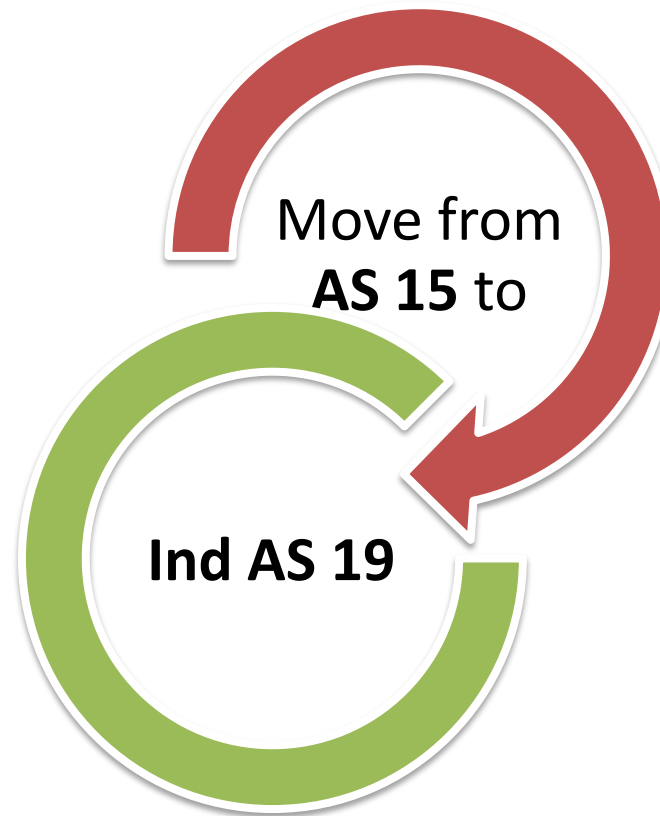




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Change in Employee Benefits Accounting

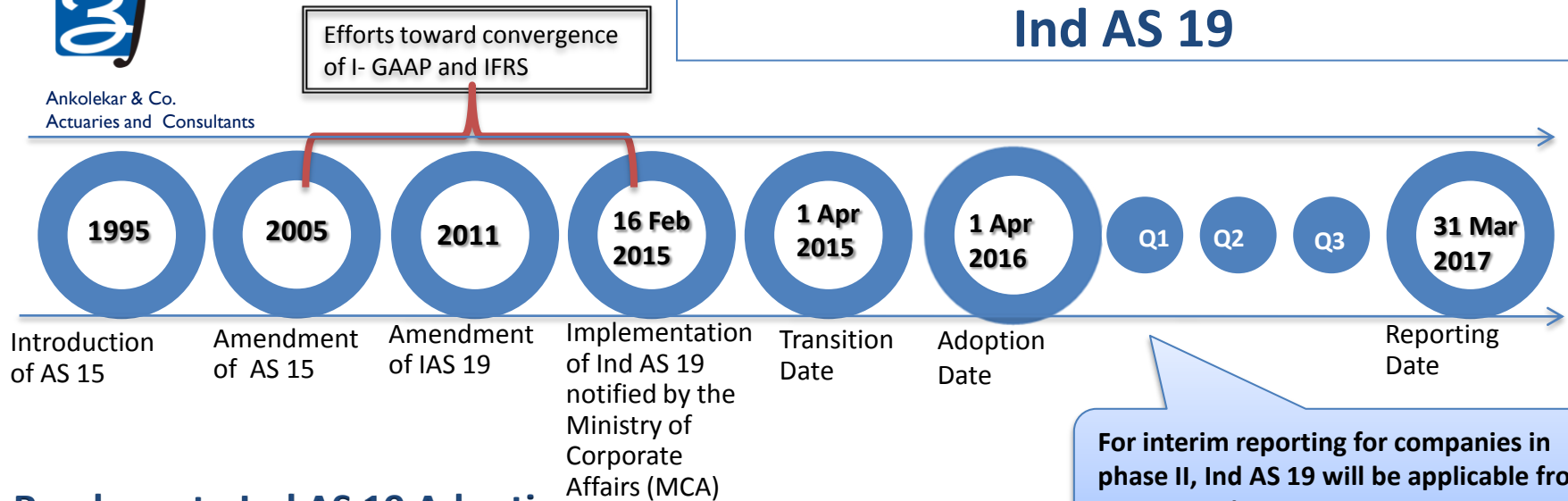
Planning the transition





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Transition timeline from AS 15 to Ind AS 19



Roadmap to Ind AS 19 Adoption

For interim reporting for companies in phase II, Ind AS 19 will be applicable from quarter ending June 30, 2016.

1 April 2015

PHASE I

Voluntary adoption from FY 15-16 by any company (excluding Insurance companies, Banks and NBFCs as they are exempted from the application of this accounting standard).

1 April 2016

PHASE II

Mandatory compliance from FY 16-17 for all entities with a net worth equal to or in excess of Rs 500 crore.

1 April 2017

PHASE III

Mandatory compliance from FY 17-18 for the remaining listed entities and unlisted entities with a net worth between Rs 250 crore and Rs 500 crore.

Valuation method has not changed



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What has changed under Ind AS 19?

1. Recognition of Actuarial Gains and Losses

Under AS 15,
immediate
recognition in P&L



Under Ind AS 19,
Immediate
recognition in Other
Comprehensive
income (OCI).

Corridor approach is
not recognised.

IMPACT

Lesser volatility in the P&L due to actuarial gain/ loss from

- i. Impact of changes in assumptions and;
 - ii. Experience being different from assumptions
- being routed through OCI**

Image: <http://www.creativeedgemag.com/assets/content/old-vs-new-300x225.jpg>



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What has changed under Ind AS 19? ...contd.

2. Financing Cost: Expected Return On Assets (EROA) = Discount Rate

Under AS 15, the P&L includes the interest cost on plan liabilities and the actual return on Plan assets,

Where actual return =
 $\text{EROA} + \text{Actuarial Gain/(Loss)}$

EROA need not equal the discount rate



Under Ind AS 19, the EROA equals the discount rate, and the net interest cost is calculated by multiplying the discount rate to the net defined benefit liability at the start of the year.

Thus, Interest Cost and EROA is replaced by the Interest Cost on net DBO.

IMPACT

1. **Asset return greater or lesser than the discount rate will be recognised as actuarial gain/ loss in OCI.**
2. **Categorization of excess/ lower asset returns to OCI means that investing in more volatile assets would not affect P&L immediately.**



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What has changed under Ind AS 19? ...contd.

3. Impact of change in Asset Ceiling

Under AS 15, the P&L includes the impact from applying the asset ceiling



Under Ind AS 19, the impact from applying the asset ceiling would be routed through OCI



Lesser P&L volatility as a result of routing of asset ceiling impact through the OCI



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What has changed under Ind AS 19? ...contd.

Consider two examples

Liability = 10000, Asset = 8000, disc rate = 6% pa, EROA = 7.5% pa

Scenario 1: Actuarial gain of 40, actual asset return @8%

THEN		NOW	
Interest Cost (6%*10000)	600	Net Interest Cost (6%*2000) .. P&L	120
EROA (7.5% * 8000)	(600)		
Actuarial gain	(40)	Actuarial Gain (2% of 8000) ... OCI	(160)
Net expense/(income)	(40)	Total charge recognised	(40)

Under Ind AS 19, the employer expense is more since the actuarial gain on assets of Rs 160 i.e. 2% of 8,000 will now be transferred to OCI

Scenario 2: Actuarial loss of 200, actual asset return @5%

THEN		NOW	
Interest Cost (6%*10000)	600	Net Interest Cost (6%*2000) .. P&L	120
EROA (7.5% * 8000)	(600)		
Actuarial loss	200	Actuarial Loss (1% of 8000) ... OCI	80
Net expense/(income)	200	Total charge recognised	200

Under Ind AS 19, employer expense is less since the actuarial loss on assets of Rs 80 i.e. 1% of 8,000 will now be transferred to OCI

The actuarial gain/ loss is excluded from the P&L, this change will remove the extra volatility that enters the P&L through actuarial gain/ loss



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What has changed under Ind AS 19? ...contd.

4. Reading Disclosures- AS 15 Vs. Ind AS 19

Under AS 15

Previous year Discount rate=8% pa
EROA=12.5% pa

DBO	Year ended 20XX
Present Value of DBO at start of period	100
Current Service Cost	20
Past Service Cost	10
Interest Cost	8
Benefits Paid	(25)
Actuarial Loss/(Gain)	(8)
Present Value of DBO at end of period	105

Employer Expense for the year	Year ended 20XX
Current Service Cost	20
Interest Cost	8
Past Service Cost	10
Expected Return on Plan Assets	(10)
Actuarial Loss/(Gain)	(6)
Employer Expense	22

Amounts in Rs'000

Fair Value of Assets	Year ended 20XX
Fair Value at start of period	80
Contributions By Employer	40
Benefits Paid	(25)
Expected Return on Plan Assets	10
Actuarial (Loss)/Gain	(2)
Fair Value at end of period	103

Movement	Year ended 20XX
Opening Net Liability (100 – 80)	20
Add: Employer Expense	22
Less: Employer Contribution	(40)
Closing Net Liability (105 - 103)	2



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What has changed under Ind AS 19? ...contd.

4. Reading Disclosures- AS 15 Vs. Ind AS 19..contd

Amounts in Rs'000

Under Ind AS 19

Previous year Discount rate=8% pa
EROA=8% pa

DBO	Year ended 20XX
Present Value of DBO at start of period	100
Current Service Cost	20
Past Service Cost	10
Interest Cost	8
Benefits Paid	(25)
Actuarial Loss/(Gain)	(8)
Present Value of DBO at end of period	105

Employer Expense	Year ended 20XX
Current Service Cost	20
Interest Cost on net DBO	2
Past Service Cost	10
Employer Expense (P&L)	32

Fair Value of Assets	Year ended 20XX
Fair Value at start of period	80
Contributions by Employer	40
Benefits Paid	(25)
Interest Income	6
Returns above Interest Income	2
Fair Value at end of period	103

Re-measurements	Year ended 20XX
Actuarial Loss/(Gain) on DBO	(8)
Returns above Interest Income	(2)
Total Re-measurements (OCI)	(10)

Movement	Year ended 20XX
Opening Net Liability (100 – 80)	20
Add: Employer Expense	32
Less: Transfer to OCI	(10)
Less: Employer Contribution	(40)
Closing Net Liability (105 -103)	2



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What has changed under Ind AS 19? ...contd.

5. The changed position

Amounts in Rs'000

AS 15

Movement	Year ended 20XX
Opening Net Liability (100 – 80)	20
Add: Employer Expense	22
Less: Employer Contribution	(40)
Closing Net Liability (105 - 103)	2

Ind AS 19

Movement	Year ended 20XX
Opening Net Liability (100 – 80)	20
Add: Employer Expense	32
Less: Transfer to OCI	(10)
Less: Employer Contribution	(40)
Closing Net Liability (105 - 103)	2



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What has changed under Ind AS 19? ...Contd.

6. Past Service Cost

Under AS 15, Past Service Cost recognized in the P&L **over the period of vesting.**



Under Ind AS 19, Past Service Cost is recognized **immediately** in the P&L.

IMPACT

P&L will be more volatile. However, the event is likely to be a one-off, e.g. scaling up the benefit formula or enhancing the benefit ceiling.



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What has changed under Ind AS 19? ...contd.

7. Additional Disclosures

Under AS 15, such disclosures are currently not required



Under Ind AS 19, disclosures are needed for:

- a) Asset Liability Matching Strategies
- b) Sensitivity Analysis of significant actuarial assumptions.
- c) Information of Future Cash Flows which includes description of funding arrangements, maturity profile of DBO.

IMPACT

1. Increase in transparency and a superior evaluation of ALM risks.
2. Depiction of the criticality of each valuation assumption and its ultimate impact on the obligation.
3. Enable stakeholders to understand the composition of assets, including whether self- managed or insurer-managed.
4. The weighted average duration will indicate the maturity of the plan which could be used to gauge the consistency with the ALM strategy.



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What has changed under Ind AS 19? ...contd.

8. Experience analysis

Under AS 15, five years' comparative tables for experience analysis for both liabilities and assets are disclosed.



Under Ind AS 19, the breakdown of actuarial gains/ losses by:

- a) assumption change, and
- b) experience

needs to be disclosed for the current and the previous year only.

IMPACT

Experience analysis provides insights to assumption setting.

Management, auditors and actuaries would need to rely on past reports to refine the assumption setting process.



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Managing the transition efficiently

For companies to whom Ind AS applies from FY 2016-17

No voluntary adoption as that would imply drawing out disclosures as per Ind AS 19 for March 2015 as well

Recommended practise: Receive both formats viz. AS 15 and Ind AS 19 for the March 2016 valuation

Use the AS 15 numbers for accounting and retain the Ind AS 19 numbers for next year's disclosures



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FAQs



Q1. Having voluntarily or mandatorily complied with the standard, if the threshold criteria do not apply subsequently, will Ind AS 19 continue to be applicable?

Yes. Once complied with, continued compliance is mandatory for all subsequent financial statements.

Q2. Has the method of measurement of obligation changed?

No.

Q3. Which period's financials should be used for checking applicability to Ind AS 19?

The net worth will be determined based on the standalone accounts of the company as on 31 March 2014 or the first audited period ending after that date.

Q4. What if the company is a Small and Medium Sized Enterprise (SME)?

SMEs are not required to comply with the new standard, unless voluntarily chosen.



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FAQs ... contd.

Q5. If a company is required to adopt Ind AS 19 from 1 April 2016, then how does this affect the company's reporting for financial year 2015-16?

Companies with applicability date 1 April 2016 may consider using both formats for March 31, 2016 valuation. For the reporting date on applicability of Ind AS 19, i.e. March 31, 2017 previous year's comparative figures are required to be disclosed.

Q6. Will actuarial gains or losses flow into Other Comprehensive Income (OCI) even for privilege and sick leave?

In our opinion: "No." Compensated absences viz. privilege leave and sick leave are classified as other long term employee benefits (Other LT EB) and not Post-Retirement Benefits. Note that leave can be availed in employment although cashed only on leaving service.



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FAQs ... contd.

Q7. How would an existing asset ceiling be treated under the new standard?

The opening net asset will be the same as per AS 15. However, any future changes in the asset ceiling as each valuation date will not be charged to P&L, but will be routed through the OCI.

Q8. A company's financial statements prior to the transition to Ind AS 19 contained items that now need a change of treatment viz. unamortized past service cost, limit due to asset ceiling, and actuarial gains and losses. Would the accounting treatment for these items need to be revisited?

For the previous financial statements before the date of transition to Ind AS 19, in our opinion, no changes are necessary. Unamortized past service cost arising from improvement in benefits before the transition to Ind AS 19 would however continue to be amortized till it is fully written off.



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FAQs ... contd.

Q9. How many periods experience adjustment needs to be disclosed?

Under Ind AS 19, the experience adjustment pertaining to the current year and previous year needs to be disclosed.

Q10. Is Ind AS 19 applicable for ESOP valuations as well?

No. ESOPs fall within the purview of accounting standard Ind AS 102.

Q11. What is the major difference in accounting for share-based payments and ESOP costs?

Till now in India, the ICAI Guidance Note 18 was used for ESOP accounting which permitted 'Intrinsic Value' accounting with disclosure of 'Fair Value' impact. However now after the adoption of Ind AS 102, companies would need to use 'Fair Value' for ESOP accounting.





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DISCLAIMER

This document has been prepared for the purpose of explaining the position with regard to transition to the Ind AS 19 Accounting Standard. Its transmittal is not intended to constitute advice, but should be seen as a viewpoint that enhances comprehension and education. The management is responsible for the preparation of its financial statements. This document does not supersede the need for the management's consulting with its advisors to implement the transition.