ACCOUNTING STANDARD 15 (EMPLOYEE BENEFITS)

AS–15 – BRIEFLY EXPLAINED

- Deals with all employee benefits other than employee share based payments and includes:
  - Formal plans or agreements of companies with employees;
  - Legislative or industry requirements;
  - Informal practices that give rise to an obligation;
  - Whether paid to the employees, family, nominees or any trusts, insurance companies or association on their behalf.

AS–15 – CONTD….

- The standard classified benefits into four categories:
  - Short term employee benefits;
  - Post employment benefits;
  - Other long term employee benefits;
  - Termination benefits.

AS–15 – CONTD….

- Employee benefit plans are classified as below:

  <u>**Defined contribution plans**</u>

  Those post-employment benefit plans where the enterprises pay fixed contributions to a fund or separate entity and will have no further obligation if the fund does not hold sufficient assets to pay off all employee benefits

  <u>**Defined benefit plans**</u>

  Those post-employment benefit plans where the enterprises provide agreed benefits to the employees irrespective of the fund status.

  The standard prescribes actuarial valuation for defined benefit plans and other long term employee benefits

EXPECTATIONS FROM ACTUARIES

Accounting for Defined Benefit Plans involves :

- use of actuarial techniques to determine the amount employees earn in return of their service for the current and prior periods, expectations about demographic variables, financial variables affecting costs;
- Using Projected Unit Credit Method (PUC) to determine the present value of defined benefit obligation and current service cost;
- Determining the fair value of plan assets;
- Determining the amounts of actuarial gains and losses;
- In case of change of plan, the resulting past service cost;
- In case of curtailment/settlement, determining the resultant gain/loss

REQUIRED– PUC METHOD

The auditors' expect the use of Projected Unit Credit (PUC) method for the determination of liability being prescribed under AS 15.

Projected Unit Credit (PUC) Method

The PUC Method considers 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. The obligation arises as employees render services in return for post-employment benefits which an enterprise expects to pay in future reporting periods. These are then discounted to their present value. An enterprise discounts the whole of a post-employment benefit obligation, even if part of the obligation falls due within twelve months of the balance sheet date

ACTUARIAL ASSUMPTIONS

- Assumptions should be unbaised and mutually compatible.
- Financial assumptions such as discount rate, future salary and benefit levels, future medical costs, expected rate of return on plan assets, etc should be based on market expectations.
- Demographic assumptions like mortality rate, rate of employee turnover, disability, early retirement, proportion of plan members with eligible dependents, claim rates under medical plans, etc should be reliable.
- Discount rate should be determined with reference to market yields at the Balance Sheet date on Government Bonds and its currency and term should be consistent with that of the plan.
- Assumptions about medical costs should take account of estimated future changes in the cost of medical services, resulting from both inflation and specific changes in medical costs.

DISCLOSURES

The auditors' expect the presentation of the following items in the Actuarial Valuation report as these are required for disclosures in the financial statements as per Para 120 of AS 15:

- a reconciliation of opening and closing balances of the present value of the defined benefit obligation showing separately, if applicable, the effects during the period attributable to each of the following:
  - (i) current service cost,
  - (ii) interest cost,
  - (iii) contributions by plan participants,
  - (iv) actuarial gains and losses,
  - (v) foreign currency exchange rate changes on plans measured in a currency different from the enterprise's reporting currency,
  - (vi) benefits paid,
  - (vii) past service cost,
  - (viii) amalgamations,
  - (ix) curtailments, and
  - (x) settlements.

DISCLOSURES ….

- 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, the effects during the period attributable to each of the following:

(i) expected return on plan assets,
(ii) actuarial gains and losses,
(iii) foreign currency exchange rate changes on plans measured in a currency different from the enterprise's reporting currency,
(iv) contributions by the employer,
(v) contributions by plan participants,
(vi) benefits paid,
(vii) amalgamations, and
(viii) settlements.

DISCLOSURES ....

- the total expense recognised in the statement of profit and loss for each of the following, and the line item(s) of the statement of profit and loss in which they are included:
  (i) current service cost;
  (ii) interest cost;
  (iii) expected return on plan assets;
  (iv) expected return on any reimbursement right recognised as an asset
  (v) actuarial gains and losses;
  (vi) past service cost;
  (vii) the effect of any curtailment or settlement;
- a narrative description of the basis used to determine the overall expected rate of return on assets, including the effect of the major categories of plan assets.
- the actual return on plan assets, as well as the actual return on any reimbursement right recognised as an asset

DISCLOSURES ....

- the principal actuarial assumptions used as at the balance sheet date, including, where 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 return for the periods presented in the financial statements on any reimbursement right recognised as an asset
  (iv) medical cost trend rates;
  (v) estimates of future salary increases
  (vi) any other material actuarial assumptions used and factors like inflation, seniority, promotion, demand and supply factors of the employment market, etc affecting valuation.

An enterprise should disclose each actuarial assumption in absolute terms (for example, as an absolute percentage) and not just as a margin between different percentages or other variables.

DISCLOSURES ….

- the effect of an increase of one percentage point and the effect of a decrease of one percentage point in the assumed medical cost trend rates on:
  - (i) the aggregate of the current service cost and interest cost components of net periodic post-employment medical costs;and
  - (ii) the accumulated post-employment benefit obligation for medical costs.

For the purposes of this disclosure, all other assumptions should be held constant. For plans operating in a high inflation environment, the disclosure should be the effect of a percentage increase or decrease in the assumed medical cost trend rate of a significance similar to one percentage point in a low inflation environment.

- the amounts for the current annual period and previous **four** annual periods of:
  - (i) the present value of the defined benefit obligation, the fair value of the plan assets and the surplus or deficit in the plan;
  - (ii) the experience adjustments arising on:
    - (A) the plan liabilities expressed either as (1) an amount or (2) a percentage of the plan liabilities at the balance sheet date, and
    - (B) the plan assets expressed either as (1) an amount or (2) a percentage of the plan assets at the balance sheet date.
- the employer's best estimate, as soon as it can reasonably be determined, of contributions expected to be paid to the plan during the annual period beginning after the balance sheet date

VALUATION REPORTS - EXPECTATIONS

On the basis of few reports received for certain companies, it is noticed that the following information is inadequately provided in the valuation certificates:

- the amounts for the current annual period and previous **four** annual periods of:
  - (i) the present value of the defined benefit obligation, the fair value of the plan assets and the surplus or deficit in the plan;
  - (ii) the experience adjustments arising on:
    - (A) the plan liabilities expressed either as (1) an amount or (2) a percentage of the plan liabilities at the balance sheet date, and
    - (B) the plan assets expressed either as (1) an amount or (2) a percentage of the plan assets at the balance sheet date.
- the employer's best estimate, as soon as it can reasonably be determined, of contributions expected to be paid to the plan during the annual period beginning after the balance sheet date
- The following actuarial assumptions are required but are not available across all reports:
  - (i) Mortality rate
  - (ii) Withdrawl rate
- The discount rate used to compute present values is different across all companies. Since this is based on earnings on government bonds, this should be common but is normally not so.

THANK YOU