

Financial statements are prepared on the **accrual basis** of accounting. The **effects** of transactions and other events are recognised **when they occur** and not when cash or its equivalent is received or paid.

Employee benefits include benefits provided either to **Employees**, their **dependants**, or their **beneficiaries** and Employee includes **directors and other management personnel**.

Employee benefits may be settled by payments directly to the employees, their **spouses, children, other dependents or insurance companies**.

An employee may provide services on a Full time, part time, permanent, casual or temporary basis.

Types of Employee Benefits (STEB, PEB, LTEB, TB)	Reporting Period
1. <u>Short Term Employee Benefits (STEB)</u> - Settled within 12 months from end of R.P. (<i>Eg - Wages, Salaries, Profit Sharing, Paid Annual Leave, Paid Sick Leave, Non Monetary Benefits</i>). It is measured on an Undiscounted Basis . Remeasurement Gain or Loss is recognised in P/L .	
2. <u>Post Employee Benefits (PEB)</u> - Payable after completion of employment other than STEB or TB. (<i>Eg Pension, Gratuity, Provident Fund, Post Employment Medical Care</i>). It is discounted to Present Value. Remeasurement Gain or Loss recognised in OCI .	
3. <u>Other Long Term Employee Benefits (LTEB)</u> - Not expected to settle wholly before 12 months after end of Annual R.P. (<i>Eg - Long term paid absences, long term disability benefits, Profit sharing and bonuses etc.</i>). It is discounted to Present Value. Remeasurement Gain or Loss recognised in P/L and not in OCI .	
4. <u>Termination Benefits (TB)</u> - Dealt separately from other benefits because obligation is due to termination of employment rather than employee service. TB results from i) <i>Entity's decision to terminate or</i> ii) <i>Employee accepted entity's offer of benefits in exchange for termination.</i> <i>Termination at employee request without entity's offer are Post Employee Benefits</i>	

1. Short Term Compensated Absences

<p>A) <u>Accumulating</u></p> <p>i) <u>Vesting</u> - Cash Payment for Unutilised Leave)</p> <p>ii) <u>Non Vesting (Leave for Leave)</u> - Not entitled to Cash but Provision made for Leave on expectations regarding probability of utilisation of unused leaves by employees, Expected salary increase and Entity's restriction on Carry forward of leaves. <i>(ie Provision for the number of accumulated leaves expected to be utilised in future)</i></p>
<p>B) Non Accumulating - Leaves cannot be carried forward and expires. (No A/c treatment)</p>

Refer ill 7 & 8

Profit Sharing and Bonus plan recognised only when Entity has present legal or constructive obligation to pay as a result of past events and Reliable Estimate of Obligation can be made.

- If settled before 12m after the end of Annual R.P. - **Short term employee benefits**
- If not settled before 12m after the end of Annual R.P. - **Long term employee benefits.**

2. Post Employment Benefits (PEB)

PEBs are classified as either - i) Defined contribution Plan or ii) Defined Benefit Plans.

<u>Defined contribution Plan (DCP)</u>	<u>Defined Benefit Plan (DBP)</u>
1. Entity's Legal or Constructive Obligation limited to contribution of Amount to the fund. 2. Actuarial or Investment Risk fall to employee. (ie Entity's obligation only to contribute)	1. Entity's obligation to provide agreed benefits to current & former employees. 2. Actuarial Risk or Investment Risk fall to Employer (ie Entity). If such risk gets worsen, Entity's obligation may increase. (ie final settlement obligation to entity) 3. Defined Benefit Plan can be Funded (in Plan Asset) or Non Funded.

Exceptions to DCP (Means it will be classified as DBP) -

1. Guarantee of a specified return on contribution.
2. Entity has history of increasing benefits for former employees to keep pace with inflation even if there is no legal obligation.
3. Entity provides further contribution if assets are insufficient to meet the benefits.

In Defined Benefit Plan Actuarial Valuation is done applying Projected Unit Credit Method (Refer practical example on Class Notes).

Accounting of Defined Contribution Plan

The obligations are measured on undiscounted basis. No actuarial assumptions are required and there is no possibility of any actuarial gain or loss

i) When employee has rendered service during a period and

<u>Contributions Paid</u>		<u>Contributions Payable</u>	
Employee Benefit Expenses (P/L)	Dr	Employee Benefit Expenses (P/L)	Dr
To Bank		To Accrued Expense (liability)	

ii) If Expenses included in the cost of an asset as per other Ind AS (Eg Ind As 2 or Ind As 16)

Employee Benefit Expenses (capitalised to PPE or Inventory) → PPE / Inventory
 To Bank or Accrued Expenses → TO EBE

iii) If Contributions paid in Advance - Expenses not yet accrued.

Prepaid Expenses (Asset)
 To Bank or ~~Accrued Expenses~~

Accounting of Defined Benefit Plan

Step 1 - Determining the Deficit or Surplus

1. This involves using Actuarial technique (PUCM) to make reliable estimate of Amount of benefit that employees have earned in return for their service in current and prior periods.

- Discounting that benefit in order to determine PVDBO and Current Service Cost.
- Deducting Fair value of any plan assets from PVDBO.

Step 2 - Determining Amount of Net Defined Benefit Liability (Asset)

Net Defined Benefit Liability (Asset) is the amount of deficit or surplus determined in step 1 adjusted for any effect of Asset ceiling.

Step 3 - Determine Amount to be recognised in Profit or loss

- Current Service Cost
- Any Past Service Cost and Gain or loss on settlement.
- Net Interest on Net Defined Benefit Liability (Asset).

Step 4 - Determining Remeasurement of Net Defined Benefit Liability (Asset), to be recognised in Other Comprehensive Income, comprising

- Actuarial gains and losses
- Return on Plan Assets excluding Net Interest on Net Defined Benefit Liability (Asset).
- Any change in effect of Asset ceiling Net Interest on Net Defined Benefit Liability (Asset).

Key Points Meaning

- Current service cost** - Increase in PVDBO from employee service in current period
- Past service cost** - Change in PVDBO for employee service in prior period resulting from plan amendment or curtailment.
- Net Interest on NDBL/NDBA (Time Basis)** - Change in Net defined benefit liability (asset) that arises from passage of time.
- Remeasurement of NDBL/NDBA** - comprises Actuarial Gain/loss, Return on Plan Asset excl Net Interest on NDBA/NDBL. $Actuarial\ net = Exp. net \pm actuarial\ gain/loss$
- Net defined benefit liability (NDBL)** - PVDBO less Plan Asset $Eq. PVDBO = 500000, PA = 400000 \therefore NDBL = 100000$
- Net defined benefit Asset (NDBA)** - Lower of Surplus (ie Plan Asset less PVDBO) or Asset ceiling
 $PVDBO = 500000, PA = 650000, Surplus = 150000$

Case 1 Asset ceiling = 200000	Case 2 Asset ceiling = 120000
NDBA = 150000	NDBA = 120000

Other Key Points

Past Service Cost (PSC) - Change in PVDBO resulting from **Modifications, Plan Amendment or Curtailment** is known as Past Service Cost. PSC recognizes as Expense as Earlier of:

- When Plan **Amendments or Curtailment** Occurs, or
- When entity recognizes related **restructuring cost or termination benefits**.

Plan Assets - Financial Assets held in a retirement plan and used to generate income to fund the plan (Eg of plan assets can include **stocks, bonds, and mutual fund inv.**). It Comprise -

- Assets held by Long Term Employee Benefit Fund which exists solely to pay or fund employee benefits.
- Qualifying Insurance Policies issued by an insurer whose proceeds can be used only to pay or fund employee benefits.

Those Assets are not available to reporting entity's own creditors even in bankruptcy.

Net defined benefit liability = PVDBO less Plan Asset (where PVDBO > Plan Asset)

Net defined benefit Asset = Surplus or Asset Ceiling whichever is lower

if plan asset > PVDBO

Discount Rate is determined by reference to market yield on Govt bonds at R.P. end.

For Subsidiaries, Associates, Joint Venture & Branches outside india, Discount Rate is determined by reference to market yield on high quality corporate bonds.

If there is no deep markets, Market rate on Govt bonds of that country shall be used.

Curtailment & Settlement

Curtailment arises when entity significantly reduces no. of employees covered by the plan. It may arise due to closing of a plant, discontinuance of an operation or termination or suspension of a plan. Curtailment reduces PVDBO

A Settlement occurs when entity enters into transaction that eliminates all further legal or constructive obligation (Gain or Loss = PV of obligation settled LESS Settlement Price)

Cash Paid or Plan Assets tfd.

3. Other Long Term Employee Benefits *Defined Cont? Plan | Defined Benefit Plan*

Accounting of LTEB is same as PEB except that Remeasurement Gain or Loss is recognised In P/L instead of OCI. The reason is degree of uncertainty in case of LTEB is less as compared to PEB.

4. Termination Benefits

i) Entity's decision to terminate or ii) Employee accepted entity's offer of benefits in exchange for termination.

Note

1. Benefits paid should not be conditional on future services being provided by employees.

2. An Entity recognises expenses and liability for termination at earlier of -
 a) when entity can no longer withdraw offer of benefits
 b) When entity recognises Restructuring Cost and involves payment of termination benefits.

3. If TB expected to be settled wholly before 12m after end of R.P. - Apply **STEB** Requirements

4. If TB **not** expected to be settled wholly before 12m after end of R.P - Apply **LTEB** Requirements

Example: On Termination Benefits

As a result of a recent acquisition, an entity plans to close a factory in ten months and, at that time, terminate the employment of all of the remaining employees at the factory. Because the entity needs the expertise of the employees at the factory to complete some contracts, it announces a plan of termination as follows.

Each employee who stays and renders service until the closure of the factory will receive on the termination date a cash payment of 30,000. Employees leaving before closure of the factory will receive 10,000. $FG = 10000$, $SG = 20000$

There are 120 employees at the factory. At the time of announcing the plan, the entity expects 20 of them to leave before closure. Therefore, the total expected cash outflows under the plan are 3,200,000 (i.e., $20 \times 10,000 + 100 \times 30,000$).

As required by paragraph 160, the entity accounts for benefits provided in exchange for termination of employment as termination benefits and accounts for benefits provided in exchange for services as short-term employee benefits. $20 \times 10000 + 100 \times 30000 =$

$FG = 1200000$
involvement

$SG = 2000000$

over a period of service i.e. 10 months
200000 per month.

$= 2000000$
FG

$100 \times 10000 = 1000000$ (FG)
 $100 \times 20000 = 2000000$ (SG)

Termination benefits

The benefit provided in exchange for termination of employment is 10,000. This is the amount that an entity would have to pay for terminating the employment regardless of whether the employees stay and render service until closure of the factory or they leave before closure. Even though the employees can leave before closure, the termination of all employees' employment is a result of the entity's decision to close the factory and terminate their employment (i.e., all employees will leave employment when the factory closes). Therefore, the entity recognises a liability of 1,200,000 (i.e. $120 \times 10,000$) for the termination benefits provided in accordance with the employee benefit plan at the earlier of when the plan of termination is announced and when the entity recognises the restructuring costs associated with the closure of the factory.

Benefits provided in exchange for service Accrued

The incremental benefits that employees will receive if they provide services for the full ten-month period are in exchange for services provided over that period. The entity accounts for them as short-term employee benefits because the entity expects to settle them before twelve months after the end of the annual reporting period. In this example, discounting is not required, so an expense of 200,000 (i.e. $2,000,000 \div 10$) is recognised in each month during the service period of ten months, with a corresponding increase in the carrying amount of the liability.

ATTRIBUTING BENEFITS TO PERIOD OF SERVICE:

An entity shall attribute benefit to periods of service under the plan's benefit formula, in determining the PVDBO and the related current service cost, and, where applicable, past service cost.

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:

- 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
- 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.

Although, certain post-employment benefits, for example, post-employment medical benefits, become payable only if a specified event occurs when an employee is no longer employed, an obligation is created when the employee renders service that will provide entitlement to the benefit if the specified event occurs.

Closing PVDBO on B/s = Opening PVDBO + Interest cost + CSC + PSC - Benefits Paid +- Actuarial gain or loss

Closing Plan Asset on B/s = Opening Plan Asset + Interest Income + Contribution - Benefits paid +- Actuarial gain or loss.