occupied by, or other assets used by, the entity.

(j) the actual return on plan assets; and

(k) the principal actuarial assumptions used, including, when applicable:

(i) the discount rates;

(ii) the expected rates of return on any plan assets for the periods presented in the **financial statements**;

(iii) the expected rates of salary increases;

(iv) medical cost trend rates; and

(v) any other **material** actuarial assumptions used.

The reconciliations in (e) and (f) need not be presented for prior periods. A subsidiary that recognises and measures employee benefit expense on the basis of a reasonable allocation of the expense recognised for the group (see paragraph 28.38) shall, in its separate financial statements, describe its policy for making the allocation and shall make the disclosures in (a)–(k) above for the plan as a whole.

Example–disclosures about defined benefit plans

Ex 57 An entity could disclose its defined benefit plans in its financial statements as follows:

Extract from an entity's statement of financial position at 31 December 20X2

All amounts are presented in currency units 'CU'

	Note	*20X2*	*20X1*
ASSETS			
…			
Net defined benefit plan assets	18	-	90
…			
LIABILITIES			
…			
Net obligations under defined benefit plans	18	11,217	7,615
…			

Extract from an entity's statement of comprehensive income at 31 December 20X2

All amounts are presented in currency units 'CU'

	Note	*For the year ended 20X2*	*For the year ended 20X1*
…			
Net profit after tax		198,702	195,310
Other comprehensive income			
…			
Actuarial loss		(2,500)	(2,650)
…			

Extract from an entity's notes to the financial statements for the year ended 31 December 20X2

Note 1 Accounting policies

Employee benefits—defined benefit post-employment plans

The group has obligations to its employees and former employees to provide pensions in accordance with its defined benefit final salary pension schemes. The terms of the schemes oblige the group to provide employees with a pension equal to 1.5% of the employee's final salary for every year of service provided. The defined benefit pension plans are partly funded by the entity through payments to separate legal entities set up for the sole purpose of paying pensions to the group's employees.

The group is also obliged to reimburse 10% of its employee's post-employment medical costs if the employee has provided 20 years or more of service to the group. The group does not fund this obligation in advance.

The group measures defined benefit liabilities (assets) at the present value of its obligations under defined benefit plans at the reporting date minus the fair value at the reporting date of plan assets. The obligations under defined benefit plans are determined using the projected unit credit method. Actuarial gains and losses are recognised in other comprehensive income in the period in which they occur.

Note 18 Net obligations under defined benefit plans

	20X2	*20X1*
…		
Post-employment plans—defined benefit plans	CU11,217	CU7,525
presented as a liability	CU11,217	CU7,615
presented as an asset	–	90
…		

Post-employment plans—defined benefits plans

	Defined benefit pension plans		*Post-employment medical benefits*	
	20X2	*20X1*	*20X2*	*20X1*
Present value of funded obligations	22,300	18,400	–	–
Fair value of plan assets	(18,420)	(17,280)	_	_
Present value of unfunded obligations	–	–	7,337	6,405
Net liability	3,880	1,120	7,337	6,405

Amounts in the statement of financial position:

	Defined benefit pension plans		*Post-employment medical benefits*	
	20X2	*20X1*	*20X2*	*20X1*
Liabilities	3,880	1,210	7,337	6,405
Assets	–	(90)	_	_
Net liability	3,880	1,120	7,337	6,405

The most recent comprehensive actuarial valuation was performed at 31 December 20X2.

The pension plan assets include ordinary shares issued by the entity with a fair value of CU317 (20X1: CU281). Plan assets also include property occupied by the entity with a fair value of CU200 (20X1: CU185).

The amounts recognised in profit or loss are as follows:

	20X2	*20X1*
Defined-benefit pension plan expense	810	750
Defined-benefit post-employment medical plan expense	1,282	411
Total defined-benefit plan expense	2,092	1,161

Changes in the present value of the defined benefit obligation are as follows:

	Defined benefit pension plans 20X2	*Post-employment medical benefits 20X2*
Opening defined benefit obligation	18,400	6,405
Service cost	850	479
Interest cost	950	803
Actuarial losses	2,350	250
Gains on curtailments	(500)	–
Exchange differences on foreign plans	900	–
Benefits paid	(650)	(600)
Closing defined benefit obligation	22,300	7,337

Changes in the fair value of plan assets of the defined benefit pension plans are as follows:

	20X2
Opening fair value of plan assets	17,280
Actual return on plan assets	500
Contributions by employer	300
Actuarial gains	100
Exchange differences on foreign plans	890
Benefits paid	(650)
Closing fair value of plan assets	18,420

The group expects to contribute CU900 to its defined benefit pension plans in 20X3.

The major categories of plan assets as a percentage of total plan assets are as follows:

	20X2	*20X1*
Jurisdiction A equities	20%	22%
Jurisdiction B equities	16%	15%
Jurisdiction C equities	10%	7%
Jurisdiction A bonds	31%	26%
Jurisdiction B bonds	13%	17%
Jurisdiction C bonds	5%	8%
Property	5%	5%

Principal actuarial assumptions at the end of the reporting period (expressed as weighted averages):

	20X2	*20X1*
Discount rate at 31 December	5%	6.5%
Expected rates of return on plan assets	3%	2%
Future salary increases	5%	4%
Future pension increases	3%	2%
Proportion of employees opting for early retirement	30%	30%
Annual increase in healthcare costs	8%	8%
Future changes in maximum state healthcare benefits	3%	2%

Disclosures about other long-term benefits

28.42 For each category of other long-term benefits that an entity provides to its employees, the entity shall disclose the nature of the benefit, the amount of its obligation and the extent of funding at the reporting date.

Example–disclosures about other long-term benefits

Ex 58 An entity could disclose information about its other long-term employee benefits as follows:

Extract from an entity's statement of financial position at 31 December 20X2

All amounts are presented in currency units 'CU'

	Note	*20X2*	*20X1*
LIABILITIES			
Non-current liabilities			
Liability for employee benefits	18	40,000	35,000
…			
Current liabilities			
…			
Liability for employee benefits	18	20,000	15,000
…			

Extract from an entity's notes to the financial statements for the year ended 31 December 20X2

All amounts are presented in currency units 'CU'

Note 18 Provision for employee benefits

	20X2	*20X1*
…		
Other long-term employee benefits	10,623	9,830
…		
Total employee benefits	60,000	50,000

Other long-term employee benefits

The liability for other long-term employee benefits obligations relates to government mandated long-service payments. All full-time members of staff, excluding directors, are covered by the programme. A payment of 5% of salary (for the 12 months before the payment) is made at the end of five years of employment. The payment is made as part of the December payroll in the fifth year. The group does not fund this obligation in advance.

The accrual recognised at the year-end is determined with a present value calculation assuming a 3% average annual salary increase, with employee turnover based on the group's recent experience, discounted using the current market yield for high quality corporate bonds.

At 1 January 20X2	9,830
Additional accrual in year	7,033
Payment made in year	(6,240)
At 31 December 20X2	10,623

	20X2	*20X1*
Current liability	6,181	5,943
Non-current liability	4,442	3,887
Total	10,623	9,830

Disclosures about termination benefits

28.43 For each category of termination benefits that an entity provides to its employees, the entity shall disclose the nature of the benefit, the amount of its obligation and the extent of funding at the reporting date.

28.44 When there is uncertainty about the number of employees who will accept an offer of termination benefits, a **contingent liability** exists. Section 21 *Provisions and Contingencies* requires an entity to disclose information about its contingent liabilities unless the possibility of an outflow in settlement is remote.

Example–disclosures about termination benefits

Ex 59 An entity could satisfy the disclosure requirement for its termination benefits as follows:

Extract from an entity's statement of financial position at 31 December 20X2

All amounts are presented in currency units 'CU'

	Note	*20X2*	*20X1*
LIABILITIES			
Non-current liabilities			
Liability for employee benefits	18	40,000	35,000
…			
Current liabilities			
…			
Liability for employee benefits	18	20,000	15,000
…			

Extract from an entity's notes to the financial statements for the year ended 31 December 20X2

All amounts are presented in currency units 'CU'

Note 18 Employee benefits

	20X2	*20X1*
…		
Termination benefits	6,000	–
…		
Total employee benefits	60,000	50,000

At 1 January 20X2	–
Accrued in year	8,000
Payment made in year	(2,000)
At 31 December 20X2 (current liability)	6,000

Termination benefits

The liability for termination benefits relates to the offer made by the group to all employees over 55 years of age for voluntary redundancy payments. In accordance with the offer qualifying employees who accept voluntary redundancy on or before 1 June 20X3 will be paid termination benefits equal to one year's salary. The voluntary redundancy payments are to be made in July 20X3.

The accrual recognised at the year-end is determined using the estimated number of employees in each of the group's salary bands expected to apply for voluntary redundancy. Salary increases are not anticipated because the group awards salary increases in December each year. Furthermore, the termination benefits are not measured at a discounted amount because settlement is due in July 20X3.

The maximum possible financial effect of the voluntary redundancy offer that has not been recognised as a liability is CU3,000, as set out in note 30 contingent liabilities.

SIGNIFICANT ESTIMATES AND OTHER JUDGEMENTS

Applying the requirements of the *IFRS for SMEs* Standard to transactions and events often requires the exercise of judgement, including making estimates. Information about significant judgements made by an entity's management and key sources of estimation uncertainty are useful when assessing an entity's financial position, performance and cash flows. Consequently, in accordance with paragraph 8.6, an entity must disclose the judgements—apart from those involving estimates—that its management has made when applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

Furthermore, applying paragraph 8.7, an entity must disclose information about the key assumptions concerning the future, and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Other sections of the *IFRS for SMEs* Standard require disclosure of information about some judgements and estimation uncertainties. Section 28 focuses on:

- short-term employee benefits;
- post-employment benefits;
- other long-term employee benefits;
- termination benefits; and
- share-based payments (sometimes referred to as equity compensation benefits).

Share-based payments are accounted for applying the requirements of Section 26. The four types of employee benefits accounted for applying Section 28 have a common general recognition principle. However, each type of employee benefit has unique measurement requirements. Judgements that may be necessary in measuring each type of employee benefit are set out under separate headings.

Short-term employee benefits

The liability for accumulating compensated absences is measured at their expected cost (the amount that the entity expects to pay because of unused accumulated entitlement).
In determining the amount the entity expects to pay, the entity may need to estimate salary increases, estimate the timing of leave relative to salary increases and estimate the extent to which accumulated entitlement will expire unused. In many cases little difficulty is encountered in measuring short-term employee benefits. However, in some cases significant judgement is required in estimating salary increases, the timing of relevant events and the expiry of entitlement to unused accumulated paid absences (when experience is limited or trends are not expected to continue).

Post-employment benefits

Post-employment benefit plans are classified as either defined contribution plans or defined benefit plans.

Defined contribution plans

With defined contribution plans, the employee bears actuarial risk (that benefits will be less than expected) and investment risk (that assets invested will be insufficient to meet expected benefits). Consequently, little difficulty is expected in measuring an entity's liability to make contributions to a defined contribution plan.

Defined benefit plans

Under defined benefit plans actuarial risk and/or investment risk are borne by the employer.

An entity measures its defined benefit liability as the net total of the present value of the benefit obligation at the reporting date, minus the fair value at the reporting date of plan assets (if any) out of which the obligations are to be settled.

The presence of actuarial risk over the years to the expected settlement requires significant judgements in the estimation of actuarial assumptions—an entity's best estimates of the variables that will determine the ultimate cost of providing post-employment benefits. When using the projected unit credit method, actuarial assumptions, include, when relevant:

(a) demographic assumptions about the future characteristics of current and former employees (and their dependants) who are eligible for benefits. Demographic assumptions deal with matters such as:

  (i) mortality, both during and after employment;

  (ii) rates of employee turnover, disability and early retirement;

  (iii) the proportion of plan members with dependants who will be eligible for benefits; and

  (iv) claim rates under medical plans; and

(b) financial assumptions, for items such as:

  (i) the discount rate;

  (ii) future salary and benefit levels; and

  (iii) in the case of medical benefits, future medical costs, including, when material, the cost of administering claims and benefit payments; and

  (iv) the expected rate of return on plan assets.

Less judgement is needed when using the simplified calculations (see paragraph 28.19).

For funded plans, the entity must measure the fair value of the plan assets at each reporting date. When assets held by the plan can be traded in active markets, there is little difficulty in determining the fair value of the plan assets. However, in the absence of active markets significant judgements may be required in estimating the fair value of the plan assets. Mandatory requirements on determining the fair value of financial instruments are set out in paragraphs 11.27 to 11.32 of Section 11 *Basic Financial Instruments*. In the absence of guidance for estimating the fair value of other types of assets, this guidance should be applied to other plan assets.

Other long-term employee benefits

Other long-term employee benefits are employee benefits (other than post-employment benefits and termination benefits) that are not due wholly within 12 months after the end of the period in which the employees render the related service (long-term compensated absences, long-service benefits, long-term disability benefits, profit-sharing and bonuses payable 12 months or more after the end of the period in which the employees render the related service and deferred compensation paid 12 months or more after the end of the period in which it is earned).

An entity measures its liability for other long-term employee benefits as the net total of the present value of the benefit obligation at the reporting date, minus the fair value at the reporting date of plan assets (if any).

In many cases, entities encounter little difficulty when measuring other long-term employee benefits. However, in some cases, significant judgement is required in estimating the applicable discount rate, future salary and benefit levels, the timing of relevant events and the expiry of entitlement to unutilised accumulated paid absences (eg when experience is limited or trends are not expected to continue).

For funded plans, the entity must measure the fair value of the plan assets at each reporting date. When assets held by the plan can be traded in active markets, there is little difficulty in determining the fair value of the plan assets. However, in the absence of active markets significant judgements may be required in estimating the fair value of the plan assets. Mandatory requirements on determining the fair value of financial instruments are set out in Section 11. In the absence of guidance for estimating the fair value of other types of assets, this guidance should be applied to other plan assets.

Termination benefits

An entity may be committed, by legislation or by contractual or other agreements with employees or their representatives or by a constructive obligation based on business practice, custom or a desire to act equitably, to make payments (or provide other benefits) to employees when it terminates their employment. Such payments are termination benefits.

An entity measures termination benefits at the best estimate of the expenditure at the reporting date that would be required to settle the obligation. In many cases, entities encounter little difficulty when measuring termination benefits. However, in some cases, significant judgement is required (for example, in the case of an offer made to encourage voluntary redundancy, the entity must estimate the number of employees it expects to accept the offer). Furthermore, when termination benefits are due more than 12 months after the end of the reporting period, the entity must determine the rate at which to discount the expected cash flows to their present value.

Module 28—Employee Benefits

COMPARISON WITH FULL IFRS STANDARDS

When accounting for and reporting employee benefits for periods beginning on 1 January 2017, the main differences between the requirements of full IFRS Standards (see IAS 19 *Employee Benefits*) and the *IFRS for SMEs* Standard (see Section 28 *Employee Benefits*) are set out separately for each major type of employee benefit.

Short-term employee benefits

Full IFRS Standards (see IAS 19 paragraphs 9–18) and the *IFRS for SMEs* Standard (see paragraphs 28.3–28.8) share principles for the recognition and measurement of short-term employee benefits. However, the *IFRS for SMEs* Standard is drafted in simple language and includes less guidance on how to apply the principles.

Post-employment benefits

Defined contribution plans

Full IFRS Standards (see IAS 19 paragraphs 50–52) and the *IFRS for SMEs* Standard (see paragraph 28.13) share principles for the recognition and measurement of defined contribution plan benefits. However, the *IFRS for SMEs* Standard is drafted in simple language and includes significantly less guidance on how to apply the principles.

Defined benefit plans

Full IFRS Standards (see IAS 19 paragraphs 55–134) and the *IFRS for SMEs* Standard (see paragraphs 28.3 and 28.14–28.28) share many principles for the recognition and measurement of defined benefit plans. The main differences between applying IFRS Standards and the *IFRS for SMEs* Standard requirements for accounting and reporting defined benefit plans include:

- The *IFRS for SMEs* Standard is drafted in simple language.
- IAS 19 requires that a defined benefit obligation always be measured using an actuarial technique—the 'projected unit credit method'. For cost-benefit reasons, the *IFRS for SMEs* Standard provides for some measurement simplifications that retain the basic IAS 19 principles but are intended to reduce the need for SMEs to engage external specialists. Accordingly, if information based on the projected unit credit method is not available and cannot be obtained without undue cost or effort, SMEs must apply an approach that is based on IAS 19 but does not consider future salary increases, future service or possible mortality during an employee's period of service. This simplified approach still reflects estimates for the life expectancy of employees after retirement age. The resulting defined benefit pension obligation reflects both vested and unvested benefits.
- The *IFRS for SMEs* Standard clarifies that annual comprehensive valuations would not normally be necessary. In between comprehensive valuations, the valuations would be rolled forward for aggregate adjustments for employee composition and salaries, without changing the turnover or mortality assumptions.
- Full IFRS Standards requires recognising all actuarial gains and losses in other comprehensive income. The *IFRS for SMEs* Standard gives entities an option to recognise actuarial gains and losses in either profit and loss or other comprehensive income.

- Full IFRS Standards require an entity to recognise in other comprehensive income any adjustments arising from the change in the effect of the asset ceiling as set out in paragraph 57(d)(iii) of IAS 19. Although the *IFRS for SMEs* Standard specifies asset recognition limits for plan surpluses (see paragraph 28.22), it does not specify that an entity that elects to recognise actuarial gains and losses in other comprehensive income must also recognise any adjustments arising from the asset recognition limits in other comprehensive income.
- Full IFRS Standards define actuarial gains and losses and specify their composition. In the context of measuring the present value of an entity's defined benefit obligation, the *IFRS for SMEs* Standard describes actuarial assumptions as estimates about demographic variables (such as employee turnover and mortality) and financial variables (such as future increases in salaries and medical costs) that influence the cost of the benefit.
- The disclosure requirements for defined benefit plans in Section 28 are less detailed than those specified in IAS 19.

Other long-term employee benefits

Full IFRS Standards (see IAS 19 paragraphs 153−157) and the *IFRS for SMEs* Standard (see paragraph 28.30) share principles for the recognition and measurement of other long-term employee benefits. However, the *IFRS for SMEs* Standard is drafted in simple language and includes less guidance on how to apply the principles.

Termination benefits

Full IFRS Standards (see IAS 19 paragraphs 159−170) and the *IFRS for SMEs* Standard (see paragraphs 28.31−28.37) share principles for the recognition and measurement of termination benefits. However, the *IFRS for SMEs* Standard is drafted in simple language and includes less guidance on how to apply the principles.

Module 28—Employee Benefits

TEST YOUR KNOWLEDGE

Test your knowledge of the requirements for accounting and reporting employee benefits applying the *IFRS for SMEs* Standard by answering the questions provided.

You should assume that all amounts mentioned are material.

Once you have completed the test, check your answers against those set out beneath it.

Mark the box next to the most correct statement.

Question 1

Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees, including directors and management. Section 28 applies to the accounting for four types of employee benefits. It does not apply to the accounting for:

☐ (a) short-term employee benefits.

☐ (b) post-employment benefits.

☐ (c) other long-term employee benefits.

☐ (d) termination benefits.

☐ (e) share-based payments.

Question 2

An entity's employees are each entitled to 20 days of paid holiday leave per calendar year. Unused holiday leave cannot be carried forward and does not vest. The entity's annual reporting date is 31 December.

The holiday leave is:

☐ (a) a short-term employee benefit.

☐ (b) a post-employment benefit.

☐ (c) an other long-term employee benefit.

☐ (d) a termination benefit.

Question 3

Consider the information in Question 2. However, in this question, unused holiday leave is paid on 31 December of each year (it vests at the end of each calendar year but does not accumulate).

The holiday leave is:

☐ (a) a short-term employee benefit.

☐ (b) a post-employment benefit.

☐ (c) an other long-term employee benefit.

☐ (d) a termination benefit.

Question 4

Consider the information in Question 2. However, in this question, unused holiday leave may be carried forward for one calendar year (it accumulates but does not vest).

The holiday leave is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a post-employment benefit.
- ☐ (c) an other long-term employee benefit.
- ☐ (d) a termination benefit.

Question 5

Consider the information in Question 2. However, in this question, unused holiday leave may be carried forward for two calendar years (it accumulates but does not vest).

The holiday leave is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a post-employment benefit.
- ☐ (c) an other long-term employee benefit.
- ☐ (d) a termination benefit.

Question 6

Consider the information in Question 2. However, in this question, unused holiday leave may be carried forward until the employee leaves the employment of the entity, at which time the entity will pay the employee for all unused holiday leave (it accumulates and vests).

The holiday leave is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a post-employment benefit.
- ☐ (c) an other long-term employee benefit.
- ☐ (d) a termination benefit.

Question 7

An entity made a public announcement of its commitment to a voluntary redundancy plan. The entity has an obligation to pay employees that choose voluntary redundancy a lump sum equal to twice their gross annual salary.

The obligation to pay employees that choose voluntary redundancy is:

- ☐ (a) a short-term employee benefit.
- ☐ (b) a post-employment benefit.
- ☐ (c) an other long-term employee benefit.
- ☐ (d) a termination benefit.

Module 28—Employee Benefits

Question 8

An entity reimburses 50% of past employees' post-employment medical costs if the employee provides 25 years of service, or more, to the entity.

The obligation to pay 50% of qualifying past employees' post-employment medical costs is:

☐ (a) a short-term employee benefit.

☐ (b) a defined benefit post-employment benefit.

☐ (c) a defined contribution post-employment benefit.

☐ (d) an other long-term employee benefit.

☐ (e) a termination benefit.

Question 9

A profit-sharing plan requires an entity to pay a specified proportion of its cumulative profit for a five-year period to employees who serve throughout the five-year period.

The profit-sharing plan is:

☐ (a) a short-term employee benefit.

☐ (b) a post-employment benefit.

☐ (c) an other long-term employee benefit.

☐ (d) a termination benefit.

Question 10

A profit-sharing plan requires an entity to pay a specified proportion of its cumulative profit for the year to employees who served the entity throughout the year.

The profit-sharing plan is:

☐ (a) a short-term employee benefit.

☐ (b) a post-employment benefit.

☐ (c) an other long-term employee benefit.

☐ (d) a termination benefit.

Question 11

Which of the following best describes the simplified method of calculating a defined benefit obligation permitted by paragraph 28.19?

☐ (a) it measures the pension obligation on the basis of the plan formula applied to years of service to date and existing salary levels.

☐ (b) it measures the pension obligation on the basis of the plan formula applied to years of service to date and future salary levels.

☐ (c) it estimates the total benefit at retirement and then computes the level cost that will be sufficient, together with interest expected to accumulate at the assumed rate, to provide the total benefits at retirement.

☐ (d) it measures the pension obligation and pension cost on the basis of the shortest possible period for funding to maximise the tax deduction.

Question 12

An entity that uses the simplified method of calculating a defined benefit obligation is not permitted:

- ☐ (a) to ignore estimated future salary increases (assume current salaries continue until current employees are expected to begin receiving post-employment benefits).
- ☐ (b) to ignore future service of current employees (assume closure of the plan for existing as well as any new employees).
- ☐ (c) to ignore possible in-service mortality of current employees between the reporting date and the date employees are expected to begin receiving post-employment benefits (assume all current employees will receive the post-employment benefits).
- ☐ (d) to ignore possible mortality after service (life expectancy).

Module 28—Employee Benefits

Answers

Q1 (e)—see paragraph 28.2
Q2 (a)—see paragraph 28.4(b)
Q3 (a)—see paragraph 28.4(b)
Q4 (a)—see paragraph 28.4(b)
Q5 (c)—see paragraph 28.29
Q6 (c)—see paragraph 28.29
Q7 (d)—see paragraph 28.31
Q8 (b)—see paragraphs 28.9 and 28.10(b)
Q9 (c)—see paragraph 28.29(d)
Q10 (a)—see paragraph 28.4(c)
Q11 (a)—see paragraph 28.19
Q12 (d)—see paragraph 28.19(c)

Module 28—Employee Benefits

APPLY YOUR KNOWLEDGE

Apply your knowledge of the requirements for accounting and reporting employee benefits applying the *IFRS for SMEs* Standard by completing the case studies provided.

Once you have completed a case study, check your answers against those set out beneath it.

Case study 1

SME A started operations on 31 December 20X1.

Summarised information about its employees at 31 December 20X5 includes:

Employee category	*Number of employees in category*	*Salary level per employee for the 12-month period ending 30/06/20X6*	*Percentage wage increase effective from 01/07/20X6*
A	9	CU100,000	5%
B	200	CU50,000	7%
C	300	CU25,000	9%

Annual salary increases are expected to continue at the same rates for the foreseeable future.

At 31 December 20X5, the appropriate discount factors (determined using the current market yield for high quality corporate bonds in the jurisdiction in which SME A operates) are 0.9524 for a 12-month period, 0.9009 for a 24-month period, 0.8547 for a 36-month period and 0.8 for a 48-month period.

SME A's employees work a five-day week. SME A's operations close for the six mandatory public holidays of the jurisdiction in which SME A operates. Three of the public holidays are before 30 June.

Assume 261 working days in a year and that all holidays fall on a working day.

Holiday leave

SME A's employees are each entitled to 20 paid days of holiday leave per year.

Category A employees can carry forward unused holiday leave for one calendar year, calculated on a FIFO basis. Holiday leave not taken within that period is forfeited.

Category B employees cannot carry forward unused holiday leave but are paid for all holiday leave not used in the previous calendar year. The payment is made as part of the January payroll of the following year.

Category C employees cannot carry forward unused holiday leave and are not paid for unused holiday leave.

At 31 December 20X5, the entity's holiday leave records were as follows:

Employee category	*Number of employees in category*	*Average days' holiday leave per employee unused on 31/12/20X5*
A	9	10
B	200	6
C	300	8

At 31 December 20X5, SME A expects 25 days' holiday leave accumulated at 31 December 20X5 by employees in category A to expire unused on 31 December 20X6.

SME A expects that holiday leave will on average be taken evenly throughout the year.

Long-service awards

SME A's employees are entitled to receive government mandated long-service payments from SME A calculated at 5% of salary (as determined for the 12 months before the payment) at the end of each five-year period of continuous employment. The payment is made as part of the December payroll in the fifth year. SME A does not fund this obligation in advance.

Employee turnover is expected to follow average historical patterns. For ease of calculation assume that staff join and leave on 31 December. Furthermore, assume that none of the employees who joined SME A after 1 January 20X2 left or are expected to leave SME A in the foreseeable future (all leavers were employed on 31 December 20X1).

At 31 December 20X5, the entity's long-service award records were as follows:

Employee category	*Employee turnover on 31 December 20X5*		*Employee turnover on 31 December 20X4*		*Employee turnover on 31 December 20X3*		*Employee turnover on 31 December 20X2*		*Employed on 31/12/20X1*
	joined	left	joined	left	joined	Left	joined	left	
A	0	0	0	0	0	0	1	1	9
B	10	9	11	10	10	9	9	8	196
C	16	18	15	12	11	16	18	20	306

Pension plan

On 5 January 20X6, SME A paid a contribution of CU100,000 to a defined contribution plan in exchange for services performed by the entity's employees in December 20X5.

Voluntary redundancy offer

In December 20X5, with a view to reducing its workforce, SME A made an irrevocable offer to its employees of a voluntary redundancy package. In accordance with the offer SME A will compensate any employee who accepts voluntary redundancy on or before 30 June 20X6. The compensation offered is equal to the employee's annualised salary for the 12-month period ending 30 June 20X6.

At 31 December 20X5, SME A's voluntary redundancy records include:

Employee category	*Number of employees who accepted voluntary redundancy by 31/12/20X5*	*Number of employees expected to accept voluntary redundancy in 20X6*
A	0	1
B	2	8
C	5	25

Calculate SME A's liability for employee benefits at 31 December 20X5.

Answer to case study 1

At 31 December 20X5, SME A's liability for employee benefits is CU2,305,228, analysed as follows:

		CU
Short-term employee benefits	see calculation below	261,423
Other long-term employee benefits	see calculation below	593,807
Post-employment benefits—defined contribution plan		100,000
Termination benefits	see calculation below	1,350,000
Provision for employee benefits		**2,305,230**

Short-term employee benefits

At 31 December 20X5, the entity's liability for holiday leave is CU261,423 (CU26,127 for category A employees + CU235,296 for category B employees).

Category A: 32.5 days[(a)] × CU392.16[(b)] + 32.5 days[(a)] × CU411.76[(c)] = CU26,127.

Category B: 1,200 days[(e)] × CU196.08[(f)] = CU235,296.

Category C: CU0—non-accumulating and non-vesting.

Other long-term employee benefits

At 31 December 20X5, SME A's liability for long-service awards is CU593,807.

Calculation:

Category A employees CU34,148 (CU31,239[(g)] + CU2,909[(h)]) +

Category B employees CU320,000 (CU297,534[(i)] + CU10,371[(j)] + CU7,799[(k)] + CU4,296[(l)]) +

Category C employees CU239,659 (CU222,321[(m)] + CU10,113[(n)] + CU4,261[(o)] + CU2,964[(p)]).

Termination benefits

Employee category	*Estimated number of employees electing voluntary redundancy by 31/12/20X5*	*Annualised salary for the 12-month period ending 30/06/20X6*	*Termination benefits*
	(A)	*(B)*	*(C) = (A) × (B)*
A	1	CU100,000	CU100,000
B	10	CU50,000	CU500,000
C	30	CU 25,000	CU750,000
			CU1,350,000

(a) 9 employees × 10 days' holiday leave accumulated, on average = 90 days accumulated in total. 90 days less 25 days expected saving due to expiration = 65 days. 65 days accumulated holiday leave expected to be taken in 20X6, half (or 32.5 days' holiday leave) before 30 June 20X6 and 32.5 days' holiday leave after 1 July 20X6.

(b) CU100,000 annual salary ÷ 255[(d)] working days for the year = CU392.16 salary per working day from 1 January 20X6 to 30 June 20X6.

(c) CU100,000 annual salary + 5% × CU100,000 annual salary = CU105,000 expected annual salary from 1 July 20X6. CU105,000 ÷ 255[(d)] working days for the year = CU411.76 salary per working day from 1 July 20X6 to 31 December 20X6.

(d) 261 working days per year less 6 public holidays per year = 255 working days for the year.

(e) 200 employees × 6 days' holiday leave vested on average = 1,200 days vested in total. 1,200 days' vested holiday leave.

(f) CU50,000 annual salary ÷ 255(d) working days for the year = CU196.08 salary per working day.

(g) Category A employees expected to receive long-service payments in December 20X6: Expected salary for 20X5 CU50,000 (January to June) + CU52,500 (July to December) = CU102,500. 5% × CU102,500 × 8 employees × 4/5 (4 out of 5 years' service performed to date) = CU32,800 expected payment. CU32,800 × 0.9524 discount factor = CU31,239. Note: SME A did not anticipate savings due to category A employees leaving the employment of the entity.

(h) Category A employees expected to receive long-service payments in December 20X7: Expected salary for 20X6 CU52,500 (January to June) + CU55,125 (July to December) = CU107,625. 5% × CU107,625 × 1 employee (started service on 31 December 20X2) × 3/5 (3 out of 5 years' service performed to date) = CU3,229 expected payment. CU3,229 × 0.9009 discount factor = CU2,909. Note: SME A did not anticipate savings due to category A employees leaving the employment of the entity.

(i) Category B employees expected to receive long-service payments in December 20X6: Expected salary for 20X5 CU25,000 (January to June) + CU26,750 (July to December) = CU51,750. 5% × CU51,750 × 77%(q) × 196 (employees at 1 January 20X2) × 4/5 (4 out of 5 years' service performed to date) = CU312,405 . CU312,405 × 0.9524 discount factor = CU297,534.

(j) Category B employees expected to receive long-service payments in December 20X7: Expected salary for 20X6 CU26,750 (January to June) + CU28,623 (July to December) = CU55,373. 5% × CU55,373 × 77%(q) × 9 employees (started service on 31 December 20X2) × 3/5 (3 out of 5 years' service performed to date) = CU11,512 expected payment. CU11,512 × 0.9009 discount factor = CU10,371.

(k) Category B employees expected to receive long-service payments in December 20X8: Expected salary for 20X7 CU28,623 (January to June) + CU30,627 (July to December) = CU59,250. 5% × CU59,250 × 77%(q) × 10 employees (started service on 31 December 20X3) × 2/5 (2 out of 5 years' service performed to date) = CU9,125 expected payment. CU9,125 × 0.8547 discount factor = CU7,799.

(l) Category B employees expected to receive long-service payments in December 20X9: Expected salary for 20X8 CU30,627 (January to June) + CU32,771 (July to December) = CU63,398. 5% × CU63,398 × 77%(q) × 11 employees (started service on 31 December 20X4) × 1/5 (1 out of 5 years' service performed to date) = CU5,370 expected payment. CU5,370 × 0.8 discount factor = CU4,296.

(m) Category C employees expected to receive long-service payments in December 20X6: Expected salary for 20X5 CU12,500 (January to June) + CU13,625 (July to December) = CU26,125. 5% × CU26,125 × 73%(r) × 306 (employees at 1 January 20X2) × 4/5 (4 out of 5 years' service performed to date) = CU233,432 . CU233,432 × 0.9524 discount factor = CU222,321.

(n) Category C employees expected to receive long-service payments in December 20X7: Expected salary for 20X6 CU13,625 (January to June) + CU14,851 (July to December) = CU28,476. 5% × CU28,476 × 73%(r) × 18 employees (started service on 31 December 20X2) × 3/5 (3 out of 5 years' service performed to date) = CU11,225 expected payment. CU11,225 × 0.9009 discount factor = CU10,113.

(o) Category C employees expected to receive long-service payments in December 20X8: Expected salary for 20X7 CU14,851 (January to June) + CU16,188 (July to December) = CU31,039. 5% × CU31,039 × 73%(r) × 11 employees (started service on 31 December 20X3) × 2/5 (2 out of 5 years' service performed to date) = CU4,985 expected payment. CU4,985 × 0.8547 discount factor = CU4,261.

(p) Category C employees expected to receive long-service payments in December 20X9: Expected salary for 20X8 CU16,188 (January to June) + CU17,645 (July to December) = CU33,833. 5% × CU33,833 × 73%(r) × 15 employees (started service on 31 December 20X4) × 1/5 (1 out of 5 years' service performed to date) = CU3,705 expected payment. CU3,705 × 0.8 discount factor = CU2,964.

(q) SME A expects to pay approximately 77% × category B employees' long-service payments in a five-year cycle (a saving of 23% due to employees leaving before the long-service payment vests).

Calculation: 36 employees left in 20X2 to 20X5 (on average 9 per year). In the absence of evidence to the contrary, SME A assumed that 9 employees would leave in 20X6. 36 (20X2 to 20X5) + 9 (expected 20X6) = 45 employees expected to leave by 31 December 20X6. 45 ÷ 196 category B employees at 1 January 20X2 = expected 23% saving due to staff turnover of category B employees.

(r) SME A expects to pay approximately 73% × category C employees' long-service payments in a five-year cycle (a saving of 27% due to employees leaving before the long-service payment vests).

Calculation: 66 employees left in 20X2 to 20X5 (on average 16 per year). In the absence of evidence to the contrary, SME A assumed that 16 employees would leave in 20X6. 66 (20X2 to 20X5) + 16 (expected 20X6) = 82 employees expected to leave by 31 December 20X6. 82 ÷ 306 category C employees at 1 January 20X2 = expected 27% saving due to staff turnover of category C employees.

Case study 2

On 1 January 20X1, to encourage employees older than 60 years to extend their employment with the entity, SME B promises its 60-year-old employees a lump-sum benefit equal to 1% of final salary for each year of service they remain employed by SME B from and after their 60th birthday provided they remain in the employ of SME B until they are 65, at which time, in accordance with local laws, employees are required to retire. The benefit is payable to the employees on retirement.

Employee A turns 60 on 1 January 20X1. Her salary for the year ended 31 December 20X1 is CU100,000.

At 1 January 20X1, SME B made the following actuarial assumptions:

- Employee A's salary should increase by 5% (compound) each year.
- There is a 20% probability that employee A's employment with SME B will terminate before 1 January 20X6.
- The appropriate discount rate is 10% per year (determined applying paragraph 28.17).

There were no changes in the actuarial assumptions by 31 December 20X1.

Employee A's salary for 20X2 is CU105,000.

On 31 December 20X2, SME B revised its actuarial assumptions as follows:

- Employee A's salary should increase by 15% (compound) each year.
- There is a 10% probability that employee A's employment with SME B will terminate before reaching retirement date of 1 January 20X6.
- The appropriate discount rate remains 10% per year (determined applying paragraph 28.17).

The actuarial assumptions had not changed by 31 December 20X3. Employees salary for 20X3 increased by 15% in line with the actuarial assumption and is now CU120,750.

SME B does not fund its obligation to pay lump-sum benefits. It recognises actuarial gains and losses in other comprehensive income. Interest is recognised by SME B on an annual basis.

Part A
SME B uses the projected unit credit method to measure its defined benefit post-retirement obligation.

Calculate the amounts that SME B would recognise in profit or loss and in other comprehensive income for the year ended 31 December 20X1, 31 December 20X2 and 31 December 20X3.

Part B
The facts are the same as in part A. However, in this part, assume that the employee is not required to retire at 65 and that the benefit vests and is payable on the employee's 65th birthday.

Calculate the amounts that SME B would recognise in profit or loss and in other comprehensive income for the year ended 31 December 20X1 and 31 December 20X2.

Part C

The facts are the same as in Part A. However, in this part, assume that SME B is not able, without undue cost or effort, to use the projected unit credit method to measure its defined benefit obligation. It measures its defined benefit obligation using all of the simplifications permitted in paragraph 28.19.

Calculate the amounts that SME B would recognise in profit or loss and in other comprehensive income for the year ended 31 December 20X1 and 31 December 20X2.

Answer to case study 2

Part A

SME B follows an accounting policy of recognising actuarial gains and losses in other comprehensive income. All other components of the cost of the defined benefit plan are recognised in profit or loss.

For the year ended 31 December 20X1 SME A recognises a current service cost expense of CU664 in profit or loss.

Calculation:

	CU
Expected final salary (CU100,000 current salary × $(1.05)^4$)	121,551
Benefit for the current year at 1% of expected final salary (1% × CU121,551)	1,216
Adjustment for vesting condition (20% × CU1,216)	(244)
Benefit for the current year after adjustment for vesting condition	972
Present value factor of the 10% discount rate over 4 years (remaining period to which the benefit is expected to be settled)	0.683013
Current service cost	664

For the year ended 31 December 20X2, the period in which the actuarial assumptions changed, SME A recognises an expense of CU797 (CU731 current service cost + CU66 interest) in profit or loss and an actuarial loss of CU699 in other comprehensive income.

Calculations:

Current service cost

	CU
Expected final salary based on beginning of the year assumptions (CU105,000 current salary × $(1.05)^3$)	121,551
Benefit for the current year at 1% of expected final salary (1% × CU121,551)	1,216
Adjustment for vesting condition (20% × CU1,216)	(244)
Benefit for the current year after adjustment for vesting condition	972
Present value factor of the 10% discount rate over 3 years (remaining period to which the benefit is expected to be settled)	0.751315
Current service cost	731

Interest

	CU
Opening balance of the defined obligation	664
Interest, 10% of opening balance of the defined obligation	66

Actuarial loss

	CU
Expected final salary based on updated/end of the year assumptions (CU105,000 current salary × $(1.15)^3$)	159,692
Accumulated benefit before discounting (from years 20X1 to 20X2, CU159,692 × 1% × 2)	3,194
Adjustment for vesting condition (10% × CU3,194)	(319)
Accumulated benefit before discounting after adjustment for vesting condition	2,875
Present value factor of the 10% discount rate over 3 years (remaining period to which the benefit is expected to be settled)	0.751315
Closing balance of the defined obligation, 20X2	2,160
Opening balance of the defined obligation, 20X2	(664)
Current service cost	(731)
Interest	(66)
Actuarial loss	699

For the year ended 31 December 20X3 SME A recognises an expense of CU1,404 (CU1,188 current service cost + CU216 interest) in profit or loss. No actuarial gain or loss was recognised because there is no change in actuarial assumptions.

Calculations:

Current service cost

	CU
Expected final salary (CU120,750 salary in 20X3 × $(1.15)^2$)	159,692
Benefit for the current year at 1% of expected final salary (1% × CU159,692)	1,597
Adjustment for vesting condition (10% × CU1,597)	(160)
Benefit for the current year after adjustment for vesting condition	1,437
Present value factor of the 10% discount rate over 2 years (remaining period to which the benefit is expected to be settled)	0.826446
Current service cost	1,188

Interest

	CU
Opening balance of the defined obligation	2,160
Interest, 10% of opening balance of the defined obligation	216

Notes:

The following table shows how the obligation builds up for employee A, assuming that the only change in actuarial assumptions after 20X2 was the removal of uncertainty regarding vesting at the end of 20X5. The difference in amounts on the following table is due to rounding-off.

	20X1	*20X2*	*20X3*	*20X4*	*20X5*
Benefit attributed to:					
– prior years	-	1,596.92	3,193.84	4,790.76	6,387.68
– current year (1% × final salary)	1,215.51	1,596.92	1,596.92	1,596.92	1,596.92
– current and prior years	**1,215.51**	**3,193.84**	**4,790.76**	**6,387.68**	**7,984.60**
Opening obligation	**-**	**664.17**	**2,159.62**	**3,563.38**	**5,226.28**
Interest at 10%	-	66.42	215.96	356.34	522.63
Current service cost[(a)]	664.17	730.58	1,187.80	1,306.56	1,437.23
Actuarial loss (balancing figure)	-	698.45	-	-	798.46
Closing obligation[(b)]	**664.17**	**2,159.62**	**3,563.38**	**5,226.28**	**7,984.60**

(a) The current service cost is the present value of benefit attributed to the current year.

(b) The closing obligation is the present value of benefit attributed to current and prior years.

Part B

The answer to Part B is the same as the answer to Part A. However, in Part B the expense would be described as ‘other long-term benefit’ instead of ‘post-employment benefit’.

Part C

For the year ended 31 December 20X1 SME A recognises a current service cost expense of CU683 in profit or loss.

Calculation:

Benefit for the current year = 1% × CU100,000 current salary = CU1,000.

Present value = CU1,000 × $1/(1.1)^4$ = CU1,000 × 0.683013 = CU683.

For the year ended 31 December 20X2 SME A recognises an expense of CU857 (CU789 current service cost + CU68 interest) in profit or loss and an expense of CU38 (actuarial loss) in other comprehensive income.

Calculations:

Current service cost

Benefit for the current year = 1% × CU105,000 expected final salary = CU1,050.

Present value = CU1,050 × $1/(1.1)^3$ = CU1,050 × 0.751315 = CU789.

Interest

CU683 opening obligation × 10% = CU68.

Actuarial loss

Calculation of closing obligation

Benefit for 20X1 and 20X2 = 2 years × 1% × CU105,000 expected final salary = CU2,100.

Present value = CU2,100 × $1/(1.1)^3$ = CU2,100 × 0.751315 = CU1,578.

CU1,578 closing obligation less CU789 current service cost less CU68 interest less CU683 opening obligation = CU38 actuarial loss.

Note: the following table shows how the obligation builds up for employee A, assuming actuarial assumptions don't change after 20X2.

Year	*20X1*	*20X2*	*20X3*	*20X4*	*20X5*
1% × current salary	1,000	1,050	1,207.50	1,388.63	1,596.92
Years service at end of year	1	2	3	4	5
Future value of obligation	**1,000**	**2,100**	**3,622.50**	**5,554.50**	**7,984.60**
Discount factor (10%)	0.683013	0.751315	0.826446	0.909091	1
Present value of obligation	**683.01**	**1,577.76**	**2,993.80**	**5,049.56**	**7,984.60**
Opening obligation	**–**	**683.01**	**1,577.76**	**2,993.80**	**5,049.56**
Interest (10%)	–	68.30	157.78	299.38	504.96
Current service cost[a]	683.01	788.88	997.93	1,262.39	1,596.92
Actuarial gain or loss (balancing figure)	–	37.57	260.33	493.99	833.16
Closing obligation[b]	**683.01**	**1,577.76**	**2,993.80**	**5,049.56**	**7,984.60**

Notes:

[a] The current service cost is the present value of benefit attributed to the current year (including the effect of salary increases with respect to prior period service).

[b] The closing obligation is the present value of benefit attributed to current and prior years.

Case study 3

SME C provides its employees with two types of post-employment benefit—a final salary scheme pension benefit and a medical scheme. It recognises actuarial gains and losses arising from the defined benefit plans in profit or loss.

Pension benefit

SME C's employees and former employees are provided with pensions in accordance with SME C's defined benefit final salary pension scheme. The scheme provides a monthly pension of 0.25% of final salary for each year of service. The pension is payable from the age of 60. The pension plan is funded through payments to a separate legal entity set up for the sole purpose of paying pensions to its employees.

At 31 December 20X2, SME C's actuaries using the projected unit credit method measured the pension plan obligation at CU20,000 (20X1: CU17,000 and 20X0: CU16,500). The current service cost is CU900 for the year ended 31 December 20X2 (20X1: CU800) and interest cost attributable to the unwinding of the discount in the defined benefit obligation is CU860 (20X1: CU1,100).

The actual return on the pension plan assets for the year ended 31 December 20X2 is CU1,950 (20X1: CU1,900).

At 31 December 20X2, SME C determined the fair value of the pension plan assets at CU18,000 (20X1: CU16,000 and 20X0: CU14,000). The major categories of plan assets as a percentage of total plan assets are as follows:

	20X2	*20X1*
Jurisdiction A equities	25%	25%
Jurisdiction B equities	25%	18%
Jurisdiction A bonds	20%	30%
Jurisdiction B bonds	20%	17%
Jurisdiction A property	10%	10%

The plan assets include property occupied by SME C with a fair value of CU300 (20X1: CU250).

In 20X2 the pension fund paid pensions of CU750 (20X1: CU500) to past employees of SME C and SME C contributed CU800 (20X1: CU600) to the fund.

Medical scheme

SME C is also obliged to reimburse 10% of its employee's post-employment medical costs if the employee has provided 25 years or more of service to the group. SME C does not fund this obligation in advance.

At 31 December 20X2, SME C's actuaries determined the carrying amount of the medical plan obligation at CU7,000 (20X1: CU6,000 and 20X0: CU5,000). The current service cost is CU490 for the year ended 31 December 20X2 (20X1: CU430) and interest cost attributable to the unwinding of the discount in the defined benefit obligation is CU800 (20X1: CU750).

In 20X2 SME C paid CU600 (20X1: CU550) for past employee medical costs.

The principal actuarial assumptions applied by SME C at the end of the reporting period (expressed as weighted averages) are:

	20X2	*20X1*
Discount rate at 31 December	5%	6.5%
Expected rate of return on plan assets	3%	2%
Future salary increases	5%	4%
Future pension increases	3%	2%
Annual increase in healthcare costs	8%	8%
Future changes in maximum state healthcare benefits	3%	2%

Prepare an extract from the annual financial statements of SME C for the year ended 31 December 20X2 to record the information set out.

Answer to case study 3

Extract from SME C's group consolidated statement of financial position at 31 December 20X2:

Description	*Note*	*20X2*	*20X1*
LIABILITIES			
…			
Provision for post-employment benefits	18	CUXX,XXX	CUXX,XXX
…			

Extract from SME C's notes to the financial statements at 31 December 20X2:

Note 2 Accounting policies

Employee benefits—defined benefit post-employment plans

SME C has obligations to its employees and former employees to provide pensions in accordance with its defined benefit final salary pension scheme. The terms of the scheme oblige SME C to provide employees with a pension equal to 0.25% of the employee's final salary for every year of service provided. The defined benefit pension plan is funded by the entity through payments to a separate legal entity set up for the sole purpose of paying pensions to its employees.

SME C is also obliged to reimburse 10% of its employee's post-employment medical costs if the employee has provided 25 years or more of service to SME C. SME C does not fund this obligation in advance.

SME C measures defined benefit liabilities (assets) at the present value of its obligations under defined benefit plans at the reporting date minus the fair value at the reporting date of plan assets out of which the obligations are to be settled directly. The obligations under defined benefit plans are determined using the projected unit credit method. Actuarial gains and losses are recognised in profit or loss in the period in which they occur.

Note 18 Employee benefits

All amounts are presented in currency units 'CU''.

	20X2	*20X1*
…		
Post-employment plans—defined benefit liabilities	CU9,000	CU7,000
…		
Total liabilities for employee benefits	CUXX,XXX	CUXX,XXX

Post-employment plans—defined benefits plans

	Defined benefit pension plans		*Post-employment medical benefits*	
	20X2	*20X1*	*20X2*	*20X1*
Present value of funded obligations	20,000	17,000	-	-
Fair value of plan assets	(18,000)	(16,000)	-	-
Present value of unfunded obligations	-	-	7,000	6,000
Net liability	2,000	1,000	7,000	6,000

The most recent comprehensive actuarial valuation was performed as at 31 December 20X2.

The pension plan assets include property occupied by SME C with a fair value of CU300 (20X1: CU250).

The amounts recognised in profit or loss are:

	Defined benefit post-employment benefits	
	20X2	*20X1*
Defined benefit pension plan	1,800 [(a)]	(900) [(b)]
Post-employment medical benefits	1,600 [(c)]	1,550 [(d)]
Post-employment benefits	**3,400**	**650**

Changes in the present value of the defined benefit obligation are as follows:

	Defined benefit pension plans	*Post-employment medical benefits*	*Total*
	20X2	*20X2*	*20X2*
Defined benefit obligations at 01/01/20X2	17,000	6,000	23,000
Service cost	900	490	1,390
Interest cost	860	800	1,660
Actuarial losses (gains)	1,990 [(e)]	310 [(f)]	2,300
Benefits paid	(750)	(600)	(1,350)
Defined benefit obligations at 31/12/20X2	**20,000**	**7,000**	**27,000**

Changes in the fair value of plan assets are as follows:

	Defined benefit pension plans 20X2
Opening fair value of plan assets	16,000
Actual return on plan assets	1,950
Contributions by employer	800
Benefits paid	(750)
Closing fair value of plan assets	**18,000**

The major categories of plan assets as a percentage of total plan assets are as follows:

	20X2	*20X1*
Jurisdiction A equities	25%	25%
Jurisdiction B equities	25%	18%
Jurisdiction A bonds	20%	30%
Jurisdiction B bonds	20%	17%
Jurisdiction A property	10%	10%

Principal actuarial assumptions at the end of the reporting period (expressed as weighted averages):

	20X2	*20X1*
Discount rate at 31 December	5%	6.5%
Expected rate of return on plan assets	3%	2%
Future salary increases	5%	4%
Future pension increases	3%	2%
Annual increase in healthcare costs	8%	8%
Future changes in maximum state healthcare benefits	3%	2%

The calculations and explanatory notes below do not form part of the answer to this case study:

(a) CU900 pension current service cost + CU860 pension interest cost + CU1,990(e) pension actuarial loss less CU1,950 pension actual return on plan assets = CU1,800 expense.

(b) CU800 pension current service cost + CU1,100 pension interest cost less CU900(e) pension actuarial gain less CU1,900 pension actual return on plan assets = CU900 income.

(c) CU490 medical plan current service cost + CU800 medical plan interest cost + CU310(f) medical plan actuarial loss = CU1,600 expense.

(d) CU430 medical plan current service cost + CU750 medical plan interest cost + CU370(e) medical plan actuarial loss = CU1,550 expense.

(e) Calculation of actuarial gains (losses) on pension plan obligation:

	20X2	20X1
Pension plan obligation, closing balance	CU20,000	17,000
Add, pension fund paid to past employees	750	500
Less:		
Pension plan obligation, opening balance	(17,000)	(16,500)
Current service cost	(900)	(800)
Interest cost	(860)	(1,100)
Actuarial loss (gain)	CU1,990	(CU900)

(f) Calculation of actuarial gains (losses) on medical plan obligation:

	20X2	20X1
Medical plan obligation, closing balance	CU7,000	6,000
Add, medical benefits paid to past employees	600	550
Less:		
Medical plan obligation, opening balance	(6,000)	(5,000)
Current service cost	(490)	(430)
Interest cost	(800)	(750)
Actuarial loss	CU310	CU370