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Exposure Draft ED/2009/4

Prepayments of a Minimum Funding Requirement

Proposed amendments to IFRIC 14

Comments to be received by 27 July 2009

International Accounting Standards Board®

Exposure Draft

PREPAYMENTS OF A MINIMUM FUNDING REQUIREMENT

(proposed amendments to IFRIC 14)

Comments to be received by 27 July 2009

ED/2009/4

This exposure draft *Prepayments of a Minimum Funding Requirement* (proposed amendments to IFRIC 14) is published by the International Accounting Standards Board (IASB) for comment only. The proposals may be modified in the light of the comments received before being issued in final form as amendments to IFRIC 14.

Comments on the exposure draft and the Basis for Conclusions should be submitted in writing so as to be received by **27 July 2009.** Respondents are asked to send their comments electronically to the IASB website (www.iasb.org), using the 'Open to Comment' page.

All responses will be put on the public record unless the respondent requests confidentiality. However, such requests will not normally be granted unless supported by good reason, such as commercial confidence.

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Introduction

IFRIC 14 *IAS 19—The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* was issued in July 2007 with mandatory application for annual periods beginning on or after 1 January 2008. This exposure draft contains proposals by the International Accounting Standards Board to amend IFRIC 14. The proposals would remove an unintended consequence arising from the treatment of prepayments in some circumstances when there is a minimum funding requirement.

Invitation to comment

The Board invites comments on all aspects of the amendments to IFRIC 14 proposed in this exposure draft. Comments are most helpful if they:

(a) indicate the specific paragraph or group of paragraphs to which they relate,

(b) contain a clear rationale, and

(c) include any alternative the Board should consider, if applicable.

The Board is not requesting comments on matters not addressed in this exposure draft. Comments should be submitted in writing so as to be received no later than 27 July 2009.

Proposed amendments to IFRIC 14 *IAS 19—The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*

Paragraphs 18, 20 and 21 are amended and paragraph 22 is deleted (new text is underlined and deleted text is struck through). Paragraph 19 is not proposed for amendment but is included here for ease of reference. Paragraphs 20A, 27B and 28A are added.

Consensus

The effect of a minimum funding requirement on the economic benefit available as a reduction in future contributions

18 An entity shall analyse any minimum funding requirement at a given date into contributions that are required to cover (a) any existing shortfall for past service on the minimum funding basis and (b) ~~the future accrual of benefits~~ <u>future service</u>.

19 Contributions to cover any existing shortfall on the minimum funding basis in respect of services already received do not affect future contributions for future service. They may give rise to a liability in accordance with paragraphs 23–26.

20 If there is a minimum funding requirement for contributions relating to ~~the~~ future ~~accrual of benefits~~ <u>service</u>, an entity shall <u>recognise an asset comprising:</u>

<u>(a)</u> <u>the amount of any prepayment of the minimum funding requirement contributions, ie any amount of any minimum funding requirement contributions that the entity has paid before being required to do so that gives the entity the right to reduce future minimum funding requirement contributions; and</u>

(b) the amount of any ~~determine the~~ economic benefit available as a reduction in future contributions determined as the lower ~~present value~~ of:

(i) the surplus in the plan excluding any prepayment in (a); and

~~(a)~~(ii) the estimated future service cost in each ~~year~~ period in accordance with paragraphs 16 and 17, less ~~(b)~~ the estimated minimum funding requirement contributions that would be required ~~in respect of the~~ for future ~~accrual of benefits~~ service in that ~~year~~ period if there were no prepayment of those contributions as described in (a).

20A If the amount determined in accordance with paragraph 20(b) is less than zero, an entity shall not recognise a liability or a reduction in the asset determined in accordance with paragraph 20(a).

21 An entity shall calculate the future minimum funding contributions required for ~~in respect of the~~ future ~~accrual of benefits~~ service taking into account the effect of any existing surplus determined in accordance with ~~on~~ the minimum funding requirement ~~basis~~. An entity shall use the assumptions required by the minimum funding requirement and, for any factors not specified by the minimum funding requirement, assumptions consistent with those used to determine the defined benefit obligation and with the situation that exists at the end of the reporting period as determined by IAS 19. The calculation shall include any changes in assumptions expected as a result of the entity paying the minimum contributions due. However, the calculation shall not include the effect of expected changes in the terms and conditions of the minimum funding requirement that are not contracted or substantively enacted ~~or contractually agreed~~ at the end of the reporting period.

22 [Deleted] ~~If the future minimum funding contribution required in respect of the future accrual of benefits exceeds the future IAS 19 service cost in any given year, the present value of that excess reduces the amount of the asset available as a reduction in future contributions at the end of the reporting period. However, the amount of the asset available as a reduction in future contributions can never be less than zero.~~

Effective date

27B Paragraphs 18, 20 and 21 were amended, paragraph 22 was deleted and paragraph 20A was added by *Prepayments of a Minimum Funding Requirement* issued in [month, year]. An entity shall apply those amendments for annual periods beginning on or after [date to be inserted when the amendments are finalised]. Earlier application is permitted. If an entity applies those amendments for an earlier period, it shall disclose that fact.

Transition

28A An entity shall apply the amendments in paragraphs 18, 20, 20A, 21 and 22 from the beginning of the earliest comparative period presented in the first financial statements in which the entity applied IFRIC 14. An entity shall recognise in retained earnings at the beginning of that period any initial adjustment arising from the application of those amendments.

In the illustrative examples, paragraphs IE9, IE11, IE12, IE16 and IE17 of Example 3 are amended (new text is underlined and deleted text is struck through). The changes to Example 3 reflect only changes in terminology and are not substantive. Example 4 is added.

Example 3—Effect of a minimum funding requirement when the contributions payable would not be fully available and the effect on the economic benefit available as a future contribution reduction

IE9 An entity has a funding level on the minimum funding requirement basis (which is measured on a different basis from that required under IAS 19) of 95 per cent in Plan C. Under the minimum funding requirements, the entity is required to pay contributions to increase the funding level to 100 per cent over the next three years. The contributions are required to make good the deficit on the minimum funding requirement basis (shortfall) and to cover future service ~~the accrual of benefits in each year on the minimum funding basis~~.

IE11 The nominal amounts of the minimum funding contribution requirements in respect of the shortfall and the future IAS 19 service cost for the next three years are set out below.

Year	Total minimum contribution requirement	Minimum contributions required to make good the shortfall	Minimum contributions required to cover future ~~accrual~~ service
1	135	120	15
2	125	112	13
3	115	104	11

Application of requirements

IE12 The entity's present obligation in respect of services already received includes the contributions required to make good the shortfall but does not include the minimum contributions required to cover future service ~~accrual~~.

IE16 In accordance with paragraph 20 of IFRIC 14, the economic benefit available as a reduction in future contributions is the present value of:

(a) the estimated future service cost in each period ~~year to the entity~~, less

(b) ~~any~~ the estimated minimum funding requirement contributions that would be required for the ~~requirements in respect of the~~ future service in that period ~~accrual of benefits in that year~~

over the expected life of the plan.

IE17 The amounts available as a future contribution reduction are set out below.

Year	IAS 19 service cost	Minimum contributions required to cover future service ~~accrual~~	Amount available as contribution reduction
1	13	15	(2)
2	13	13	0
3	13	11	2
4+	13	9	4

Example 4—Effect of a prepayment when a minimum funding requirement exceeds the expected future service charge

IE22 An entity is required to fund Plan D so that there is no deficit determined in accordance with the minimum funding requirement. The entity is required to pay minimum funding requirement contributions to cover the service cost in each period determined in accordance with the minimum funding requirement.

IE23 Plan D also has an IAS 19 surplus of CU35[*] that cannot be refunded to the entity under any circumstances but can be used for reductions in future contributions. There are no unrecognised amounts. This example assumes that the discount rate and expected return on assets are 0 per cent.

IE24 The minimum contributions required to cover future service are CU15 for each year of the next five-year period. The expected service cost is CU10 in each year. For simplicity, this example assumes that the plan does not continue after five years.

[*] In this example monetary amounts are denominated in 'currency units (CU)'.

IE25 The entity makes a prepayment of CU30 in respect of years 20X1 and 20X2, increasing its surplus at the beginning of 20X1 to CU65. That prepayment reduces the future contributions it expects to make in the following two years, as follows:

Year	20X1	20X2	20X3	20X4	20X5
Service charge/CU	10	10	10	10	10
Minimum funding requirement contribution/CU	0	0	15	15	15

Application of requirements

IE26 In accordance with paragraph 20 of IFRIC 14, the entity recognises an asset comprising:

(a) CU30, being the amount of the prepayment of the minimum funding requirement contribution; and

(b) CU0. No part of the surplus of CU35 described in paragraph IE23 may be recognised because, if there were no prepayment, the estimated minimum funding requirement contributions (CU75) that would be required for future service exceeds the estimated future service cost (CU50).

IE27 Thus the entity recognises a recoverable asset of CU30.

In the Basis for Conclusions, paragraph BC25 is amended.

BC25 The entity's minimum funding requirements at a given date can be analysed into the contributions that are required to cover (a) an existing shortfall for past service on the minimum funding basis and (b) ~~the~~ future service ~~accrual of benefits~~.

Approval by the Board of *Prepayments of a Minimum Funding Requirement* (proposed amendments to IFRIC 14) published in May 2009

Prepayments of a Minimum Funding Requirement (proposed amendments to IFRIC 14) was approved for publication by the fourteen members of the International Accounting Standards Board.

Sir David Tweedie	Chairman
Thomas E Jones	Vice-Chairman
Mary E Barth	
Stephen Cooper	
Philippe Danjou	
Jan Engström	
Robert P Garnett	
Gilbert Gélard	
Prabhakar Kalavacherla	
James J Leisenring	
Warren J McGregor	
John T Smith	
Tatsumi Yamada	
Wei-Guo Zhang	

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, the proposed amendments to IFRIC 14.

BC1 This Basis for Conclusions summarises the International Accounting Standards Board's considerations in proposing amendments to IFRIC 14 *IAS 19—The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*. Individual Board members gave greater weight to some factors than to others.

BC2 The Board noted that the requirements of IFRIC 14 for the treatment of prepayments produced unintended consequences in some circumstances. IFRIC 14 is effective for annual periods beginning on or after 1 January 2008. Accordingly, the Board intends to finalise the amendments as soon as possible so that the unintended consequences are eliminated as soon as possible.

BC3 IFRIC 14 states that the surplus in the plan created by the prepayment is not regarded as available as an economic benefit if the future minimum funding contribution required in respect of future service exceeds the future IAS 19 service cost. Therefore, in such cases the prepayment is recognised as an expense.

BC4 In the Board's view, an entity that has made a prepayment expects to obtain future economic benefits from that prepayment in the form of reduced cash outflows in future years in which payments would otherwise have been required. Those cash outflows relate to both future service cost and future minimum funding requirement (MFR) contributions. Accordingly, the entity has an asset.

BC5 The Board further noted that recognising an asset for a prepayment of future MFR contributions would convey decision-useful information to users of financial statements because an entity that has such an asset is in a more economically favourable position than one that does not.

BC6 The Board noted that a prepayment would reduce future contributions that cover:

(a) future service cost; and

(b) future excess of MFR contributions over service cost.

BC7 Some argue that the economic benefit accruing to the entity arises only for reductions in future service cost. They argue that there is no benefit to the entity for the prepayment of future excess of MFR contributions over service cost and thus that such an amount should be recognised as an expense.

BC8 The Board rejected this view. In the Board's view, the future excess of MFR contributions over service cost does give an economic benefit to the entity because it relieves the entity of an obligation that it would otherwise incur in the future. Accordingly, the Board proposes that that amount should be recognised as an asset, not as an expense.

BC9 Accordingly, the Board decided to amend IFRIC 14 to require an entity to recognise an asset for a prepayment that will reduce future MFR contributions by the entity.

Transition

BC10 Paragraph BC39 of the Basis for Conclusions on IFRIC 14 states:

> ... paragraph 58A of IAS 19 causes the limit on the defined benefit asset to affect the deferred recognition of actuarial gains and losses. Retrospective application of the Interpretation could change the amount of that limit for previous periods, thereby also changing the deferred recognition of actuarial gains and losses. Calculating these revised amounts retrospectively over the life of the plan would be costly and of little benefit to users of financial statements.

BC11 The Board concluded the same arguments also apply to the proposed amendments. Accordingly, the Board proposes that entities should apply the proposed amendments from the beginning of the first period presented in the financial statements in which the entity applied the original version of IFRIC 14. In the Board's view, this would remove the unintended consequence arising from the treatment of prepayments in the financial statements of those entities for previous years, and should not be unduly onerous given the short time that the Board intends will elapse between the issue of IFRIC 14 and the issue of the amendments.

Exposure period

BC12 Although these amendments are proposed by the Board, they relate to an IFRIC Interpretation. Accordingly, the Board decided on an exposure period of 60 days, the usual period for draft IFRIC Interpretations. The Board believes that an exposure period shorter than the Board's normal 120 days is justified because this matter is urgent, the document is short, and the Board believes from discussions in the IFRIC and with the Board's Employee Benefits Working Group that there is likely to be a broad consensus on the issue.

