

SSAP 34
STATEMENT OF STANDARD ACCOUNTING PRACTICE 34
EMPLOYEE BENEFITS

(Issued December 2001; revised August 2002 and May 2003 in shaded type)

*The standards, which have been set in **bold italic type**, should be read in the context of the background material and implementation guidance and in the context of the Foreword to Statements of Standard Accounting Practice, Interpretations and Accounting Guidelines. Statements of Standard Accounting Practice are not intended to apply to immaterial items (see paragraph 8 of the Foreword).*

Objective

The objective of this Statement is to prescribe the accounting and disclosure for employee benefits. The Statement requires an enterprise to recognise:

- (a) a liability when an employee has provided service in exchange for employee benefits to be paid in the future; and
- (b) an expense when the enterprise consumes the economic benefit arising from service provided by an employee in exchange for employee benefits.

Scope

1. ***This Statement should be applied by an employer in accounting for employee benefits.***
2. This Statement does not deal with reporting by employee benefit plans (see Accounting Guideline 2.302, Financial Statements of Retirement Schemes).
3. This Statement applies to all employee benefits, including those provided:
 - (a) under formal plans or other formal agreements between an enterprise and individual employees, groups of employees or their representatives;
 - (b) under legislative requirements, or through industry arrangements, whereby enterprises are required to contribute to national, state, industry or other multi-employer plans; or
 - (c) by those informal practices that give rise to a constructive obligation. Informal practices give rise to a constructive obligation where the enterprise has no realistic alternative but to pay employee benefits. An example of a constructive obligation is where a change in the enterprise's informal practices would cause unacceptable damage to its relationship with employees.
4. Employee benefits include:
 - (a) short-term employee benefits, such as wages, salaries and social security contributions, paid annual leave and paid sick leave, profit sharing and bonuses (if payable within twelve months of the end of the period) and non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees;
 - (b) post-employment benefits such as pensions, other retirement benefits, post-employment life insurance and post-employment medical care;

- (c) other long-term employee benefits, including long-service leave or sabbatical leave, jubilee or other long-service benefits, long-term disability benefits and, if they are not payable wholly within twelve months after the end of the period, profit sharing, bonuses and deferred compensation;
- (d) termination benefits; and
- (e) equity compensation benefits.

Because each category identified in (a) to (e) above has different characteristics, this Statement establishes separate requirements for each category.

- 5. Employee benefits include benefits provided to either employees or their dependants and may be settled by payments (or the provision of goods or services) made either directly to the employees, to their spouses, children or other dependants or to others, such as insurance companies.
- 6. An employee may provide services to an enterprise on a full time, part time, permanent, casual or temporary basis. For the purpose of this Statement, employees include directors and other management personnel.

Definitions

- 7. *The following terms are used in this Statement with the meanings specified:*

Employee benefits are all forms of consideration given by an enterprise in exchange for service rendered by employees.

Short-term employee benefits are employee benefits (other than termination benefits and equity compensation benefits) which fall due wholly within twelve months after the end of the period in which the employees render the related service.

Post-employment benefits are employee benefits (other than termination benefits and equity compensation benefits) which are payable after the completion of employment.

Post-employment benefit plans are formal or informal arrangements under which an enterprise provides post-employment benefits for one or more employees.

Defined contribution plans are post-employment benefit plans under which an enterprise pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods.

Defined benefit plans are post-employment benefit plans other than defined contribution plans.

Multi-employer plans are defined contribution plans (other than state plans) or defined benefit plans (other than state plans) that:

- (a) *pool the assets contributed by various enterprises that are not under common control; and*
- (b) *use those assets to provide benefits to employees of more than one enterprise, on the basis that contribution and benefit levels are determined without regard to the identity of the enterprise that employs the employees concerned.*

Other long-term employee benefits are employee benefits (other than post-employment benefits, termination benefits and equity compensation benefits) which do not fall due wholly within twelve months after the end of the period in which the employees render the related service.

Termination benefits are employee benefits payable as a result of either:

- (a) an enterprise's decision to terminate an employee's employment before the normal retirement date; or
- (b) an employee's decision to accept voluntary redundancy in exchange for those benefits.

Equity compensation benefits are employee benefits under which either:

- (a) employees are entitled to receive equity financial instruments issued by the enterprise (or its parent); or
- (b) the amount of the enterprise's obligation to employees depends on the future price of equity financial instruments issued by the enterprise.

Equity compensation plans are formal or informal arrangements under which an enterprise provides equity compensation benefits for one or more employees.

Vested employee benefits are employee benefits that are not conditional on future employment.

The **present value of a 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.

Current service cost is the increase in the present value of the defined benefit obligation resulting from employee service in the current period.

Interest cost is the increase during a period in the present value of a defined benefit obligation which arises because the benefits are one period closer to settlement.

Plan assets comprise:

- (a) assets held by a long-term employee benefit fund; and
- (b) qualifying insurance policies.

Assets held by a long-term employee benefit fund are assets (other than non-transferable financial instruments issued by the reporting enterprise) that:

- (a) are held by an entity (a fund) that is legally separate from the reporting enterprise and exists solely to pay or fund employee benefits; and
- (b) are available to be used only to pay or fund employee benefits, are not available to the reporting enterprise's own creditors (even in bankruptcy), and cannot be returned to the reporting enterprise, unless either:
 - (i) the remaining assets of the fund are sufficient to meet all the related employee benefit obligations of the plan or the reporting enterprise; or
 - (ii) the assets are returned to the reporting enterprise to reimburse it for employee benefits already paid.

A **qualifying insurance policy** is an insurance policy issued by an insurer that is not a related party (as defined in SSAP 20, Related Party Disclosures) of the reporting enterprise, if the proceeds of the policy:

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

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

- (i) the proceeds represent surplus assets that are not needed for the policy to meet all the related employee benefit obligations; or*
- (ii) the proceeds are returned to the reporting enterprise to reimburse it for employee benefits already paid.*

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction.

The return on plan assets is interest, dividends and other revenue derived from the plan assets, together with realised and unrealised gains or losses on the plan assets, less any costs of administering the plan and less any tax payable by the plan itself.

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.*

Past service cost is the increase in the present value of the defined benefit obligation for employee service in prior periods, resulting in the current period from the introduction of, or changes to, post-employment benefits or other long-term employee benefits. Past service cost may be either positive (where benefits are introduced or improved) or negative (where existing benefits are reduced).

Short-term Employee Benefits

8. Short-term employee benefits 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) where 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.
9. Accounting for short-term employee benefits is generally straightforward because no actuarial assumptions are required to measure the obligation or the cost and there is no possibility of any actuarial gain or loss. Moreover, short-term employee benefit obligations are measured on an undiscounted basis.

Recognition and Measurement

All Short-term Employee Benefits

10. *When an employee has rendered service to an enterprise during an accounting period, the enterprise should recognise the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service:*

- (a) *as a liability (accrued expense), after deducting any amount already paid. If the amount already paid exceeds the undiscounted amount of the benefits, an enterprise should recognise that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and*
- (b) *as an expense, unless another Statement of Standard Accounting Practice requires or permits the inclusion of the benefits in the cost of an asset (see, for example, SSAP 22, Inventories, and SSAP 17, Property, Plant and Equipment).*

Paragraphs 11, 14 and 17 explain how an enterprise should apply this requirement to short-term employee benefits in the form of compensated absences and profit sharing and bonus plans.

Short-term Compensated Absences

11. *An enterprise should recognise the expected cost of short-term employee benefits in the form of compensated absences under paragraph 10 as follows:*
 - (a) *in the case of accumulating compensated absences, when the employees render service that increases their entitlement to future compensated absences; and*
 - (b) *in the case of non-accumulating compensated absences, when the absences occur.*
12. An enterprise may compensate employees for absence for various reasons including vacation, sickness and short-term disability, maternity or paternity, jury service and military service. Entitlement to compensated absences falls into two categories:
 - (a) accumulating; and
 - (b) non-accumulating.
13. Accumulating compensated absences are those that are carried forward and can be used in future periods if the current period's entitlement is not used in full. Accumulating compensated absences may be either vesting (in other words, employees are entitled to a cash payment for unused entitlement on leaving the enterprise) or non-vesting (when employees are not entitled to a cash payment for unused entitlement on leaving). An obligation arises as employees render service that increases their entitlement to future compensated absences. The obligation exists, and is recognised, even if the compensated absences are non-vesting, although the possibility that employees may leave before they use an accumulated non-vesting entitlement affects the measurement of that obligation.
14. *An enterprise should measure the expected cost of accumulating compensated absences as the additional amount that the enterprise expects to pay as a result of the unused entitlement that has accumulated at the balance sheet date.*
15. The method specified in the previous paragraph measures the obligation at the amount of the additional payments that are expected to arise solely from the fact that the benefit accumulates. In many cases, an enterprise may not need to make detailed computations to estimate that there is no material obligation for unused compensated absences. For example, a sick leave obligation is likely to be material only if there is a formal or informal understanding that unused paid sick leave may be taken as paid vacation.

Example Illustrating Paragraphs 14 and 15

An enterprise has 100 employees, who are each entitled to five working days of paid sick leave for each year. Unused sick leave may be 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 (a LIFO basis). At 31 December 20X1, the average unused entitlement is two days per employee. The enterprise expects, based on past experience which is expected to continue, that 92 employees will take no more than five days of paid sick leave in 20X2 and that the remaining 8 employees will take an average of six and a half days each.

The enterprise expects that it will pay an additional 12 days of sick pay as a result of the unused entitlement that has accumulated at 31 December 20X1 (one and a half days each, for 8 employees). Therefore, the enterprise recognises a liability equal to 12 days of sick pay.

16. Non-accumulating compensated absences do not carry forward: they lapse if the current period's entitlement is not used in full and do not entitle employees to a cash payment for unused entitlement on leaving the enterprise. This is commonly the case for sick pay (to the extent that unused past entitlement does not increase future entitlement), maternity or paternity leave and compensated absences for jury service or military service. An enterprise recognises no liability or expense until the time of the absence, because employee service does not increase the amount of the benefit.

Profit Sharing and Bonus Plans

17. *An enterprise should recognise the expected cost of profit sharing and bonus payments under paragraph 10 when, and only when:*
- (a) *the enterprise has a present legal or constructive obligation to make such payments as a result of past events; and*
 - (b) *a reliable estimate of the obligation can be made.*
- A present obligation exists when, and only when, the enterprise has no realistic alternative but to make the payments.*
18. Under some profit sharing plans, employees receive a share of the profit only if they remain with the enterprise for a specified period. Such plans create a constructive obligation as employees render service that increases the amount to be paid if they remain in service until the end of the specified period. The measurement of such constructive obligations reflects the possibility that some employees may leave without receiving profit sharing payments.

Example Illustrating Paragraph 18

A profit sharing plan requires an enterprise to pay a specified proportion of its net profit for the year to employees who serve throughout the year. If no employees leave during the year, the total profit sharing payments for the year will be 3% of net profit. The enterprise estimates that staff turnover will reduce the payments to 2.5% of net profit.

The enterprise recognises a liability and an expense of 2.5% of net profit.

19. An enterprise may have no legal obligation to pay a bonus. Nevertheless, in some cases, an enterprise has a practice of paying bonuses. In such cases, the enterprise has a constructive obligation because the enterprise has no realistic alternative but to pay the bonus. The measurement of the constructive obligation reflects the possibility that some employees may leave without receiving a bonus.

20. An enterprise can make a reliable estimate of its legal or constructive obligation under a profit sharing or bonus plan when, and only when:
- (a) the formal terms of the plan contain a formula for determining the amount of the benefit;
 - (b) the enterprise determines the amounts to be paid before the financial statements are authorised for issue; or
 - (c) past practice gives clear evidence of the amount of the enterprise's constructive obligation.
21. An obligation under profit sharing and bonus plans results from employee service and not from a transaction with the enterprise's owners. Therefore, an enterprise recognises the cost of profit sharing and bonus plans not as a distribution of net profit but as an expense.
22. If profit sharing and bonus payments are not due wholly within twelve months after the end of the period in which the employees render the related service, those payments are other long-term employee benefits (see paragraphs ~~129-134~~126 - 131). If profit sharing and bonus payments meet the definition of equity compensation benefits, an enterprise treats them under paragraphs ~~147-155~~144 - 152.

Disclosure

23. Although this Statement does not require specific disclosures about short-term employee benefits, other Statements of Standard Accounting Practice may require disclosures. For example, where required by SSAP 20, Related Party Disclosures, an enterprise discloses information about employee benefits for key management personnel. SSAP 1, Presentation of Financial Statements, requires that an enterprise should disclose staff costs.

Post-employment Benefits: Distinction between Defined Contribution Plans and Defined Benefit Plans

24. 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 enterprise provides post-employment benefits are post-employment benefit plans. An enterprise applies this Statement to all such arrangements whether or not they involve the establishment of a separate entity to receive contributions and to pay benefits.

25. Post-employment benefit plans are classified as either defined contribution plans or defined benefit plans, depending on the economic substance of the plan as derived from its principal terms and conditions. Under defined contribution plans:
- (a) the enterprise's legal or constructive obligation is limited to the amount that it agrees to contribute to the fund. Thus, the amount of the post-employment benefits received by the employee is determined by the amount of contributions paid by an enterprise (and perhaps also the employee) to a post-employment benefit plan or to an insurance company, together with investment returns arising from the contributions; and
 - (b) in consequence, actuarial risk (that benefits will be less than expected) and investment risk (that assets invested will be insufficient to meet expected benefits) fall on the employee.

26. Examples of cases where an enterprise's obligation is not limited to the amount that it agrees to contribute to the fund are when the enterprise has a legal or constructive obligation through:
- (a) a plan benefit formula that is not linked solely to the amount of contributions;
 - (b) a guarantee, either indirectly through a plan or directly, of a specified return on contributions; or
 - (c) those informal practices that give rise to a constructive obligation. For example, a constructive obligation may arise where an enterprise has a history of increasing benefits for former employees to keep pace with inflation even where there is no legal obligation to do so.
27. Under defined benefit plans:
- (a) the enterprise's obligation is to provide the agreed benefits to current and former employees; and
 - (b) actuarial risk (that benefits will cost more than expected) and investment risk fall, in substance, on the enterprise. If actuarial or investment experience are worse than expected, the enterprise's obligation may be increased.
28. Paragraphs 29 to 42 below explain the distinction between defined contribution plans and defined benefit plans in the context of multi-employer plans, state plans and insured benefits.

Multi-employer Plans

29. *An enterprise should classify a multi-employer plan as a defined contribution plan or a defined benefit plan under the terms of the plan (including any constructive obligation that goes beyond the formal terms). Where a multi-employer plan is a defined benefit plan, an enterprise should:*
- (a) *account for its proportionate share of the defined benefit obligation, plan assets and cost associated with the plan in the same way as for any other defined benefit plan; and*
 - (b) *disclose the information required by paragraph ~~123~~120.*
30. *When sufficient information is not available to use defined benefit accounting for a multi-employer plan that is a defined benefit plan, an enterprise should:*
- (a) *account for the plan under paragraphs 44 - 46 as if it were a defined contribution plan;*
 - (b) *disclose:*
 - (i) *the fact that the plan is a defined benefit plan; and*
 - (ii) *the reason why sufficient information is not available to enable the enterprise to account for the plan as a defined benefit plan; and*
 - (c) *to the extent that a surplus or deficit in the plan may affect the amount of future contributions, disclose in addition:*
 - (i) *any available information about that surplus or deficit;*
 - (ii) *the basis used to determine that surplus or deficit; and*
 - (iii) *the implications, if any, for the enterprise.*

31. One example of a defined benefit multi-employer plan is one where:
- (a) the plan is financed on a pay-as-you go basis such that: contributions are set at a level that is expected to be sufficient to pay the benefits falling due in the same period; and future benefits earned during the current period will be paid out of future contributions; and
 - (b) employees' benefits are determined by the length of their service and the participating enterprises 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 enterprise: if the ultimate cost of benefits already earned at the balance sheet date is more than expected, the enterprise will have to either increase its contributions or persuade employees to accept a reduction in benefits. Therefore, such a plan is a defined benefit plan.
32. Where sufficient information is available about a multi-employer plan which is a defined benefit plan, an enterprise accounts for its proportionate share of the defined benefit obligation, plan assets and post-employment benefit cost associated with the plan in the same way as for any other defined benefit plan. However, in some cases, an enterprise may not be able to identify its share of the underlying financial position and performance of the plan with sufficient reliability for accounting purposes. This may occur if:
- (a) the enterprise does not have access to information about the plan that satisfies the requirements of this Statement; or
 - (b) the plan exposes the participating enterprises to actuarial risks associated with the current and former employees of other enterprises, with the result that there is no consistent and reliable basis for allocating the obligation, plan assets and cost to individual enterprises participating in the plan.
- In those cases, an enterprise accounts for the plan as if it were a defined contribution plan and discloses the additional information required by paragraph 30.
33. Multi-employer plans are distinct from group administration plans. A group administration plan is merely an aggregation of single employer plans combined to allow participating employers to pool their assets for investment purposes and reduce investment management and administration costs, but the claims of different employers are segregated for the sole benefit of their own employees. Group administration plans pose no particular accounting problems because information is readily available to treat them in the same way as any other single employer plan and because such plans do not expose the participating enterprises to actuarial risks associated with the current and former employees of other enterprises. The definitions in this Statement require an enterprise to classify a group administration plan as a defined contribution plan or a defined benefit plan in accordance with the terms of the plan (including any constructive obligation that goes beyond the formal terms).
34. Defined benefit plans that pool the assets contributed by various enterprises under common control, for example a parent and its subsidiaries, are not multi-employer plans. Therefore, an enterprise treats all such plans as defined benefit plans.
35. SSAP 28, Provisions, Contingent Liabilities and Contingent Assets, requires an enterprise to recognise, or disclose information about, certain contingent liabilities. In the context of a multi-employer plan, a contingent liability may arise from, for example:
- (a) actuarial losses relating to other participating enterprises because each enterprise that participates in a multi-employer plan shares in the actuarial risks of every other participating enterprise; or
 - (b) any responsibility under the terms of a plan to finance any shortfall in the plan if other enterprises cease to participate.

State Plans

36. *An enterprise should account for a state plan in the same way as for a multi-employer plan (see paragraphs 29 and 30).*
37. State plans are established by legislation to cover all enterprises (or all enterprises in a particular category, for example a specific industry) and are operated by national or local government or by another body (for example an autonomous agency created specifically for this purpose) which is not subject to control or influence by the reporting enterprise. Some plans established by an enterprise provide both compulsory benefits which substitute for benefits that would otherwise be covered under a state plan and additional voluntary benefits. Such plans are not state plans.
38. State plans are characterised as defined benefit or defined contribution in nature based on the enterprise's obligation under the plan. Many state plans are funded on a pay-as-you go basis: contributions are set at a level that is expected to be sufficient to pay the required benefits falling due in the same period; future benefits earned during the current period will be paid out of future contributions. Nevertheless, in most state plans, the enterprise has no legal or constructive obligation to pay those future benefits: its only obligation is to pay the contributions as they fall due and if the enterprise ceases to employ members of the state plan, it will have no obligation to pay the benefits earned by its own employees in previous years. For this reason, state plans are normally defined contribution plans. However, in the rare cases when a state plan is a defined benefit plan, an enterprise applies the treatment prescribed in paragraphs 29 and 30.

Insured Benefits

39. *An enterprise may pay insurance premiums to fund a post-employment benefit plan. The enterprise should treat such a plan as a defined contribution plan unless the enterprise will have (either directly, or indirectly through the plan) a legal or constructive obligation to either:*
- (a) pay the employee benefits directly when they fall due; or*
 - (b) pay further amounts if the insurer does not pay all future employee benefits relating to employee service in the current and prior periods.*
- If the enterprise retains such a legal or constructive obligation, the enterprise should treat the plan as a defined benefit plan.*
40. The benefits insured by an insurance contract need not have a direct or automatic relationship with the enterprise's obligation for employee benefits. Post-employment benefit plans involving insurance contracts are subject to the same distinction between accounting and funding as other funded plans.
41. Where an enterprise funds a post-employment benefit obligation by contributing to an insurance policy under which the enterprise (either directly, indirectly through the plan, through the mechanism for setting future premiums or through a related party relationship with the insurer) retains a legal or constructive obligation, the payment of the premiums does not amount to a defined contribution arrangement. It follows that the enterprise:
- (a) accounts for a qualifying insurance policy as a plan asset (see paragraph 7); and
 - (b) recognises other insurance policies as reimbursement rights (if the policies satisfy the criteria in paragraph ~~405104A~~).

42. Where an insurance policy is in the name of a specified plan participant or a group of plan participants and the enterprise does not have any legal or constructive obligation to cover any loss on the policy, the enterprise has no obligation to pay benefits to the employees and the insurer has sole responsibility for paying the benefits. The payment of fixed premiums under such contracts is, in substance, the settlement of the employee benefit obligation, rather than an investment to meet the obligation. Consequently, the enterprise no longer has an asset or a liability. Therefore, an enterprise treats such payments as contributions to a defined contribution plan.

Post-employment Benefits: Defined Contribution Plans

43. Accounting for defined contribution plans is straightforward because the reporting enterprise's obligation for each period is determined by the amounts to be contributed for that period. Consequently, no actuarial assumptions are required to measure the obligation or the expense and there is no possibility of any actuarial gain or loss. Moreover, the obligations are measured on an undiscounted basis, except where they do not fall due wholly within twelve months after the end of the period in which the employees render the related service.

Recognition and Measurement

44. *When an employee has rendered service to an enterprise during a period, the enterprise should recognise the contribution payable to a defined contribution plan in exchange for that service:*
- (a) *as a liability (accrued expense), after deducting any contribution already paid. If the contribution already paid exceeds the contribution due for service before the balance sheet date, an enterprise should recognise that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund; and*
 - (b) *as an expense, unless another Statement of Standard Accounting Practice requires or permits the inclusion of the contribution in the cost of an asset (see, for example, SSAP 22, Inventories, and SSAP 17, Property, Plant and Equipment).*
45. *Where contributions to a defined contribution plan do not fall due wholly within twelve months after the end of the period in which the employees render the related service, they should be discounted using the discount rate specified in paragraph 78.*

Disclosure

46. *An enterprise should disclose the amount recognised as an expense for defined contribution plans.*
47. Where required by SSAP 20, Related Party Disclosures, an enterprise discloses information about contributions to defined contribution plans for key management personnel.

Post-employment Benefits: Defined Benefit Plans

48. Accounting for defined benefit plans is complex because actuarial assumptions are required to measure the obligation and the expense and there is a possibility of actuarial gains and losses. Moreover, the obligations are measured on a discounted basis because they may be settled many years after the employees render the related service.

Recognition and Measurement

49. Defined benefit plans may be unfunded, or they may be wholly or partly funded by contributions by an enterprise, and sometimes its employees, into an entity, or fund, that is legally separate from the reporting enterprise and from which the employee benefits are paid. The payment of funded benefits when they fall due depends not only on the financial position and the investment performance of the fund but also on an enterprise's ability (and willingness) to make good any shortfall in the fund's assets. Therefore, the enterprise is, in substance, underwriting the actuarial and investment risks associated with the plan. Consequently, the expense recognised for a defined benefit plan is not necessarily the amount of the contribution due for the period.
50. Accounting by an enterprise for defined benefit plans involves the following steps:
- (a) using actuarial techniques to make a reliable estimate of the amount of benefit that employees have earned in return for their service in the current and prior periods. This requires an enterprise to determine how much benefit is attributable to the current and prior periods (see paragraphs 67 - 71) 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 will influence the cost of the benefit (see paragraphs 72 - 91);
 - (b) discounting that benefit using the Projected Unit Credit Method in order to determine the present value of the defined benefit obligation and the current service cost (see paragraphs 64 - 66);
 - (c) determining the fair value of any plan assets (see paragraphs 102 -104);
 - (d) determining the total amount of actuarial gains and losses and the amount of those actuarial gains and losses that should be recognised (see paragraphs 92 - 95);
 - (e) where a plan has been introduced or changed, determining the resulting past service cost (see paragraphs 96 - 101); and
 - (f) where a plan has been curtailed or settled, determining the resulting gain or loss (see paragraphs ~~113—119~~ 109 - 115).

Where an enterprise has more than one defined benefit plan, the enterprise applies these procedures for each material plan separately.

51. In some cases, estimates, averages and computational shortcuts may provide a reliable approximation of the detailed computations illustrated in this Statement.

Accounting for the Constructive Obligation

52. *An enterprise should account not only for its legal obligation under the formal terms of a defined benefit plan, but also for any constructive obligation that arises from the enterprise's informal practices. Informal practices give rise to a constructive obligation where the enterprise has no realistic alternative but to pay employee benefits. An example of a constructive obligation is where a change in the enterprise's informal practices would cause unacceptable damage to its relationship with employees.*
53. The formal terms of a defined benefit plan may permit an enterprise to terminate its obligation under the plan. Nevertheless, it is usually difficult for an enterprise to cancel a plan if employees are to be retained. Therefore, in the absence of evidence to the contrary, accounting for post-employment benefits assumes that an enterprise which is currently promising such benefits will continue to do so over the remaining working lives of employees.

Balance Sheet

54. *The amount recognised as a defined benefit liability should be the net total of the following amounts:*
- (a) *the present value of the defined benefit obligation at the balance sheet date (see paragraph 64);*
 - (b) *plus any actuarial gains (less any actuarial losses) not recognised because of the treatment set out in paragraphs 92 - 93;*
 - (c) *minus any past service cost not yet recognised (see paragraph 96);*
 - (d) *minus the fair value at the balance sheet date of plan assets (if any) out of which the obligations are to be settled directly (see paragraphs 102 - 104).*
55. The present value of the defined benefit obligation is the gross obligation, before deducting the fair value of any plan assets.
56. *An enterprise should determine the present value of defined benefit obligations and the fair value of any plan assets with sufficient regularity that the amounts recognised in the financial statements do not differ materially from the amounts that would be determined at the balance sheet date.*
57. This Statement encourages, but does not require, an enterprise to involve a qualified actuary in the measurement of all material post-employment benefit obligations. For practical reasons, an enterprise may request a qualified actuary to carry out a detailed valuation of the obligation before the balance sheet date. Nevertheless, the results of that valuation are updated for any material transactions and other material changes in circumstances (including changes in market prices and interest rates) up to the balance sheet date.
58. *The amount determined under paragraph 54 may be negative (an asset). An enterprise should measure the resulting asset at the lower of:*
- (a) *the amount determined under paragraph 54; and*
 - (b) *the net total of:*
 - (i) *any cumulative unrecognised net actuarial losses and past service cost (see paragraphs 92, 93 and 96); and*
 - (ii) *the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan. The present value of these economic benefits should be determined using the discount rate specified in paragraph 78.*
- 58A.** *The application of paragraph 58 should not result in a gain being recognised solely as a result of an actuarial loss or past service cost in the current period or in a loss being recognised solely as a result of an actuarial gain in the current period. The enterprise should therefore recognise immediately under paragraph 54 the following, to the extent that they arise while the defined benefit asset is determined in accordance with paragraph 58(b):*
- (a) *net actuarial losses of the current period and past service cost of the current period to the extent that they exceed any reduction in the present value of the economic benefits specified in paragraph 58(b)(ii). If there is no change or an increase in the present value of the economic benefits, the entire net actuarial losses of the current period and past service cost of the current period should be recognised immediately under paragraph 54.*

(b) net actuarial gains of the current period after the deduction of past service cost of the current period to the extent that they exceed any increase in the present value of the economic benefits specified in paragraph 58(b)(ii). If there is no change or a decrease in the present value of the economic benefits, the entire net actuarial gains of the current period after the deduction of past service cost of the current period should be recognised immediately under paragraph 54.

58B. Paragraph 58A applies to an enterprise only if it has, at the beginning or end of the accounting period, a surplus* in a defined benefit plan and cannot, based on the current terms of the plan, recover that surplus fully through refunds or reductions in future contributions. In such cases, past service cost and actuarial losses that arise in the period, the recognition of which is deferred under paragraph 54, will increase the amount specified in paragraph 58(b)(i). If that increase is not offset by an equal decrease in the present value of economic benefits that qualify for recognition under paragraph 58(b)(ii), there will be an increase in the net total specified by paragraph 58(b) and, hence, a recognised gain. Paragraph 58A prohibits the recognition of a gain in these circumstances. The opposite effect arises with actuarial gains that arise in the period, the recognition of which is deferred under paragraph 54, to the extent that the actuarial gains reduce cumulative unrecognised actuarial losses. Paragraph 58A prohibits the recognition of a loss in these circumstances. For examples of the application of this paragraph, see Appendix C.

59. An asset may arise where a defined benefit plan has been overfunded or in certain cases where actuarial gains are recognised. An enterprise recognises an asset in such cases because:

- (a) the enterprise controls a resource, which is the ability to use the surplus to generate future benefits;
- (b) that control is a result of past events (contributions paid by the enterprise and service rendered by the employee); and
- (c) future economic benefits are available to the enterprise in the form of a reduction in future contributions or a cash refund, either directly to the enterprise or indirectly to another plan in deficit.

60. The limit in paragraph 58(b) does not over-ride the delayed recognition of certain actuarial losses (see paragraphs 92 and 93) and certain past service cost (see paragraph 96), other than as specified in paragraph 58A. However, that limit does over-ride the transitional option in paragraph ~~158~~155(b). Paragraph ~~123~~120(c)(vi) requires an enterprise to disclose any amount not recognised as an asset because of the limit in paragraph 58(b).

* A surplus is an excess of the fair value of the plan assets over the present value of the defined benefit obligation.

Example Illustrating Paragraph 60

A defined benefit plan has the following characteristics:

Present value of the obligation	1,100
Fair value of plan assets	(1,190)
	<hr/>
	(90)
Unrecognised actuarial losses	(110)
Unrecognised past service cost	(70)
Unrecognised increase in the liability on initial adoption of the Statement under paragraph 458 <u>155</u> (b)	(50)
	<hr/>
Negative amount determined under paragraph 54	(320)
	<hr/> <hr/>
Present value of available future refunds and reductions in future contributions	100
	<hr/> <hr/> <hr/>

The limit under paragraph 58(b) is computed as follows:

<i>Unrecognised actuarial losses</i>	<i>110</i>
<i>Unrecognised past service cost</i>	<i>70</i>
<i>Present value of available future refunds and reductions in future contributions</i>	<i>100</i>
	<hr/>
<i>Limit</i>	<i>280</i>
	<hr/> <hr/> <hr/>

280 is less than 320. Therefore, the enterprise recognises an asset of 280 and discloses that the limit reduced the carrying amount of the asset by 40 (see paragraph ~~123~~ 120(c)(vi)).

Income Statement

61. *An enterprise should recognise the net total of the following amounts as expense or (subject to the limit in paragraph 58(b)) income, except to the extent that another Statement of Standard Accounting Practice requires or permits their inclusion in the cost of an asset:*
- (a) current service cost (see paragraphs 63 - 91);*
 - (b) interest cost (see paragraph 82);*
 - (c) the expected return on any plan assets (see paragraphs ~~109-111~~ 105 - 107) and on any reimbursement rights (paragraph ~~105~~ 104A);*
 - (d) actuarial gains and losses, to the extent that they are recognised under paragraphs 92 and 93;*

- (e) *past service cost, to the extent that paragraph 96 requires an enterprise to recognise it; and*
 - (f) *the effect of any curtailments or settlements (see paragraphs ~~113~~109 and ~~114~~110).*
62. Other Statements of Standard Accounting Practice require the inclusion of certain employee benefit costs within the cost of assets such as inventories or property, plant and equipment (see SSAP 22, Inventories, and SSAP 17, Property, Plant and Equipment). Any post-employment benefit costs included in the cost of such assets include the appropriate proportion of the components listed in paragraph 61.

Recognition and Measurement: Present Value of Defined Benefit Obligations and Current Service Cost

63. The ultimate cost of a defined benefit plan may be influenced by many variables, such as final salaries, employee turnover and mortality, medical cost trends and, for a funded plan, the investment earnings on the plan assets. The ultimate cost of the plan is uncertain and this uncertainty is likely to persist over a long period of time. In order to measure the present value of the post-employment benefit obligations and the related current service cost, it is necessary to:
- (a) apply an actuarial valuation method (see paragraphs 64 - 66);
 - (b) attribute benefit to periods of service (see paragraphs 67 - 71); and
 - (c) make actuarial assumptions (see paragraphs 72 - 91).

Actuarial Valuation Method

64. *An enterprise should use the Projected Unit Credit Method to determine the present value of its defined benefit obligations and the related current service cost and, where applicable, past service cost.*
65. The Projected Unit Credit Method (sometimes known as the accrued benefit method pro-rated on service or as the benefit/years of service method) sees each period of service as giving rise to an additional unit of benefit entitlement (see paragraphs 67 - 71) and measures each unit separately to build up the final obligation (see paragraphs 72 - 91).
66. 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.

Example Illustrating Paragraph 65

A lump sum benefit is payable on termination of service and equal to 1% of final salary for each year of service. The salary in year 1 is 10,000 and is assumed to increase at 7% (compound) each year. The discount rate used is 10% per annum. The following table shows how the obligation builds up for an employee who is expected to leave at the end of year 5, assuming that there are no changes in actuarial assumptions. For simplicity, this example ignores the additional adjustment needed to reflect the probability that the employee may leave the enterprise at an earlier or later date.

<i>Year</i>	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
<i>Benefit attributed to:</i>					
<i>- prior years</i>	<i>0</i>	<i>131</i>	<i>262</i>	<i>393</i>	<i>524</i>
<i>- current year</i>					
<i>(1% of final salary)</i>	<i>131</i>	<i>131</i>	<i>131</i>	<i>131</i>	<i>131</i>
	—	—	—	—	—
<i>- current and prior years</i>	<i>131</i>	<i>262</i>	<i>393</i>	<i>524</i>	<i>655</i>
	===	===	===	===	===
<i>Opening Obligation</i>	<i>-</i>	<i>89</i>	<i>196</i>	<i>324</i>	<i>476</i>
<i>Interest at 10%</i>	<i>-</i>	<i>9</i>	<i>20</i>	<i>33</i>	<i>48</i>
<i>Current Service Cost</i>	<i>89</i>	<i>98</i>	<i>108</i>	<i>119</i>	<i>131</i>
	—	—	—	—	—
<i>Closing Obligation</i>	<i>89</i>	<i>196</i>	<i>324</i>	<i>476</i>	<i>655</i>
	===	===	===	===	===

Note:

- 1. The Opening Obligation is the present value of benefit attributed to prior years.*
- 2. The Current Service Cost is the present value of benefit attributed to the current year.*
- 3. The Closing Obligation is the present value of benefit attributed to current and prior years.*

Attributing Benefit to Periods of Service

- 67. In determining the present value of its defined benefit obligations and the related current service cost and, where applicable, past service cost, an enterprise should 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 enterprise should 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.**

68. The Projected Unit Credit Method requires an enterprise to attribute benefit to the current period (in order to determine current service cost) and the current and prior periods (in order to determine the present value of defined benefit obligations). An enterprise attributes benefit to periods in which the obligation to provide post-employment benefits arises. That obligation arises as employees render services in return for post-employment benefits which an enterprise expects to pay in future reporting periods. Actuarial techniques allow an enterprise to measure that obligation with sufficient reliability to justify recognition of a liability.

Examples Illustrating Paragraph 68

1. A defined benefit plan provides a lump-sum benefit of 100 payable on retirement for each year of service.

A benefit of 100 is attributed to each year. The current service cost is the present value of 100. The present value of the defined benefit obligation is the present value of 100, multiplied by the number of years of service up to the balance sheet date.

If the benefit is payable immediately when the employee leaves the enterprise, the current service cost and the present value of the defined benefit obligation reflect the date at which the employee is expected to leave. Thus, because of the effect of discounting, they are less than the amounts that would be determined if the employee left at the balance sheet date.

2. 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.

Benefit equal to the present value, at the expected retirement date, of a monthly pension of 0.2% of the estimated final salary payable from the expected retirement date until the expected date of death is attributed to each year of service. The current service cost is the present value of that benefit. The present value of the defined benefit obligation is the present value of monthly pension payments of 0.2% of final salary, multiplied by the number of years of service up to the balance sheet date. The current service cost and the present value of the defined benefit obligation are discounted because pension payments begin at the age of 65

69. 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 vested). Employee service before the vesting date gives rise to a constructive obligation because, at each successive balance sheet 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 enterprise considers the probability that some employees may not satisfy any vesting requirements. Similarly, 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. The probability that the specified event will occur affects the measurement of the obligation, but does not determine whether the obligation exists.

Examples Illustrating Paragraph 69

1. A plan pays a benefit of 100 for each year of service. The benefits vest after ten years of service.

A benefit of 100 is attributed to each year. In each of the first ten years, the current service cost and the present value of the obligation reflect the probability that the employee may not complete ten years of service.

2. A plan pays a benefit of 100 for each year of service, excluding service before the age of 25. The benefits vest immediately.

No benefit is attributed to service before the age of 25 because service before that date does not lead to benefits (conditional or unconditional). A benefit of 100 is attributed to each subsequent year.

70. The obligation increases until the date when further service by the employee will lead to no material amount of further benefits. Therefore, all benefit is attributed to periods ending on or before that date. Benefit is attributed to individual accounting periods 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 enterprise attributes benefit on a straight-line basis until the date when further service by the employee will lead to no material amount of further benefits. That is because the employee's service throughout the entire period will ultimately lead to benefit at that higher level.

Examples Illustrating Paragraph 70

1. A plan pays a lump-sum benefit of 1,000 that vests after ten years of service. The plan provides no further benefit for subsequent service.

A benefit of 100 (1,000 divided by ten) is attributed to each of the first ten years. The current service cost in each of the first ten years reflects the probability that the employee may not complete ten years of service. No benefit is attributed to subsequent years.

2. A plan pays a lump-sum retirement benefit of 2,000 to all employees who are still employed at the age of 55 after twenty years of service, or who are still employed at the age of 65, regardless of their length of service.

For employees who join before the age of 35, service first leads to benefits under the plan at the age of 35 (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. Also, service beyond the age of 55 will lead to no material amount of further benefits. For these employees, the enterprise attributes benefit of 100 (2,000 divided by 20) to each year from the age of 35 to the age of 55.

For employees who join between the ages of 35 and 45, service beyond twenty years will lead to no material amount of further benefits. For these employees, the enterprise attributes benefit of 100 (2,000 divided by 20) to each of the first twenty years.

For an employee who joins at the age of 55, service beyond ten years will lead to no material amount of further benefits. For this employee, the enterprise attributes benefit of 200 (2,000 divided by 10) to each of the first ten years.

For all employees, the current service cost and the present value of the obligation reflect the probability that the employee may not complete the necessary period of service.

3. A post-employment medical plan reimburses 40% of an employee's post-employment medical costs if the employee leaves after more than ten and less than twenty years of service and 50% of those costs if the employee leaves after twenty or more years of service.

Under the plan's benefit formula, the enterprise attributes 4% of the present value of the expected medical costs (40% divided by ten) to each of the first ten years and 1% (10% divided by ten) to each of the second ten years. The current service cost in each year reflects the probability that the employee may not complete the necessary period of service to earn part or all of the benefits. For employees expected to leave within ten years, no benefit is attributed.

4. A post-employment medical plan reimburses 10% of an employee's post-employment medical costs if the employee leaves after more than ten and less than twenty years of service and 50% of those costs if the employee leaves after twenty or more years of service.

Service in later years will lead to a materially higher level of benefit than in earlier years. Therefore, for employees expected to leave after twenty or more years, the enterprise attributes benefit on a straight-line basis under paragraph 68. Service beyond twenty years will lead to no material amount of further benefits. Therefore, the benefit attributed to each of the first twenty years is 2.5% of the present value of the expected medical costs (50% divided by twenty).

For employees expected to leave between ten and twenty years, the benefit attributed to each of the first ten years is 1% of the present value of the expected medical costs. For these employees, no benefit is attributed to service between the end of the tenth year and the estimated date of leaving.

For employees expected to leave within ten years, no benefit is attributed.

71. Where the amount of a benefit is a constant proportion of final salary for each year of service, future salary increases will affect the amount required to settle the obligation that exists for service before the balance sheet date, but do not create an additional obligation. Therefore:
- (a) for the purpose of paragraph 67(b), salary increases do not lead to further benefits, even though the amount of the benefits is dependent on final salary; and
 - (b) the amount of benefit attributed to each period is a constant proportion of the salary to which the benefit is linked.

Example Illustrating Paragraph 71

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

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 material amount of further benefits under the plan. No benefit is attributed to service after that age.

Actuarial Assumptions

72. *Actuarial assumptions should be unbiased and mutually compatible.*
73. Actuarial assumptions are an enterprise's best estimates of the variables that will determine the ultimate cost of providing post-employment benefits. 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 (see paragraphs 78 - 82);
 - (ii) future salary and benefit levels (see paragraphs 83 - 87);
 - (iii) in the case of medical benefits, future medical costs, including, where material, the cost of administering claims and benefit payments (see paragraphs 88 - 91); and
 - (iv) the expected rate of return on plan assets (see paragraphs ~~105-107~~¹⁰⁹⁻¹¹¹).
74. Actuarial assumptions are unbiased if they are neither imprudent nor excessively conservative.
75. Actuarial assumptions are mutually compatible if they reflect the economic relationships between factors such as inflation, rates of salary increase, the return on plan assets and discount rates. For example, all assumptions which depend on a particular inflation level (such as assumptions about interest rates and salary and benefit increases) in any given future period assume the same inflation level in that period.
76. An enterprise determines the discount rate and other financial assumptions in nominal (stated) terms, unless estimates in real (inflation-adjusted) terms are more reliable, for example, in a hyper-inflationary economy, or where the benefit is index-linked and there is a deep market in index-linked bonds of the same currency and term.

77. *Financial assumptions should be based on market expectations, at the balance sheet date, for the period over which the obligations are to be settled.*

Actuarial Assumptions: Discount Rate

78. *The rate used to discount post-employment benefit obligations (both funded and unfunded) should be determined by reference to market yields at the balance sheet date on high quality corporate bonds. In countries where there is no deep market in such bonds, the market yields (at the balance sheet date) on government bonds should be used. The currency and term of the corporate bonds or government bonds should be consistent with the currency and estimated term of the post-employment benefit obligations.*
79. One actuarial assumption which has a material effect is the discount rate. The discount rate reflects the time value of money but not the actuarial or investment risk. Furthermore, the discount rate does not reflect the enterprise-specific credit risk borne by the enterprise's creditors, nor does it reflect the risk that future experience may differ from actuarial assumptions.
80. The discount rate reflects the estimated timing of benefit payments. In practice, an enterprise often achieves this by applying a single weighted average discount rate that reflects the estimated timing and amount of benefit payments and the currency in which the benefits are to be paid.
81. In some cases, there may be no deep market in bonds with a sufficiently long maturity to match the estimated maturity of all the benefit payments. In such cases, an enterprise uses current market rates of the appropriate term to discount shorter term payments, and estimates the discount rate for longer maturities by extrapolating current market rates along the yield curve. The total present value of a defined benefit obligation is unlikely to be particularly sensitive to the discount rate applied to the portion of benefits that is payable beyond the final maturity of the available corporate or government bonds.
82. Interest cost is computed by multiplying the discount rate as determined at the start of the period by the present value of the defined benefit obligation throughout that period, taking account of any material changes in the obligation. The present value of the obligation will differ from the liability recognised in the balance sheet because the liability is recognised after deducting the fair value of any plan assets and because some actuarial gains and losses, and some past service cost, are not recognised immediately. [Appendix 1 illustrates the computation of interest cost, among other things.]

Actuarial Assumptions: Salaries, Benefits and Medical Costs

83. *Post-employment benefit obligations should be measured on a basis that reflects:*
- (a) estimated future salary increases;*
 - (b) the benefits set out in the terms of the plan (or resulting from any constructive obligation that goes beyond those terms) at the balance sheet date; and*
 - (c) estimated future changes in the level of any state benefits that affect the benefits payable under a defined benefit plan, if, and only if, either:*
 - (i) those changes were enacted before the balance sheet date; or*
 - (ii) 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.*
84. Estimates of future salary increases take account of inflation, seniority, promotion and other relevant factors, such as supply and demand in the employment market.

85. If the formal terms of a plan (or a constructive obligation that goes beyond those terms) require an enterprise to change benefits in future periods, the measurement of the obligation reflects those changes. This is the case when, for example:
- (a) the enterprise has a past history of increasing benefits, for example to mitigate the effects of inflation, and there is no indication that this practice will change in the future; or
 - (b) actuarial gains have already been recognised in the financial statements and the enterprise is obliged, by either the formal terms of a plan (or a constructive obligation that goes beyond those terms) or legislation, to use any surplus in the plan for the benefit of plan participants (see paragraph 98(c)).
86. Actuarial assumptions do not reflect future benefit changes that are not set out in the formal terms of the plan (or a constructive obligation) at the balance sheet date. Such changes will result in:
- (a) past service cost, to the extent that they change benefits for service before the change; and
 - (b) current service cost for periods after the change, to the extent that they change benefits for service after the change.
87. Some post-employment benefits are linked to variables such as the level of state retirement benefits or state medical care. The measurement of such benefits reflects expected changes in such variables, based on past history and other reliable evidence.
- 88. *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.***
89. Measurement of post-employment medical benefits requires assumptions about the level and frequency of future claims and the cost of meeting those claims. An enterprise estimates future medical costs on the basis of historical data about the enterprise's own experience, supplemented where necessary by historical data from other enterprises, insurance companies, medical providers or other sources. Estimates of future medical costs consider the effect of technological advances, changes in health care utilisation or delivery patterns and changes in the health status of plan participants.
90. The level and frequency of claims is particularly sensitive to the age, health status and sex of employees (and their dependants) and may be sensitive to other factors such as geographical location. Therefore, historical data is adjusted to the extent that the demographic mix of the population differs from that of the population used as a basis for the historical data. It is also adjusted where there is reliable evidence that historical trends will not continue.
91. Some post-employment health care plans require employees to contribute to the medical costs covered by the plan. Estimates of future medical costs take account of any such contributions, based on the terms of the plan at the balance sheet date (or based on any constructive obligation that goes beyond those terms). Changes in those employee contributions result in past service cost or, where applicable, curtailments. The cost of meeting claims may be reduced by benefits from state or other medical providers (see paragraphs 83(c) and 87).

Actuarial Gains and Losses

92. *In measuring its defined benefit liability under paragraph 54, an enterprise should, subject to paragraph 58A, recognise a portion (as specified in paragraph 93) of its actuarial gains and losses as income or expense if the net cumulative unrecognised actuarial gains and losses at the end of the previous reporting period exceeded the greater of:*

(a) *10% of the present value of the defined benefit obligation at that date (before deducting plan assets); and*

(b) *10% of the fair value of any plan assets at that date.*

These limits should be calculated and applied separately for each defined benefit plan.

93. *The portion of actuarial gains and losses to be recognised for each defined benefit plan is the excess determined under paragraph 92, divided by the expected average remaining working lives of the employees participating in that plan. However, an enterprise may adopt any systematic method that results in faster recognition of actuarial gains and losses, provided that the same basis is applied to both gains and losses and the basis is applied consistently from period to period. An enterprise may apply such systematic methods to actuarial gains and losses even if they fall within the limits specified in paragraph 92.*

94. Actuarial gains and losses may result from increases or decreases in either the present value of a defined benefit obligation or the fair value of any related plan assets. Causes of actuarial gains and losses include, for example:

(a) unexpectedly high or low rates of employee turnover, early retirement or mortality or of increases in salaries, benefits (if the formal or constructive terms of a plan provide for inflationary benefit increases) or medical costs;

(b) the effect of changes in estimates of future employee turnover, early retirement or mortality or of increases in salaries, benefits (if the formal or constructive terms of a plan provide for inflationary benefit increases) or medical costs;

(c) the effect of changes in the discount rate; and

(d) differences between the actual return on plan assets and the expected return on plan assets (see paragraphs ~~109~~~~111~~105-107).

95. In the long term, actuarial gains and losses may offset one another. Therefore, estimates of post-employment benefit obligations are best viewed as a range (or 'corridor') around the best estimate. An enterprise is permitted, but not required, to recognise actuarial gains and losses that fall within that range. This Statement requires an enterprise to recognise, as a minimum, a specified portion of the actuarial gains and losses that fall outside a 'corridor' of plus or minus 10%. [Appendix 1 illustrates the treatment of actuarial gains and losses, among other things] The Statement also permits systematic methods of faster recognition, provided that those methods satisfy the conditions set out in paragraph 93. Such permitted methods include, for example, immediate recognition of all actuarial gains and losses, both within and outside the 'corridor'. Paragraph ~~158~~155(b)(iii) explains the need to consider any unrecognised part of the transitional liability in accounting for subsequent actuarial gains.

Past Service Cost

96. *In measuring its defined benefit liability under paragraph 54, an enterprise should, subject to paragraph 58A, recognise past service cost as an expense on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits are already vested immediately following the introduction of, or changes to, a defined benefit plan, an enterprise should recognise past service cost immediately.*

97. Past service cost arises when an enterprise introduces a defined benefit plan or changes the benefits payable under an existing defined benefit plan. Such changes are in return for employee service over the period until the benefits concerned are vested. Therefore, past service cost is recognised over that period, regardless of the fact that the cost refers to employee service in previous periods. Past service cost is measured as the change in the liability resulting from the amendment (see paragraph 64).

Example Illustrating Paragraph 97

An enterprise operates a pension plan that provides a pension of 2% of final salary for each year of service. The benefits become vested after five years of service. On 1 January 20X5 the enterprise improves the pension to 2.5% of final salary for each year of service starting from 1 January 20X1. At the date of the improvement, the present value of the additional benefits for service from 1 January 20X1 to 1 January 20X5 is as follows:

Employees with more than five years' service at 1/1/X5	150
Employees with less than five years' service at 1/1/X5 (average period until vesting: three years)	120
	—
	270
	===

The enterprise recognises 150 immediately because those benefits are already vested. The enterprise recognises 120 on a straight-line basis over three years from 1 January 20X5.

98. Past service cost excludes:
- (a) the effect of differences between actual and previously assumed salary increases on the obligation to pay benefits for service in prior years (there is no past service cost because actuarial assumptions allow for projected salaries);
 - (b) under and over estimates of discretionary pension increases where an enterprise has a constructive obligation to grant such increases (there is no past service cost because actuarial assumptions allow for such increases);
 - (c) estimates of benefit improvements that result from actuarial gains that have already been recognised in the financial statements if the enterprise is obliged, by either the formal terms of a plan (or a constructive obligation that goes beyond those terms) or legislation, to use any surplus in the plan for the benefit of plan participants, even if the benefit increase has not yet been formally awarded (the resulting increase in the obligation is an actuarial loss and not past service cost, see paragraph 85(b));
 - (d) the increase in vested benefits when, in the absence of new or improved benefits, employees complete vesting requirements (there is no past service cost because the estimated cost of benefits was recognised as current service cost as the service was rendered); and
 - (e) the effect of plan amendments that reduce benefits for future service (a curtailment).

99. An enterprise establishes the amortisation schedule for past service cost when the benefits are introduced or changed. It would be impracticable to maintain the detailed records needed to identify and implement subsequent changes in that amortisation schedule. Moreover, the effect is likely to be material only where there is a curtailment or settlement. Therefore, an enterprise amends the amortisation schedule for past service cost only if there is a curtailment or settlement.
100. Where an enterprise reduces benefits payable under an existing defined benefit plan, the resulting reduction in the defined benefit liability is recognised as (negative) past service cost over the average period until the reduced portion of the benefits becomes vested.
101. Where an enterprise reduces certain benefits payable under an existing defined benefit plan and, at the same time, increases other benefits payable under the plan for the same employees, the enterprise treats the change as a single net change.

Recognition and Measurement: Plan Assets

Fair Value of Plan Assets

102. The fair value of any plan assets is deducted in determining the amount recognised in the balance sheet under paragraph 54. When no market price is available, the fair value of plan assets is estimated; for example, by discounting expected future cash flows using a discount rate that reflects both the risk associated with the plan assets and the maturity or expected disposal date of those assets (or, if they have no maturity, the expected period until the settlement of the related obligation).
103. Plan assets exclude unpaid contributions due from the reporting enterprise to the fund, as well as any non-transferable financial instruments issued by the enterprise and held by the fund. Plan assets are reduced by any liabilities of the fund that do not relate to employee benefits, for example, trade and other payables and liabilities resulting from derivative financial instruments.
104. Where plan assets include qualifying insurance policies that exactly match the amount and timing of some or all of the benefits payable under the plan, the fair value of those insurance policies is deemed to be the present value of the related obligations, as described in paragraph 54 (subject to any reduction required if the amounts receivable under the insurance policies are not recoverable in full).

Reimbursements

- ~~104A~~¹⁰⁵. *When, and only when, it is virtually certain that another party will reimburse some or all of the expenditure required to settle a defined benefit obligation, an enterprise should recognise its right to reimbursement as a separate asset. The enterprise should measure the asset at fair value. In all other respects, an enterprise should treat that asset in the same way as plan assets. In the income statement, the expense relating to a defined benefit plan may be presented net of the amount recognised for a reimbursement.*
- ~~104B~~¹⁰⁶. Sometimes, an enterprise is able to look to another party, such as an insurer, to pay part or all of the expenditure required to settle a defined benefit obligation. Qualifying insurance policies, as defined in paragraph 7, are plan assets. An enterprise accounts for qualifying insurance policies in the same way as for all other plan assets and paragraph ~~105~~^{104A} does not apply (see paragraphs 39 - 42 and 104).

104C107. When an insurance policy is not a qualifying insurance policy, that insurance policy is not a plan asset. Paragraph ~~105~~104A deals with such cases: the enterprise recognises its right to reimbursement under the insurance policy as a separate asset, rather than as a deduction in determining the defined benefit liability recognised under paragraph 54; in all other respects, the enterprise treats that asset in the same way as plan assets. In particular, the defined benefit liability recognised under paragraph 54 is increased (reduced) to the extent that net cumulative actuarial gains (losses) on the defined benefit obligation and on the related reimbursement right remain unrecognised under paragraphs 92 and 93. Paragraph ~~123~~120(c)(vii) requires the enterprise to disclose a brief description of the link between the reimbursement right and the related obligation.

Example Illustrating Paragraphs ~~105~~104A-C

Present value of obligation	1,241
Unrecognised actuarial gains	17

Liability recognised in balance sheet	1,258
	=====
Rights under insurance policies that exactly match the amount and timing of some of the benefits payable under the plan. Those benefits have a present value of 1,092	1,092
	=====

The unrecognised actuarial gains of 17 are the net cumulative actuarial gains on the obligation and on the reimbursement rights.

104D108. If the right to reimbursement arises under an insurance policy that exactly matches the amount and timing of some or all of the benefits payable under a defined benefit plan, the fair value of the reimbursement right is deemed to be the present value of the related obligation, as described in paragraph 54 (subject to any reduction required if the reimbursement is not recoverable in full).

Return on Plan Assets

105~~109~~. The expected return on plan assets is one component of the expense recognised in the income statement. The difference between the expected return on plan assets and the actual return on plan assets is an actuarial gain or loss; it is included with the actuarial gains and losses on the defined benefit obligation in determining the net amount that is compared with the limits of the 10% 'corridor' specified in paragraph 92.

106~~110~~. The expected return on plan assets is based on market expectations, at the beginning of the period, for returns over the entire life of the related obligation. The expected return on plan assets reflects changes in the fair value of plan assets held during the period as a result of actual contributions paid into the fund and actual benefits paid out of the fund.

- ~~10744~~. In determining the expected and actual return on plan assets, an enterprise deducts expected administration costs, other than those included in the actuarial assumptions used to measure the obligation.

Example Illustrating Paragraph ~~10644~~

At 1 January 20X1, the fair value of plan assets was 10,000 and net cumulative unrecognised actuarial gains were 760. On 30 June 20X1, the plan paid benefits of 1,900 and received contributions of 4,900. At 31 December 20X1, the fair value of plan assets was 15,000 and the present value of the defined benefit obligation was 14,792. Actuarial losses on the obligation for 20X1 were 60.

At 1 January 20X1, the reporting enterprise made the following estimates, based on market prices at that date:

	%
Interest and dividend income, after tax payable by the fund	9.25
Realised and unrealised gains on plan assets (after tax)	2.00
Administration costs	(1.00)
	<hr/>
Expected rate of return	10.25
	<hr/> <hr/>

For 20X1, the expected and actual return on plan assets are as follows:

<i>Return on 10,000 held for 12 months at 10.25%</i>	<i>1,025</i>
<i>Return on 3,000 held for six months at 5% (equivalent to 10.25% annually, compounded every six months)</i>	<i>150</i>
	<hr/>
<i>Expected return on plan assets for 20X1</i>	<i>1,175</i>
	<hr/> <hr/>
<i>Fair value of plan assets at 31 December 20X1</i>	<i>15,000</i>
<i>Less fair value of plan assets at 1 January 20X1</i>	<i>(10,000)</i>
<i>Less contributions received</i>	<i>(4,900)</i>
<i>Add benefits paid</i>	<i>1,900</i>
	<hr/>
<i>Actual return on plan assets</i>	<i>2,000</i>
	<hr/> <hr/>

The difference between the expected return on plan assets (1,175) and the actual return on plan assets (2,000) is an actuarial gain of 825. Therefore, the cumulative net unrecognised actuarial gains are 1,525 (760 plus 825 less 60). Under paragraph 92, the limits of the corridor are set at 1,500 (greater of: (i) 10% of 15,000 and (ii) 10% of 14,792). In the following year (20X2), the enterprise recognises in the income statement an actuarial gain of 25 (1,525 less 1,500) divided by the expected average remaining working life of the employees concerned.

The expected return on plan assets for 20X2 will be based on market expectations at 1/1/X2 for returns over the entire life of the obligation.

Business Combinations

~~108~~¹¹². In a business combination that is an acquisition, an enterprise recognises assets and liabilities arising from post-employment benefits at the present value of the obligation less the fair value of any plan assets (see SSAP 30, Business Combinations). The present value of the obligation includes all of the following, even if the acquiree had not yet recognised them at the date of the acquisition:

- (a) actuarial gains and losses that arose before the date of the acquisition (whether or not they fell inside the 10% 'corridor');
- (b) past service cost that arose from benefit changes, or the introduction of a plan, before the date of the acquisition; and
- (c) amounts that, under the transitional provisions of paragraph ~~158~~¹⁵⁵(b), the acquiree had not recognised.

Curtailments and Settlements

~~109~~¹¹³. *An enterprise should recognise gains or losses on the curtailment or settlement of a defined benefit plan when the curtailment or settlement occurs. The gain or loss on a curtailment or settlement should comprise:*

- (a) *any resulting change in the present value of the defined benefit obligation;*
- (b) *any resulting change in the fair value of the plan assets;*
- (c) *any related actuarial gains and losses and past service cost that, under paragraphs 92 and 96, had not previously been recognised.*

~~110~~¹¹⁴. *Before determining the effect of a curtailment or settlement, an enterprise should remeasure the obligation (and the related plan assets, if any) using current actuarial assumptions (including current market interest rates and other current market prices).*

~~111~~¹¹⁵. A curtailment occurs when an enterprise either:

- (a) is demonstrably committed to make a material reduction in the number of employees covered by a plan; or
- (b) amends the terms of a defined benefit plan such that a material element of future service by current employees will no longer qualify for benefits, or will qualify only for reduced benefits.

A curtailment may arise from an isolated event, such as the closing of a plant, discontinuance of an operation or termination or suspension of a plan. An event is material enough to qualify as a curtailment if the recognition of a curtailment gain or loss would have a material effect on the financial statements. Curtailments are often linked with a restructuring. Therefore, an enterprise accounts for a curtailment at the same time as for a related restructuring.

~~112~~¹¹⁶. A settlement occurs when an enterprise enters into a transaction that eliminates all further legal or constructive obligation for part or all of the benefits provided under a defined benefit plan, for example, when a lump-sum cash payment is made to, or on behalf of, plan participants in exchange for their rights to receive specified post-employment benefits.

~~113~~¹¹⁷. In some cases, an enterprise acquires an insurance policy to fund some or all of the employee benefits relating to employee service in the current and prior periods. The acquisition of such a policy is not a settlement if the enterprise retains a legal or constructive obligation (see paragraph 39) to pay further amounts if the insurer does not pay the employee benefits specified in the insurance policy. Paragraphs ~~105–108~~^{104A - D} deal with the recognition and measurement of reimbursement rights under insurance policies that are not plan assets.

- ~~114~~118. A settlement occurs together with a curtailment if a plan is terminated such that the obligation is settled and the plan ceases to exist. However, the termination of a plan is not a curtailment or settlement if the plan is replaced by a new plan that offers benefits that are, in substance, identical.
- ~~115~~119. Where a curtailment relates to only some of the employees covered by a plan, or where only part of an obligation is settled, the gain or loss includes a proportionate share of the previously unrecognised past service cost and actuarial gains and losses (and of transitional amounts remaining unrecognised under paragraph ~~458~~155(b)). The proportionate share is determined on the basis of the present value of the obligations before and after the curtailment or settlement, unless another basis is more rational in the circumstances. For example, it may be appropriate to apply any gain arising on a curtailment or settlement of the same plan to first eliminate any unrecognised past service cost relating to the same plan.

Example Illustrating Paragraph ~~419~~115

An enterprise discontinues a business segment and employees of the discontinued segment will earn no further benefits. This 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 enterprise has a defined benefit obligation with a net present value of 1,000, plan assets with a fair value of 820 and net cumulative unrecognised actuarial gains of 50. The enterprise had first adopted the Statement one year before. This increased the net liability by 100, which the enterprise chose to recognise over five years (see paragraph ~~458~~155(b)). The curtailment reduces the net present value of the obligation by 100 to 900.

Of the previously unrecognised actuarial gains and transitional amounts, 10% (100/1,000) relates to the part of the obligation that was eliminated through the curtailment. Therefore, the effect of the curtailment is as follows:

	<u>Before</u> <u>curtailment</u>	<u>Curtailment</u> <u>gain</u>	<u>After</u> <u>curtailment</u>
<i>Net present value of obligation</i>	1,000	(100)	900
<i>Fair value of plan assets</i>	(820)	-	(820)
	-----	-----	-----
	180	(100)	80
<i>Unrecognised actuarial gains</i>	50	(5)	45
<i>Unrecognised transitional amount (100 x 4/5)</i>	(80)	8	(72)
	-----	-----	-----
<i>Net liability recognised in balance sheet</i>	150 =====	(97) =====	53 =====

Presentation

Offset

- 116120.** *An enterprise should offset an asset relating to one plan against a liability relating to another plan when, and only when, the enterprise:*
- (a) has a legally enforceable right to use a surplus in one plan to settle obligations under the other plan; and*
 - (b) intends either to settle the obligations on a net basis, or to realise the surplus in one plan and settle its obligation under the other plan simultaneously.*
117. [Not used]

Current/Non-current Distinction

- 118121.** Some enterprises distinguish current assets and liabilities from non-current assets and liabilities. This Statement does not specify whether an enterprise should distinguish current and non-current portions of assets and liabilities arising from post-employment benefits.

Financial Components of Post-employment Benefit Costs

- 119122.** This Statement does not specify whether an enterprise should present current service cost, interest cost and the expected return on plan assets as components of a single item of income or expense on the face of the income statement.

Disclosure

- 120123.** *An enterprise should disclose the following information about defined benefit plans:*
- (a) the enterprise's accounting policy for recognising actuarial gains and losses;*
 - (b) a general description of the type of plan;*
 - (c) a reconciliation of the assets and liabilities recognised in the balance sheet, showing at least:*
 - (i) the present value at the balance sheet date of defined benefit obligations that are wholly unfunded;*
 - (ii) the present value (before deducting the fair value of plan assets) at the balance sheet date of defined benefit obligations that are wholly or partly funded;*
 - (iii) the fair value of any plan assets at the balance sheet date;*
 - (iv) the net actuarial gains or losses not recognised in the balance sheet (see paragraph 92);*
 - (v) the past service cost not yet recognised in the balance sheet (see paragraph 96);*
 - (vi) any amount not recognised as an asset, because of the limit in paragraph 58(b);*

- (vii) *the fair value at the balance sheet date of any reimbursement right recognised as an asset under paragraph ~~105~~104A (with a brief description of the link between the reimbursement right and the related obligation); and*
- (viii) *the other amounts recognised in the balance sheet;*
- (d) *the amounts included in the fair value of plan assets for:*
 - (i) *each category of the reporting enterprise's own financial instruments; and*
 - (ii) *any property occupied by, or other assets used by, the reporting enterprise;*
- (e) *a reconciliation showing the movements during the period in the net liability (or asset) recognised in the balance sheet;*
- (f) *the total expense recognised in the income statement for each of the following, and the line item(s) of the income statement 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 under paragraph ~~105~~104A;*
 - (v) *actuarial gains and losses;*
 - (vi) *past service cost; and*
 - (vii) *the effect of any curtailment or settlement;*
- (g) *the actual return on plan assets, as well as the actual return on any reimbursement right recognised as an asset under paragraph ~~105~~104A; and*
- (h) *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 under paragraph ~~105~~104A;*
 - (iv) *the expected rates of salary increases (and of changes in an index or other variable specified in the formal or constructive terms of a plan as the basis for future benefit increases);*
 - (iv) *medical cost trend rates; and*
 - (vi) *any other material actuarial assumptions used.*

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.

~~121~~¹²⁴. Paragraph ~~123~~¹²⁰(b) requires a general description of the type of plan. Such a description distinguishes, for example, flat salary pension plans from final salary pension plans and from post-employment medical plans. Further detail is not required.

~~122~~~~25~~. When an enterprise has more than one defined benefit plan, disclosures may be made in total, separately for each plan, or in such groupings as are considered to be the most useful. It may be useful to distinguish groupings by criteria such as the following:

- (a) the geographical location of the plans, for example by distinguishing domestic plans from foreign plans; or
- (b) whether plans are subject to materially different risks, for example, by distinguishing flat salary pension plans from final salary pension plans and from post-employment medical plans.

When an enterprise provides disclosures in total for a grouping of plans, such disclosures are provided in the form of weighted averages or of relatively narrow ranges.

~~123~~~~26~~. Paragraph 30 requires additional disclosures about multi-employer defined benefit plans that are treated as if they were defined contribution plans.

~~124~~~~27~~. Where required by SSAP 20, Related Party Disclosures, an enterprise discloses information about:

- (a) related party transactions with post-employment benefit plans; and
- (b) post-employment benefits for key management personnel.

~~125~~~~28~~. Where required by SSAP 28, Provisions, Contingent Liabilities and Contingent Assets, an enterprise discloses information about contingent liabilities arising from post-employment benefit obligations.

Other Long-term Employee Benefits

~~126~~~~29~~. Other long-term employee benefits include, for example:

- (a) long-term compensated absences such as long-service or sabbatical leave;
- (b) jubilee or other 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.

~~127~~~~30~~. The measurement of other long-term employee benefits is not usually subject to the same degree of uncertainty as the measurement of post-employment benefits. Furthermore, the introduction of, or changes to, other long-term employee benefits rarely causes a material amount of past service cost. For these reasons, this Statement requires a simplified method of accounting for other long-term employee benefits. This method differs from the accounting required for post-employment benefits as follows:

- (a) actuarial gains and losses are recognised immediately and no 'corridor' is applied; and
- (b) all past service cost is recognised immediately.

Recognition and Measurement

~~128~~~~31~~. *The amount recognised as a liability for other long-term employee benefits should be the net total of the following amounts:*

- (a) *the present value of the defined benefit obligation at the balance sheet date (see paragraph 64);*

- (b) *minus the fair value at the balance sheet date of plan assets (if any) out of which the obligations are to be settled directly (see paragraphs 102 - 104).*

In measuring the liability, an enterprise should apply paragraphs 49 - 91, excluding paragraphs 54 and 61. An enterprise should apply paragraph ~~105~~104A in recognising and measuring any reimbursement right.

129~~132~~. *For other long-term employee benefits, an enterprise should recognise the net total of the following amounts as expense or (subject to paragraph 58) income, except to the extent that another Statement of Standard Accounting Practice requires or permits their inclusion in the cost of an asset:*

- (a) *current service cost (see paragraphs 63 - 91);*
- (b) *interest cost (see paragraph 82);*
- (c) *the expected return on any plan assets (see paragraphs ~~109-111~~ 105-107) and on any reimbursement right recognised as an asset (see paragraph ~~105~~104A);*
- (d) *actuarial gains and losses, which should all be recognised immediately;*
- (e) *past service cost, which should all be recognised immediately; and*
- (f) *the effect of any curtailments or settlements (see paragraphs ~~113~~ 109 and ~~114~~ 110).*

130~~133~~. One form of other long-term employee benefit is long-term disability benefit. If the level of benefit depends on the length of service, an obligation arises when the service is rendered. Measurement of that obligation reflects the probability that payment will be required and the length of time for which payment is expected to be made. If the level of benefit is the same for any disabled employee regardless of years of service, the expected cost of those benefits is recognised when an event occurs that causes a long-term disability.

Disclosure

131~~134~~. Although this Statement does not require specific disclosures about other long-term employee benefits, other Statements of Standard Accounting Practice may require disclosures, for example where the expense resulting from such benefits is of such size, nature or incidence that its disclosure is relevant to explain the performance of the enterprise for the period (see SSAP 2, Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies). Where required by SSAP 20, Related Party Disclosures, an enterprise discloses information about other long-term employee benefits for key management personnel.

Termination Benefits

132~~135~~. This Statement deals with termination benefits separately from other employee benefits because the event which gives rise to an obligation is the termination rather than employee service.

Recognition

133~~136~~. *An enterprise should recognise termination benefits as a liability and an expense when, and only when, the enterprise is demonstrably committed to either:*

- (a) *terminate the employment of an employee or group of employees before the normal retirement date; or*
- (b) *provide termination benefits as a result of an offer made in order to encourage voluntary redundancy.*

134137. *An enterprise is demonstrably committed to a termination when, and only when, the enterprise has a detailed formal plan for the termination and is without realistic possibility of withdrawal. The detailed plan should include, as a minimum:*

- (a) the location, function, and approximate number of employees whose services are to be terminated;*
- (b) the termination benefits for each job classification or function; and*
- (c) the time at which the plan will be implemented. Implementation should begin as soon as possible and the period of time to complete implementation should be such that material changes to the plan are not likely.*

135138. An enterprise 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. Termination benefits are typically lump-sum payments, but sometimes also include:

- (a) enhancement of retirement benefits or of other post-employment benefits, either indirectly through an employee benefit plan or directly; and
- (b) salary until the end of a specified notice period if the employee renders no further service that provides economic benefits to the enterprise.

136139. Some employee benefits are payable regardless of the reason for the employee's departure. The payment of such benefits is certain (subject to any vesting or minimum service requirements) but the timing of their payment is uncertain. Although such benefits are described in some countries as termination indemnities, or termination gratuities, they are post-employment benefits, rather than termination benefits and an enterprise accounts for them as post-employment benefits. Some enterprises provide a lower level of benefit for voluntary termination at the request of the employee (in substance, a post-employment benefit) than for involuntary termination at the request of the enterprise. The additional benefit payable on involuntary termination is a termination benefit.

137140. Termination benefits do not provide an enterprise with future economic benefits and are recognised as an expense immediately.

138141. Where an enterprise recognises termination benefits, the enterprise may also have to account for a curtailment of retirement benefits or other employee benefits (see paragraph ~~113~~ 109).

Measurement

139142. *Where termination benefits fall due more than 12 months after the balance sheet date, they should be discounted using the discount rate specified in paragraph 78.*

140143. *In the case of an offer made to encourage voluntary redundancy, the measurement of termination benefits should be based on the number of employees expected to accept the offer.*

Disclosure

141144. Where there is uncertainty about the number of employees who will accept an offer of termination benefits, a contingent liability exists. As required by SSAP 28, Provisions, Contingent Liabilities and Contingent Assets, an enterprise discloses information about the contingent liability unless the possibility of an outflow in settlement is remote.

- 142~~145~~. As required by SSAP 2, Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies, an enterprise discloses the nature and amount of an expense if it is of such size, nature or incidence that its disclosure is relevant to explain the performance of the enterprise for the period. Termination benefits may result in an expense needing disclosure in order to comply with this requirement.
- 143~~146~~. Where required by SSAP 20, Related Party Disclosures, an enterprise discloses information about termination benefits for key management personnel.

Equity Compensation Benefits

- 144~~147~~. Equity compensation benefits include benefits in such forms as:
- (a) shares, share options, and other equity instruments, issued to employees at less than the fair value at which those instruments would be issued to a third party; and
 - (b) cash payments, the amount of which will depend on the future market price of the reporting enterprise's shares.

Recognition and Measurement

- 145~~148~~. This Statement does not specify recognition and measurement requirements for equity compensation benefits.

Disclosure

- 146~~149~~. The disclosures required below are intended to enable users of financial statements to assess the effect of equity compensation benefits on an enterprise's financial position, performance and cash flows. Equity compensation benefits may affect:
- (a) an enterprise's financial position by requiring the enterprise to issue equity financial instruments or convert financial instruments, for example when employees, or employee compensation plans, hold share options or have partially satisfied the vesting provisions that will enable them to acquire share options in the future; and
 - (b) an enterprise's performance and cash flows by reducing the amount of cash or other employee benefits that the enterprise provides to employees in exchange for their services.
- 147~~150~~. *An enterprise should disclose:*
- (a) *the nature and terms (including any vesting provisions) of equity compensation plans;*
 - (b) *the accounting policy for equity compensation plans;*
 - (c) *the amounts recognised in the financial statements for equity compensation plans;*
 - (d) *the number and terms (including, where applicable, dividend and voting rights, conversion rights, exercise dates, exercise prices and expiry dates) of the enterprise's own equity financial instruments which are held by equity compensation plans (and, in the case of share options, by employees) at the beginning and end of the period. The extent to which employees' entitlements to those instruments are vested at the beginning and end of the period should be specified;*

- (e) *the number and terms (including, where applicable, dividend and voting rights, conversion rights, exercise dates, exercise prices and expiry dates) of equity financial instruments issued by the enterprise to equity compensation plans or to employees (or of the enterprise's own equity financial instruments distributed by equity compensation plans to employees) during the period and the fair value of any consideration received from the equity compensation plans or the employees;*
- (f) *the number, exercise dates and exercise prices of share options exercised under equity compensation plans during the period;*
- (g) *the number of share options held by equity compensation plans, or held by employees under such plans, that lapsed during the period; and*
- (h) *the amount, and principal terms, of any loans or guarantees granted by the reporting enterprise to, or on behalf of, equity compensation plans.*

~~148151.~~ *An enterprise should also disclose:*

- (a) *the fair value, at the beginning and end of the period, of the enterprise's own equity financial instruments (other than share options) held by equity compensation plans; and*
- (b) *the fair value, at the date of issue, of the enterprise's own equity financial instruments (other than share options) issued by the enterprise to equity compensation plans or to employees, or by equity compensation plans to employees, during the period.*

If it is not practicable to determine the fair value of the equity financial instruments (other than share options), that fact should be disclosed.

~~149152.~~ When an enterprise has more than one equity compensation plan, disclosures may be made in total, separately for each plan, or in such groupings as are considered most useful for assessing the enterprise's obligations to issue equity financial instruments under such plans and the changes in those obligations during the current period. Such groupings may distinguish, for example, the location and seniority of the employee groups covered. When an enterprise provides disclosures in total for a grouping of plans, such disclosures are provided in the form of weighted averages or of relatively narrow ranges.

~~150153.~~ When an enterprise has issued share options to employees, or to employee compensation plans, disclosures may be made in total, or in such groupings as are considered most useful for assessing the number and timing of shares that may be issued and the cash that may be received as a result. For example, it may be useful to distinguish options that are 'out-of-the-money' (where the exercise price exceeds the current market price) from options that are 'in-the-money' (where the current market price exceeds the exercise price). Furthermore, it may be useful to combine the disclosures in groupings that do not aggregate options with a wide range of exercise prices or exercise dates.

~~151154.~~ The disclosures required by paragraphs ~~150147~~ and ~~151148~~ are intended to meet the objectives of this Statement. Additional disclosure may be required to satisfy the requirements of SSAP 20, Related Party Disclosures, if an enterprise:

- (a) provides equity compensation benefits to key management personnel;
- (b) provides equity compensation benefits in the form of instruments issued by the enterprise's parent; or
- (c) enters into related party transactions with equity compensation plans.

~~152155.~~ In the absence of specific recognition and measurement requirements for equity compensation plans, information about the fair value of the reporting enterprise's financial instruments used in such plans is useful to users of financial statements. However, because there is no consensus on the appropriate way to determine the fair value of share options, this Statement does not require an enterprise to disclose their fair value.

Transitional Provisions

- ~~153~~¹⁵⁶. This section specifies the transitional treatment for defined benefit plans. Where an enterprise first adopts this Statement for other employee benefits, the enterprise applies SSAP 2, Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies.
- ~~154~~¹⁵⁷. *On first adopting this Statement, an enterprise should determine its transitional liability for defined benefit plans at that date as:*
- (a) *the present value of the obligation (see paragraph 64) at the date of adoption;*
 - (b) *minus the fair value, at the date of adoption, of plan assets (if any) out of which the obligations are to be settled directly (see paragraphs 102 - 104);*
 - (c) *minus any past service cost that, under paragraph 96, should be recognised in later periods.*
- ~~155~~¹⁵⁸. *If the transitional liability is more than the liability that would have been recognised at the same date under the enterprise's previous accounting policy, the enterprise should make an irrevocable choice to recognise that increase as part of its defined benefit liability under paragraph 54:*
- (a) *immediately, under SSAP 2, Net Profit or Loss for the Period, Fundamental Errors and Changes in Accounting Policies; or*
 - (b) *as an expense on a straight-line basis over up to five years from the date of adoption. If an enterprise chooses (b), the enterprise should:*
 - (i) *apply the limit described in paragraph 58(b) in measuring any asset recognised in the balance sheet;*
 - (ii) *disclose at each balance sheet date: (1) the amount of the increase that remains unrecognised; and (2) the amount recognised in the current period;*
 - (iii) *limit the recognition of subsequent actuarial gains (but not negative past service cost) as follows. If an actuarial gain is to be recognised under paragraphs 92 and 93, an enterprise should recognise that actuarial gain only to the extent that the net cumulative unrecognised actuarial gains (before recognition of that actuarial gain) exceed the unrecognised part of the transitional liability; and*
 - (iv) *include the related part of the unrecognised transitional liability in determining any subsequent gain or loss on settlement or curtailment.*
- If the transitional liability is less than the liability that would have been recognised at the same date under the enterprise's previous accounting policy, the enterprise should recognise that decrease immediately under SSAP 2.*
- ~~156~~¹⁵⁹. On the initial adoption of the Statement, the effect of the change in accounting policy includes all actuarial gains and losses that arose in earlier periods even if they fall inside the 10% 'corridor' specified in paragraph 92.

Example Illustrating Paragraphs ~~157~~154 to ~~159~~156

At 31 December 2001, an enterprise's balance sheet includes a pension liability of 100. The enterprise adopts the Statement as of 1 January 2002, when the present value of the obligation under the Statement is 1,300 and the fair value of plan assets is 1,000. On 1 January 1996, the enterprise had improved pensions (cost for non-vested benefits: 160; and average remaining period at that date until vesting: 10 years).

The transitional effect is as follows:

<i>Present value of the obligation</i>	1,300
<i>Fair value of plan assets</i>	(1,000)
<i>Less: past service cost to be recognised in later periods (160 x 4/10)</i>	(64)
	<hr/>
<i>Transitional liability</i>	236
<i>Liability already recognised</i>	(100)
	<hr/>
<i>Increase in liability</i>	136
	<hr/> <hr/>

The enterprise may choose to recognise the increase of 136 either immediately or over up to 5 years. The choice is irrevocable. The enterprise also restates comparative information (SSAP 2) unless impracticable.

At 31 December 2002, the present value of the obligation under the Statement is 1,400 and the fair value of plan assets is 1,050. Net cumulative unrecognised actuarial gains since the date of adopting the Statement are 120. The expected average remaining working life of the employees participating in the plan was eight years. The enterprise has adopted a policy of recognising all actuarial gains and losses immediately, as permitted by paragraph 93.

The effect of the limit in paragraph ~~158~~155(b)(iii) is as follows.

<i>Net cumulative unrecognised actuarial gains</i>	120
<i>Unrecognised part of transitional liability (136 x 4/5)</i>	(109)
	<hr/>
<i>Maximum gain to be recognised (paragraph 158155(b)(iii))</i>	11
	<hr/> <hr/>

Effective Date

157~~160~~. *Except for the revised paragraph 162 concerning accounting for long service payments, the accounting practices set out in this Statement should be regarded as standard in respect of financial statements relating to periods beginning on or after 1 January 2002. Earlier adoption is encouraged but not required. If an enterprise applies this Statement for financial statements covering periods beginning before 1 January 2002, the enterprise should disclose that fact. The revised paragraph 162 should be regarded as standard in respect of financial statements relating to periods beginning on or after 1 January 2003.*

158 - 160. [Not used]

Notes on Legal Requirements in Hong Kong

161. The legal requirements as regards the disclosure of directors' emoluments, rights to acquire shares or debentures and other benefits are dealt with in SSAP 20, Related Party Disclosures.
162. Under the Employment Ordinance, an enterprise is required to make long service payments to its employees upon the termination of their employment or retirement when the employee fulfils certain conditions and the termination meets the required circumstances. However, where an employee is simultaneously entitled to a long service payment and to a retirement scheme payment, the amount of the long service payment may be reduced by certain benefits arising from the retirement scheme. Based on the enterprise's past experience and the directors' knowledge of the business and work force, it is probable that the enterprise will have to make long service payments to some employees on termination of their employment or retirement. Such long service payments are accounted for as ~~"other long-term employee benefits"~~ "post-employment benefits: defined benefit plans" under paragraphs ~~12912648~~ to ~~134131125~~ of the Statement.
163. The references to the "Schedule" below are to the Tenth Schedule to the Companies Ordinance.
164. Paragraph 30(1) of the Schedule defines "provision" as any amount written off or retained by way of providing for depreciation, renewals or diminution in value of assets or any amount retained by way of providing for any known liability of which the amount cannot be determined with substantial accuracy. The amount provided for certain employee benefits (e.g. pensions) falls within this definition.
165. Paragraph 4(1) of the Schedule requires the classification of provisions under headings appropriate to the company's business.
166. Paragraph 6 of the Schedule requires the disclosure of the aggregate amount of provisions (other than provisions for depreciation, renewals and diminution in value of assets) under separate headings.
167. Paragraph 7 of the Schedule requires the disclosure of the source of any increase and the application of any decrease in each sub-heading of provisions.
168. Paragraph 13(1)(f) of the Schedule requires the disclosure of the amount set aside to provisions (other than provisions for depreciation, renewals and diminution in value of assets) or the amount withdrawn from such provisions and not applied for the purposes of the provisions, if its is material.
169. Paragraph 12(5) of the Schedule requires the disclosure of the general nature of any other contingent liabilities not provided for, and, when practicable, the aggregate amount or estimated amount of those liabilities, if it is material. Paragraph 35 of the Statement gives an example of the circumstance where a contingent liability may arise in the context of a multi-employer plan.

Compliance with International Accounting Standard

170. Compliance with this Statement ensures compliance, in all material respects, with International Accounting Standard IAS 19, Employee Benefits.

Appendix A

Illustrative Example

The appendix is illustrative only and does not form part of the standards. The purpose of the appendix is to illustrate the application of the standards to assist in clarifying their meaning. Extracts from income statements and balance sheets are provided to show the effects of the transactions described below. These extracts do not necessarily conform with all the disclosure and presentation requirements of other Statements of Standard Accounting Practice.

Background Information

The following information is given about a funded defined benefit plan. To keep interest computations simple, all transactions are assumed to occur at the year end. The present value of the obligation and the fair value of the plan assets were both 1,000 at 1 January 20X1. Net cumulative unrecognised actuarial gains at that date were 140.

	20X1	20X2	20X3
Discount rate at start of year	10.0%	9.0%	8.0%
Expected rate of return on plan assets at start of year	12.0%	11.1%	10.3%
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
Expected average remaining working lives of employees (years)	10	10	10

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 50 for vested benefits and 30 for non-vested benefits. As at 1 January 20X2, the enterprise estimated that the average period until the non-vested benefits would become vested was three years; the past service cost arising from additional non-vested benefits is therefore recognised on a straight-line basis over three years. The past service cost arising from additional vested benefits is recognised immediately (paragraph 96 of the Statement). The enterprise has adopted a policy of recognising actuarial gains and losses under the minimum requirements of paragraph 93.

Changes in the Present Value of the Obligation and in the Fair Value of the Plan Assets

The first step is to summarise the changes in the present value of the obligation and in the fair value of the plan assets and use this to determine the amount of the actuarial gains or losses for the period. These are as follows:

	<i>20X1</i>	<i>20X2</i>	<i>20X3</i>
Present value of obligation, 1 January	1,000	1,141	1,197
Interest cost	100	103	96
Current service cost	130	140	150
Past service cost - non-vested benefits	-	30	-
Past service cost - vested benefits	-	50	-
Benefits paid	(150)	(180)	(190)
Actuarial (gain) loss on obligation (balancing figure)	61	(87)	42
Present value of obligation, 31 December	<u>1,141</u>	<u>1,197</u>	<u>1,295</u>
Fair value of plan assets, 1 January	1,000	1,092	1,109
Expected return on plan assets	120	121	114
Contributions	90	100	110
Benefits paid	(150)	(180)	(190)
Actuarial gain (loss) on plan assets (balancing figure)	32	(24)	(50)
Fair value of plan assets, 31 December	<u>1,092</u>	<u>1,109</u>	<u>1,093</u>

Limits of the 'Corridor'

The next step is to determine the limits of the corridor and then compare these with the cumulative unrecognised actuarial gains and losses in order to determine the net actuarial gain or loss to be recognised in the following period. Under paragraph 92 of the Statement, the limits of the 'corridor' are set at the greater of:

- (a) 10% of the present value of the obligation before deducting plan assets; and
- (b) 10% of the fair value of any plan assets.

These limits, and the recognised and unrecognised actuarial gains and losses, are as follows:

	<i>20X1</i>	<i>20X2</i>	<i>20X3</i>
Net cumulative unrecognised actuarial gains (losses) at 1 January	140	107	170
Limits of 'corridor' at 1 January	100	114	120
	-----	-----	-----
Excess [A]	40	-	50
	=====	=====	=====
Average expected remaining working lives (years) [B]	10	10	10
Actuarial gain (loss) to be recognised [A/B]	4	-	5
Unrecognised actuarial gains (losses) at 1 January	140	107	170
Actuarial gain (loss) for year - obligation	(61)	87	(42)
Actuarial gain (loss) for year - plan assets	32	(24)	(50)
	-----	-----	-----
Subtotal	111	170	78
Actuarial (gain) loss recognised	(4)	-	(5)
	-----	-----	-----
Unrecognised actuarial gains (losses) at 31 December	107	170	73
	=====	=====	=====

Amounts Recognised in the Balance Sheet and Income Statement, and Related Analyses

The final step is to determine the amounts to be recognised in the balance sheet and income statement, and the related analyses to be disclosed under paragraphs ~~123~~120(c), (e), (f) and (g) of the Statement. These are as follows:

	20X1	20X2	20X3
Present value of the obligation	1,141	1,197	1,295
Fair value of plan assets	(1,092)	(1,109)	(1,093)
	<u>49</u>	<u>88</u>	<u>202</u>
Unrecognised actuarial gains (losses)	107	170	73
Unrecognised past service cost - non-vested benefits	-	(20)	(10)
Liability recognised in balance sheet	<u>156</u>	<u>238</u>	<u>265</u>
Current service cost	130	140	150
Interest cost	100	103	96
Expected return on plan assets	(120)	(121)	(114)
Net actuarial (gain) loss recognised in year	(4)	-	(5)
Past service cost - non-vested benefits	-	10	10
Past service cost - vested benefits	-	50	-
Expense recognised in the income statement	<u>106</u>	<u>182</u>	<u>137</u>

Movements in the net liability recognised in the balance sheet, to be disclosed under paragraph ~~123~~120(e):

Opening net liability	140	156	238
Expense as above	106	182	137
Contributions paid	(90)	(100)	(110)
	<u>156</u>	<u>238</u>	<u>265</u>

Actual return on plan assets, to be disclosed under paragraph ~~123~~120(g):

Expected return on plan assets	120	121	114
Actuarial gain (loss) on plan assets	32	(24)	(50)
	<u>152</u>	<u>97</u>	<u>64</u>

Note: see example illustrating paragraphs ~~105—107~~104A - C for presentation of reimbursements.

Appendix B

Illustrative Disclosures

The appendix is illustrative only and does not form part of the standards. The purpose of the appendix is to illustrate the application of the standards to assist in clarifying their meaning. Extracts from notes to the financial statements show how the required disclosures may be aggregated in the case of a large multi-national group that provides a variety of employee benefits. These extracts do not necessarily conform with all the disclosure and presentation requirements of other Statements of Standard Accounting Practice. In particular, they do not illustrate the disclosure of:

- (a) accounting policies for employee benefits (see SSAP 1, Presentation of Financial Statements). Under paragraph ~~123~~120(a) of the Statement, this disclosure should include the enterprise's accounting policy for recognising actuarial gains and losses; or*
- (b) employee benefits granted to directors and key management personnel (see SSAP 20, Related Party Disclosures).*

Employee Benefit Obligations

The amounts recognised in the balance sheet are as follows:

	Defined benefit pension plans		Post-employment medical benefits	
	20X2	20X1	20X2	20X1
Present value of funded obligations	12,310	11,772	2,819	2,721
Fair value of plan assets	(11,982)	(11,188)	(2,480)	(2,415)
	328	584	339	306
Present value of unfunded obligations	6,459	6,123	5,160	5,094
Unrecognised actuarial gains (losses)	(97)	(17)	31	72
Unrecognised past service cost	(450)	(650)	-	-
Net liability in balance sheet	6,240	6,040	5,530	5,472

	Defined benefit pension plans		Post-employment medical benefits	
	20X2	20X1	20X2	20X1
Amounts in the balance sheet:				
liabilities	6,451	6,278	5,530	5,472
assets	(211)	(238)	-	-
Net liability in balance sheet	<u>6,240</u>	<u>6,040</u>	<u>5,530</u>	<u>5,472</u>

The pension plan assets include ordinary shares issued by [name of reporting enterprise] with a fair value of 317 (20X1: 281). Plan assets also include property occupied by [name of reporting enterprise] with a fair value of 200 (20X1: 185).

The amounts recognised in the income statement are as follows:

	Defined benefit pension plans		Post-employment medical benefits	
	20X2	20X1	20X2	20X1
Current service cost	1,679	1,554	471	411
Interest on obligation	1,890	1,650	819	705
Expected return on plan assets	(1,392)	(1,188)	(291)	(266)
Net actuarial losses (gains) recognised in year	90	(187)	-	-
Past service cost	200	200	-	-
Losses (gains) on curtailments and settlements	221	(47)	-	-
Total, included in 'staff costs'	<u>2,688</u>	<u>1,982</u>	<u>999</u>	<u>850</u>
Actual return on plan assets	<u>1,232</u>	<u>1,205</u>	<u>275</u>	<u>254</u>

Movements in the net liability recognised in the balance sheet are as follows:

	Defined benefit pension plans		Post-employment medical benefits	
	20X2	20X1	20X2	20X1
Net liability at start of year	6,040	5,505	5,472	5,439
Net expense recognised in the income statement	2,688	1,982	999	850
Contributions	(2,261)	(1,988)	(941)	(817)
Exchange differences on foreign plan	(227)	221	-	-
Liabilities acquired in business combinations	-	320	-	-
Net liability at end of year	<u>6,240</u>	<u>6,040</u>	<u>5,530</u>	<u>5,472</u>

Principal actuarial assumptions at the balance sheet date (expressed as weighted averages):

	20X2	20X1
Discount rate at 31 December	10.0%	9.1%
Expected return on plan assets at 31 December	12.0%	10.9%
Future salary increases	5%	4%
Future pension increases	3%	2%
Proportion of employees opting for early retirement	30%	30%
Annual increase in health care costs	8%	8%
Future changes in maximum state health care benefits	3%	2%

The group also participates in an industry-wide defined benefit plan which provides pensions linked to final salaries and is funded on a pay-as-you-go basis. It is not practicable to determine the present value of the group's obligation or the related current service cost as the plan computes its obligations on a basis that differs materially from the basis used in [name of reporting enterprise]'s financial statements. [describe basis] On that basis, the plan's financial statements to 30 June 20X0 show an unfunded liability of 27,525. The unfunded liability will result in future payments by participating employers. The plan has approximately 75,000 members, of whom approximately 5,000 are current or former employees of [name of reporting enterprise] or their dependants. The expense recognised in the income statement, which is equal to contributions due for the year, and is not included in the above amounts, was 230 (20X1: 215). The group's future contributions may be increased substantially if other enterprises withdraw from the plan.

Equity Compensation Benefits

Share Option Plan

The group offers vested share options, without payment, to directors and other senior employees with more than three years' service. Movements in the number of share options held by employees are as follows:

	20X2	20X1
Outstanding at 1 January	10,634	10,149
Issued	2,001	1,819
Exercised	(957)	(891)
Lapsed	(481)	(443)
	<hr/>	<hr/>
Outstanding at 31 December	<u>11,197</u>	<u>10,634</u>

Details of share options granted during the period:

Expiry date	1/1/X7	1/1/X6
Exercise price per share	12.17 - 12.27	10.05 - 10.22
Aggregate proceeds if shares are issued ('000)	24	20
Amounts recognised in the balance sheet and income statement (and accounting policy)	<i>Not shown in this example, as the Statement prescribes no particular accounting treatment.</i>	

Details of share options exercised during the period:

Expiry date	1/1/X2	1/1/X1
Exercise price per share	7.45 - 7.49	7.37 - 7.48
Aggregate issue proceeds ('000)	7	7

Terms of the options outstanding at 31 December:

<i>Expiry date</i>	<i>Exercise price</i>	<i>20X2 Number</i>	<i>20X1 Number</i>
1 January 20X2	7.43 - 7.51	-	1,438
1 January 20X3	7.57 - 7.65	1,952	1,952
1 January 20X4	7.89 - 8.01	2,118	2,118
1 January 20X5	9.09 - 9.12	3,307	3,307
1 January 20X6	10.05 - 10.22	1,819	1,819
1 January 20X7	12.17 - 12.27	2,001	-
		11,197	10,634
		11,197	10,634

Employee Share Ownership Plan

The Enterprise operates an Employee Share Ownership Plan for senior employees with more than three years' service. The Enterprise grants unsecured, interest-free loans with no fixed repayment terms to the Plan which enable the Plan to acquire Ordinary Shares in the Enterprise. The shares carry full dividend and voting rights. The Plan subsequently allocates shares to employees who meet certain performance criteria. Employees are not required to contribute to the cost of the shares. Movements in shares held by the Plan were as follows:

	<i>20X2</i>	<i>20X1</i>
Outstanding at 1 January	125	100
Issued to the Plan for consideration of 60 (20X1: 52)	42	37
Allocated to employees	(18)	(12)
	149	125
Outstanding at 31 December	149	125
Fair value of shares held at 31 December	781	607
Loans outstanding at 31 December	590	530
Fair value, on issuance, of shares issued in the year	166	137
Fair value of shares allocated to employees in the year	57	41
Amounts recognised in the balance sheet and income statement (and accounting policy)	<i>Not shown in this example, as the Statement prescribes no particular accounting treatment.</i>	

Appendix C

Illustration of the application of paragraph 58A

The issue

Paragraph 58 of the Statement imposes a ceiling on the defined benefit asset that can be recognised.

58. The amount determined under paragraph 54 may be negative (an asset). An enterprise should measure the resulting asset at the lower of:

- (a) the amount determined under paragraph 54 [ie the surplus/deficit in the plan plus (minus) any unrecognised losses (gains)]; and**
- (b) the total of:**
 - (i) any cumulative unrecognised net actuarial losses and past service cost (see paragraphs 92, 93 and 96); and**
 - (ii) the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan. The present value of these economic benefits should be determined using the discount rate specified in paragraph 78.**

Without paragraph 58A (see below), paragraph 58(b)(i) has the following consequence: sometimes deferring the recognition of an actuarial loss (gain) in determining the amount specified by paragraph 54 leads to a gain (loss) being recognised in the income statement.

The following example illustrates the effect of applying paragraph 58 without paragraph 58A. The example assumes that the enterprise's accounting policy is not to recognise actuarial gains and losses within the 'corridor' and to amortise actuarial gains and losses outside the 'corridor'. (Whether the 'corridor' is used is not significant. The issue can arise whenever there is deferred recognition under paragraph 54.)

Example 1

	A	B	C	D =A+C	E =B+C	F =lower of D and E	G
Year	Surplus in plan	Economic benefits available (paragraph 58(b)(ii))	Losses unrecognised under paragraph 54	Paragraph 54	Paragraph 58(b)	Asset ceiling, ie recognised asset	Gain recognised in year 2
1	100	0	0	100	0	0	
2	70	0	30	100	30	30	30

At the end of year 1, there is a surplus of 100 in the plan (column A in the table above), but no economic benefits are available to the enterprise either from refunds or reductions in future contributions* (column B). There are no unrecognised gains and losses under paragraph 54 (column C). So, if there were no asset ceiling, an asset of 100 would be recognised, being the amount specified by paragraph 54 (column D). The asset ceiling in paragraph 58 restricts the asset to nil (column F).

In year 2 there is an actuarial loss in the plan of 30 that reduces the surplus from 100 to 70 (column A) the recognition of which is deferred under paragraph 54 (column C). So, if there were no asset ceiling, an asset of 100 (column D) would be recognised. The asset ceiling without paragraph 58A would be 30 (column E). An asset of 30 would be recognised (column F), giving rise to a gain in income (column G) even though all that has happened is that a surplus from which the enterprise cannot benefit has decreased.

Paragraph 58A

Paragraph 58A prohibits the recognition of gains (losses) that arise solely from past service cost and actuarial losses (gains).

58A. ***The application of paragraph 58 should not result in a gain being recognised solely as a result of an actuarial loss or past service cost in the current period or in a loss being recognised solely as a result of an actuarial gain in the current period. The enterprise should therefore recognise immediately under paragraph 54 the following, to the extent that they arise while the defined benefit asset is determined in accordance with paragraph 58(b):***

(a) net actuarial losses of the current period and past service cost of the current period to the extent that they exceed any reduction in the present value of the economic benefits specified in paragraph 58(b)(ii). If there is no change or an increase in the present value of the economic benefits, the entire net actuarial losses of the current period and past service cost of the current period should be recognised immediately under paragraph 54.

(b) net actuarial gains of the current period after the deduction of past service cost of the current period to the extent that they exceed any increase in the present value of the economic benefits specified in paragraph 58(b)(ii). If there is no change or a decrease in the present value of the economic benefits, the entire net actuarial gains of the current period after the deduction of past service cost of the current period should be recognised immediately under paragraph 54.

In the above example, there is no change in the present value of the economic benefits available to the enterprise. The application of paragraph 58A becomes more complex when there are changes in present value of the economic benefits available, as illustrated in the following examples.

Example 2 - adjustment when there are actuarial losses and a decrease in the economic benefits available

	A	B	C	D =A+C	E =B+C	F =lower of D and E	G
Year	Surplus in plan	Economic benefits available (paragraph 58(b)(ii))	Losses unrecognised under paragraph 54	Paragraph 54	Paragraph 58(b)	Asset ceiling, ie recognised asset	Gain recognised in year 2
1	60	30	40	100	70	70	
2	25	20	50	75	70	70	0

* based on the current terms of the plan.

At the end of year 1, there is a surplus of 60 in the plan (column A) and economic benefits available to the enterprise of 30 (column B). There are unrecognised losses of 40 under paragraph 54* (column C). So, if there were no asset ceiling, an asset of 100 would be recognised (column D). The asset ceiling restricts the asset to 70 (column F).

In year 2, an actuarial loss of 35 in the plan reduces the surplus from 60 to 25 (column A). The economic benefits available to the enterprise fall by 10 from 30 to 20 (column B). Applying paragraph 58A, the actuarial loss of 35 is analysed as follows:

<u>Actuarial loss equal to the reduction in economic benefits</u>	10
<u>Actuarial loss that exceeds the reduction in economic benefits</u>	25

In accordance with paragraph 58A, 25 of the actuarial loss is recognised immediately under paragraph 54 (column D). The reduction in economic benefits of 10 is included in the cumulative unrecognised losses that increase to 50 (column C). The asset ceiling, therefore, also remains at 70 (column E) and no gain is recognised.

In effect, an actuarial loss of 25 is recognised immediately, but is offset by the reduction in the effect of the asset ceiling.

	Balance sheet asset under paragraph 54 (column D above)	Effect of the asset ceiling	Asset ceiling (column F above)
Year 1	100	(30)	70
Year 2	75	(5)	70
Gain/(loss)	(25)	25	0

Example 3 - adjustment when there are actuarial gains and a decrease in the economic benefits available to the enterprise

	A	B	C	D =A+C	E =B+C	F =lower of D and E	G
Year	Surplus in plan	Economic benefits available (paragraph 58(b)(ii))	Losses unrecognised under paragraph 54	Paragraph 54	Paragraph 58(b)	Asset ceiling, ie recognised asset	Gain recognised in year 2
1	60	30	40	100	70	70	
2	110	25	40	150	65	65	(5)

* The application of paragraph 58A allows the recognition of some actuarial gains and losses to be deferred under paragraph 54 and, hence, to be included in the calculation of the asset ceiling. For example, cumulative unrecognised actuarial losses that have built up while the amount specified by paragraph 58(b) is not lower than the amount specified by paragraph 54 will not be recognised immediately at the point that the amount specified by paragraph 58(b) becomes lower. Instead their recognition will continue to be deferred in line with the enterprise's accounting policy. The cumulative unrecognised losses in this example are losses the recognition of which is deferred even though paragraph 58A applies.

At the end of year 1 there is a surplus of 60 in the plan (column A) and economic benefits available to the enterprise of 30 (column B). There are unrecognised losses of 40 under paragraph 54 that arose before the asset ceiling had any effect (column C). So, if there were no asset ceiling, an asset of 100 would be recognised (column D). The asset ceiling restricts the asset to 70 (column F).

In year 2, an actuarial gain of 50 in the plan increases the surplus from 60 to 110 (column A). The economic benefits available to the enterprise decrease by 5 (column B). Applying paragraph 58A, there is no increase in economic benefits available to the enterprise. Therefore, the entire actuarial gain of 50 is recognised immediately under paragraph 54 (column D) and the cumulative unrecognised loss under paragraph 54 remains at 40 (column C). The asset ceiling decreases to 65 because of the reduction in economic benefits. That reduction is not an actuarial loss as defined by SSAP 34 and therefore does not qualify for deferred recognition.

In effect, an actuarial gain of 50 is recognised immediately, but is (more than) offset by the increase in the effect of the asset ceiling.

	Balance sheet asset under paragraph 54 (column D above)	Effect of the asset ceiling	Asset ceiling (column F above)
Year 1	100	(30)	70
Year 2	150	(85)	65
Gain/(loss)	50	(55)	(5)

In both examples 2 and 3 there is a reduction in economic benefits available to the enterprise. However, in example 2 no loss is recognised whereas in example 3 a loss is recognised. This difference in treatment is consistent with the treatment of changes in the present value of economic benefits before paragraph 58A was introduced. The purpose of paragraph 58A is solely to prevent gains (losses) being recognised because of past service cost or actuarial losses (gains). As far as is possible, all other consequences of deferred recognition and the asset ceiling are left unchanged.

Example 4 - adjustment in a period in which the asset ceiling ceases to have an effect

	A	B	C	D =A+C	E =B+C	F =lower of D and E	G
Year	Surplus in plan	Economic benefits available (paragraph 58(b)(ii))	Losses unrecognised under paragraph 54	Paragraph 54	Paragraph 58(b)	Asset ceiling, ie recognised asset	Gain recognised in year 2
1	60	25	40	100	65	65	
2	(50)	0	115	65	115	65	0

At the end of year 1 there is a surplus of 60 in the plan (column A) and economic benefits are available to the enterprise of 25 (column B). There are unrecognised losses of 40 under paragraph 54 that arose before the asset ceiling had any effect (column C). So, if there were no asset ceiling, an asset of 100 would be recognised (column D). The asset ceiling restricts the asset to 65 (column F).

In year 2, an actuarial loss of 110 in the plan reduces the surplus from 60 to a deficit of 50 (column A). The economic benefits available to the enterprise decrease from 25 to 0 (column B). To apply paragraph 58A it is necessary to determine how much of the actuarial loss arises while the defined benefit asset is determined in accordance with paragraph 58(b). Once the surplus becomes a deficit, the amount determined by paragraph 54 is lower than the net total under paragraph 58(b). So, the actuarial loss that arises while the defined benefit asset is determined in accordance with paragraph 58(b) is the loss that reduces the surplus to nil, ie 60. The actuarial loss is, therefore, analysed as follows:

Actuarial loss that arises while the defined benefit asset is measured under paragraph 58(b):

<u>Actuarial loss that equals the reduction in economic benefits</u>	25
<u>Actuarial loss that exceeds the reduction in economic benefits</u>	35
	—
	60
<u>Actuarial loss that arises while the defined benefits asset is measured under paragraph 54</u>	50
	—
<u>Total actuarial loss</u>	110

In accordance with paragraph 58A, 35 of the actuarial loss is recognised immediately under paragraph 54 (column D); 75 (25+50) of the actuarial loss is included in the cumulative unrecognised losses which increase to 115 (column C). The amount determined under paragraph 54 becomes 65 (column D) and under paragraph 58(b) becomes 115 (column E). The recognised asset is the lower of the two, ie 65 (column F), and no gain or loss is recognised (column G).

In effect, an actuarial loss of 35 is recognised immediately, but is offset by the reduction in the effect of the asset ceiling.

	Balance sheet asset under paragraph 54 (column D above)	Effect of the asset ceiling	Asset ceiling (column F (above))
Year 1	100	(35)	65
Year 2	65	0	65
Gain/(loss)	(35)	35	0

Notes

- 1 In applying paragraph 58A in situations when there is an increase in the present value of the economic benefits available to the enterprise, it is important to remember that the present value of the economic benefits available cannot exceed the surplus in the plan.¹

¹ The example following paragraph 60 of SSAP 34 is corrected so that the present value of available future refunds and reductions in contributions equals the surplus in the plan of 90 (rather than 100), with a further correction to make the limit 270 (rather than 280).

- 2 In practice, benefit improvements often result in a past service cost and an increase in expected future contributions due to increased current service costs of future years. The increase in expected future contributions may increase the economic benefits available to the enterprise in the form of anticipated reductions in those future contributions. The prohibition against recognising a gain solely as a result of past service cost in the current period does not prevent the recognition of a gain because of an increase in economic benefits. Similarly, a change in actuarial assumptions that causes an actuarial loss may also increase expected future contributions and, hence, the economic benefits available to the enterprise in the form of anticipated reductions in future contributions. Again, the prohibition against recognising a gain solely as a result of an actuarial loss in the current period does not prevent the recognition of a gain because of an increase in economic benefits.

Appendix D

Basis for Conclusions

The Hong Kong Society of Accountants (HKSA) Financial Accounting Standards Committee (FASC) agreed with the IASB's (Board) basis for amending the asset ceiling. The relevant section of the IASB's basis for conclusions is reproduced below for reference (paragraph numbers referred to below correspond with those in SSAP 34).

- 78A. In April 2002, the Board agreed on an amendment to the limit on the recognition of an asset (the asset ceiling) in paragraph 58 of the Standard. The objective of the amendment was to prevent gains (losses) being recognised solely as a result of the deferred recognition of past service cost and actuarial losses (gains).
- 78B. The asset ceiling is specified in paragraph 58 of IAS 19, which requires a defined benefit asset to be measured at the lower of
- (a) the amount determined under paragraph 54; and
 - (b) the total of:
 - (i) any cumulative unrecognised net actuarial losses and past service cost; and
 - (ii) the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.
- 78C. The problem arises when an enterprise defers recognition of actuarial losses or past service cost in determining the amount specified in paragraph 54 but is required to measure the defined benefit asset at the net total specified in paragraph 58(b). Paragraph 58(b)(i) could result in the enterprise recognising an increased asset because of actuarial losses or past service cost in the period. The increase in the asset would be reported as a gain in income. Examples illustrating the issue are given in Appendix C.
- 78D. The Board agreed that recognising gains (losses) arising from past service cost and actuarial losses (gains) is not representationally faithful. Further, the Board holds the view that this issue demonstrates that IAS 19 can give rise to serious problems. The Board intends to undertake a comprehensive review of the aspects of IAS 19 that cause concern, including the interaction of the asset ceiling and the options to defer recognition of certain gains and losses. In the meantime, the Board regards as an improvement a limited amendment to prevent their interaction giving rise to unfaithful representations of events.
- 78E. Paragraph 58A, therefore, prevents gains (losses) from being recognised solely as a result of the deferred recognition of past service cost or actuarial losses (gains).
- 78F. Some Board members and respondents to the exposure draft of this amendment suggested that the issue be dealt with by removing paragraph 58(b)(i). Paragraph 58(b)(i) is the component of the asset ceiling that gives rise to the problem: losses that are unrecognised under paragraph 54 are added to the amount that can be recognised as an asset. However, deleting paragraph 58(b)(i) effectively removes the option of deferred recognition of actuarial losses for all enterprises that have a defined benefit asset. Removing this option would have wide reaching implications for the deferred recognition approach in IAS 19 that can be considered fully only within the context of the comprehensive review noted above.

APPENDIX E**Comparison with International Accounting Standards**

This comparison appendix, which was prepared as at 31 July 2002 and deals only with significant differences in the standards extant, is produced for information only and does not form part of the standards in SSAP 34.

The International Accounting Standard comparable with SSAP 34 is IAS 19 (revised 2002), Employee Benefits.

The following sets out the major textual differences between SSAP 34 and IAS 19 and the reasons for such differences.

Differences	Reasons for the differences
<p>1. <u>IAS 19 para 2 SSAP 34 para 2</u></p> <p>IAS 19 paragraph 2 has a cross-reference to IAS 26, Accounting and Reporting by Retirement Benefit Plans. The corresponding paragraph in SSAP 34, however, has a cross-reference to Accounting Guideline 2.302, Financial Statements of Retirement Schemes.</p>	<p>Accounting Guideline 2.302 is the guidance in Hong Kong that deals with reporting by employee benefits plans.</p>
<p>2. <u>IAS 19 para 76 SSAP 34 para 76</u></p> <p>IAS 19 paragraph 76 has a cross-reference to IAS 29, Financial Reporting in Hyperinflationary Economics. The corresponding paragraph in SSAP 34, however, does not include a similar cross-reference.</p>	<p>There is currently no SSAP equivalent to IAS 29.</p>
<p>3. <u>IAS 19 para 117</u></p> <p>IAS 19 includes a statement pointing out that the offsetting criteria in IAS 19 is similar to those established for financial instruments in IAS 32, Financial Instruments: Disclosure and Presentation. SSAP 34 does not contain such a statement.</p>	<p>There is currently no SSAP equivalent to IAS 32.</p>