



To:	AASB Members	Date:	1 July 2013
From:	Kala Kandiah and Angus Thomson	Agenda Item:	11.1 (M132)
Subject:	Proposed amendments to AASB 119	File:	

Action

Subject to consideration of any further comments that might be received from AASB constituents, form preliminary views on the proposals in IASB ED/2013/4 *Defined Benefit Plans: Employee Contributions*, and decide on an approach for finalising the AASB's comment letter to the IASB.

Attachments

Agenda paper 11.2 – AASB ED 239 *Defined Benefit Plans: Employee Contributions* (which incorporates IASB ED/2013/4)

Agenda paper 11.3 – Full text of the two submissions¹ received on ED 239.

Background

1. The IFRS Interpretations Committee (IC) received two requests, in May and September 2012 respectively, seeking clarification of paragraph 93² of IAS 19 *Employee Benefits* (2011), which is effective for annual reporting periods beginning on or after 1 January 2013. The submitters requested guidance on the accounting for employee contributions in respect of service, in particular whether certain types of employee contributions to a defined benefit plan reduce short-term employee benefits cost instead of reducing post-employment benefits cost. The IC noted that the existing wording in paragraph 93 did not make this clear and at its January 2013 meeting, decided to propose that the IASB consider a narrow-scope amendment to IAS 19 to clarify the issue.
2. The IASB observed that contributions from employees or third parties to a defined benefit plan form part of the post-employment benefit rather than the short-term employee benefit and

1 The submissions are from the Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) and the Institute of Actuaries of Australia.

2 “Contributions from employees or third parties set out in the formal terms of the plan either reduce service cost (if they are linked to service), or reduce remeasurements of the net defined benefit liability (asset) (eg if the contributions are required to reduce a deficit arising from losses on plan assets or actuarial losses). Contributions from employees or third parties in respect of service are attributed to periods of service as a negative benefit in accordance with paragraph 70 (i.e. the net benefit is attributed in accordance with that paragraph).”

noted that contributions from employees or third parties to a defined benefit plan should be attributed to periods of service as a negative benefit. However, the IASB noted the general concern about the complexity of the required calculations and decided to propose adding a practical expedient to paragraph 93.

3. The IASB also observed that paragraph 93 of IAS 19 is unclear as to whether the back-end loading test in paragraph 70³ of IAS 19 should be performed on the net benefit, or on the gross benefit and the negative benefit separately. The IASB noted that performing the test on the net benefit would result in added complexity and decided to propose clarifying the issue by amending paragraph 93.

Overview of proposals

4. The IASB issued ED/2013/4 in March 2013, proposing to amend paragraph 93 so that contributions from employees or third parties as set out in the formal terms of a defined benefit plan may be excluded from being attributed to periods of service as a negative benefit and recognised as a reduction in the service cost in that period if, and only if, they are linked solely to the employee's service rendered in the same period in which they are payable. An example of a situation that qualifies for the practical expedient would be contributions that are a fixed percentage of an employee's salary, so the percentage of the employee's salary does not depend on the employee's number of years of service to the employer.
5. The IASB also proposes to specify in paragraph 93 that the negative benefit from contributions from employees or third parties should be attributed to periods of service in the same way that the gross benefit is attributed in accordance with paragraph 70, when they are not recognised as a reduction in the service cost in the same period in which they are payable.
6. AASB ED 239 incorporates IASB ED/2013/4. Comments on ED 239 were due by 24 June 2013. At the time of writing this memo, two submissions had been received (see Agenda Paper 10.3). AASB staff will provide a verbal update and table any further submissions received. Comments to the IASB on ED/2013/4 are due by 25 July 2013.

Preliminary staff views

7. Based on informal discussions with constituents from both the public sector and the private sector, AASB staff understand that employee contributions to defined benefit plans are reasonably common in Australia, and that notional contributions from employees are generally set out in the formal terms of the plan.
8. In forming a AASB staff recommendation to the Board, we noted (1) the comments from the Institute of Actuaries of Australia that the proposed amendment may be too narrow and only achieve its aim of avoiding the complexity of the required calculations and the potential confusion [paragraph BC4 of the ED] in some cases; and (2) the existing broad 'practical expedient' in the last sentence of paragraph 92 of AASB 119.

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- 3 In determining the present value of its defined benefit obligations and the related current service cost and, where applicable, past service cost, an entity shall attribute benefit to periods of service under the plan's benefit formula. However, if an employee's service in later years will lead to a materially higher level of benefit than in earlier years, an entity shall attribute benefit on a straight-line basis from:
 - (a) the date when service by the employee first leads to benefits under the plan (whether or not the benefits are conditional on further service) until
 - (b) the date when further service by the employee will lead to no material amount of further benefits under the plan, other than from further salary increases.

9. The Institute of Actuaries of Australia submission identifies cases other than where the contributions are linked solely to service rendered in that period. The Institute's suggests that, instead, the benchmark should be to allow employee or third party contributions to be treated as current service cost if they do not contribute to reducing a plan deficit.
10. The last sentence of paragraph 92 of IAS 19 states: "Discretionary contributions by employees or third parties reduce service cost upon payment of these contributions to the plan". Staff consider that this existing 'practical expedient' is potentially far wider in concept than the practical expedient being proposed by the IASB for employee or third party contributions that are part of the formal terms of the plan.
11. A concern with the Institute of Actuaries of Australia view is that it would potentially permit the allocation of amounts as adjustments to current service cost that have little to do with the provision of current service.
12. On balance, staff agree with the IASB proposal to amend paragraph 93 to allow entities to choose between accounting for contributions from employees or third parties either as a reduction in service cost in that period or as a negative benefit when applying the projected unit method, provided that these contributions are linked solely to the employee's service rendered in that period. We believe that such a practical expedient would provide helpful relief to constituents in accounting for simple plans like those where employees' contributions are a fixed percentage of employees' salaries.
13. Staff also agree with the IASB proposal to specify in paragraph 93 that the negative benefit from contributions from employees or third parties should be attributed to periods of service in the same way that the gross benefit is attributed in accordance with paragraph 70, when they are not recognised as a reduction in the service cost in the same period in which they are payable. We believe that attribution should be consistent between gross benefit and employee contributions to arrive at a net benefit and the clarification proposed should remove any confusion that currently exists.

Process for finalising Board submission

14. Staff recommend that, subject to the nature of any responses subsequently received, the submission be finalised out-of-session via the Chairman.

Questions to Board members:

1. Do you agree with staff's preliminary views on IASB ED/2013/4?
2. Do you agree to finalise AASB's submission to the IASB out-of-session via the Chairman?