17 ACCOUNTING STANDARD 15 "EMPLOYEE BENEFITS"

4*

Quote:

THE MIND IS NOT A VESSEL TO BE FILLED BUT A FIRE TO BE IGNITED

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SECTION A – CONCEPT

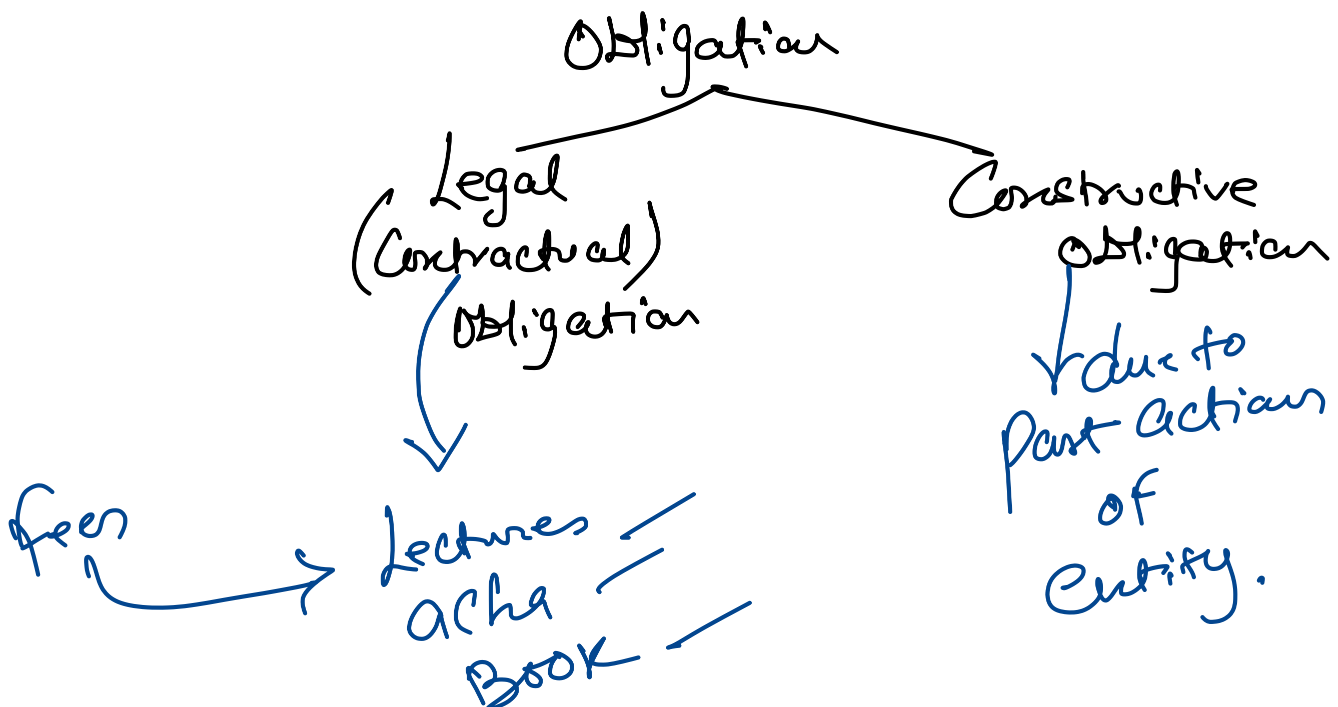
1. APPLICABILITY

- *This Standard should be applied by an employer in accounting for all employee benefits, **except employee share-based payments**.* (ESOP)
- *The Standard applies in its entirety for **all Level I enterprises**. Certain exemptions are given to other than Level I enterprises, depending upon whether they employ 50 or more employees.*

2. EMPLOYEE BENEFITS INCLUDEs

(a) *formal plans or other formal agreements between an enterprise and employees;*
(b) *under legislative requirements or through industry arrangements where entities are required to contribute to the National, State or Industry plans; OR* PF, ESI
(c) *By those **informal practices** that give rise to a **Constructive obligation**.*

CONSTRUCTIVE OBLIGATION:
An Obligation to pay that arises out of entity's actions rather than a contract. It may typically occur from past conduct.



3. TYPES OF EMPLOYEE BENEFITS

(a) SHORT-TERM EMPLOYEE BENEFITS, which are expected to be settled wholly before Twelve Months after the end of reporting period, such as wages, salaries and social security contributions (e.g., contribution to an insurance company by an employer to pay for medical care of its employees), paid annual leave, profit-sharing and bonuses (if payable within twelve months non-monetary benefits (such as medical care, housing, cars and free or subsidized goods or services) for current employees;

(b) POST-EMPLOYMENT BENEFITS, which are payable after the completion of employment such as gratuity, pension, 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, long-term disability benefits and, profit-sharing bonuses and deferred compensation; and

(d) TERMINATION BENEFITS are employee benefits provided in exchange for the termination of an employee's employment as a result of either:

(a) an entity's decision to terminate an employee's employment before the normal retirement date; or

(b) An employee's decision to accept an offer of benefits in exchange for the termination of employment. (VRS)

Employee benefits include benefits provided to either employees or their dependents or beneficiaries:

> *Note*: An employee may provide services on a full-time, part-time, permanent, casual or temporary basis. Employees include whole-time directors and other management personnel.

4. POST-EMPLOYMENT BENEFITS & OTHER LONG TERM EMPLOYEE BENEFITS

Same Treatment

4.1 DIFFERENCE BETWEEN DEFINED BENEFIT PLANS AND DEFINED CONTRIBUTION PLANS

Imp Theory

Defined Contribution Plans (DCP)	Basis of Difference	Defined Benefit Plans (DBP)
Entity 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 benefits	Meaning	No fixed Contribution. Post-employment benefit plans other than defined contribution plans. Entity may liable for additional Contri:
Obligation is limited to the amount that it agrees to contribute.	Employers' Obligation (Amount Payable)	Obligation is to provide agreed benefits to current and former employees. (Obligation is not limited)
No Change in the contribution made except some extreme conditions	Change in the obligation	If actuarial or investment experience are worse than expected, the entity's obligation may be increased for providing to the employees.
Risk in substance on the Employee	Actuarial Risk (Benefits will be more/less than expected)	Risk in substance on the entity.
Risk in substance on the Employee.	Investment Risk	Risk in substance on the entity.
Provident Fund Contribution by employer	Examples	Gratuity
Not Required	Actuarial Assumptions	Required
Not Required except where the obligation falls due after twelve months after the end of the annual reporting period in which the employees render the related service.	Discounting	Always Required

4.2 ACCOUNTING FOR DEFINED BENEFIT PLANS (DBP)

Summary:

1. Calculate Current Service Cost (CSC) using actuarial assumptions under "Projected unit credit method". CSC means the amount of expense to be recognised every year against the services performed by the employees. CSC is always calculated by discounting technique, since the service has been performed but the amount to be paid in future. It is shown under Employee Benefit Expense in Profit and Loss A/c.
2. Calculate Interest on defined benefit liability using same discounting rate used in CSC. It is show under Finance Cost in Profit and Loss A/c

3. CSC and Interest on defined benefit Liability is charged to Profit & Loss A/c and corresponding liability is credited in the name of **PV of defined benefit Liability or defined benefit obligation.** (LT Provision)
4. Determine the **Fair Value of Plan Assets** (Investments made)
5. We have to present Net defined benefit liability (asset) by deducting Fair Value of Plan Assets from PV of defined benefit liability.
6. If it is deficit then – Net defined benefit liability, if it is surplus then net defined benefit asset.
7. **Asset is to be show at lower of:**
   (a) *The surplus in the defined benefit plan; and*
   (b) the present value of any economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

   Pending

   (Difference is charged to Profit and Loss Account)

8. Re-measure the liability, if there is change in estimates and actuarial assumptions, any change is known as Actuarial Gain or Loss and **transfer to Profit and Loss A/c.**

9. **How to Calculate Expected Return?** On Plan Asset
   First of all we have to check whether separate Rate (%) is given for calculation of expected return, if not given then we shall take same discount rate which is used to calculate the Interest on Defined benefit obligation.
   Now, next issue is on which value such Rate (%) should be applied to calculate the expected return? For this we have to check the question's information and follow below guidance:
   a. If Contributions made to Plan Assets and Benefits paid **at the end of the year** then apply the Rate (%) on Opening Balance of Plan Assets. (Class Ex:- 4 Notes)
   b. If Contributions made to Plan Assets & Benefits paid **in the beginning of the year** then apply the Rate (%) on (Opening Balance + Contributions Made – Benefits Paid). (Class Ex:-3 Notes)
   c. If Contributions made to Plan Assets & Benefits paid **in the mid of the year** then follow the below steps: (Class Ex. 5 Notes)
      - First calculate the Return on Opening Balance with the given annual rate (%)
      - Now, calculate Six Monthly Compounded Rate of Expected Return as under:

        $$[\sqrt{1 + annaul\ rate} - 1] \times 100$$

      - Calculate the Return on Net Contibution (contribution made to Plan Asset less Benefits Paid out of Plant Assets) by applying the above six monthly compounded rate.

10. At every BS date, re-measure the Plan assets at Fair Value. Any change on re-measurement is called Actuarial loss or gain and **transfer to Profit and Loss A/c.** **(Fair Value of Plan Assets will be given in the Question)**

11. **Items to be shown in Profit and Loss A/c:**
    i. Current service cost under Employee benefit expenses.
    ii. Interest Cost;
    iii. Expected Return on Plan Assets; (Income)

iv. Actuarial gains and losses on defined benefit Liability and Plan Assets due to change in actuarial assumptions.
v. any Past service cost (to the extent they are recognized); Emp Benf. Exp.
vi. and gain or loss on settlement (curtailment);
vii. Any change in the effect of the Net Defined Benefit Asset.

12. Items to be shown in Balance sheet:
Net defined liability (deficit) or Net defined asset (Surplus)

13. Actuarial Assumptions comprise -
i. Demographic assumptions such as mortality, employee turnover rate, disability, early retirement, claims rates under medical plans and;
ii. Financial assumptions such as discount rate, future salary, expected rate of return on plan assets.

Example: (on Define Benefit Obligation)

A lump sum gratuity, equal to 1% of final salary for each year of service, is payable on termination of service. The salary in year 1 is Rs. 10,000 and is assumed to increase at 7% (compound) each year resulting in Rs. 13,100 at the end of year 5. The discount rate used is 10% per annum. 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.

SOLUTION: (Amount in Rs.)

Computation of benefits attributed to the current and prior years:

Year	1	2	3	4	5
Benefit attributed to:					
- Prior year	0	131	262	393	524
- Current year (1% of final salary)	131	131	131	131	131
- Current and prior years	131	262	393	524	655

Computation of obligation for an employee:

Year	1	2	3	4	5
Opening Obligation	-	89	196	324	476
Interest at 10%	-	9	20	33	48
Current service cost (see note 2)	89	98	108	119	131
Closing Obligation (see note 1)	89	196	324	476	655

Note 1

Closing obligation

Year	1	2	3	4	5
Gratuity attributable	131	262	393	524	655
Payable after (years)	4	3	2	1	0
Discounting factor	.683	.751	.826	.909	1
PV	89	196	324	476	655

Note 2

Current Service Cost

Year	1	2	3	4	5
Gratuity of current year	131	131	131	131	131
Payable after (years)	4	3	2	1	0

Discounting factor	.683	.751	.826	.909	1
PV	89	98	108	119	131

Example: 2

On 1.4.20X1, the fair value of plan assets is Rs.10,000. On 30.9.20X1 it paid benefits of Rs. 1,500 and received contributions of Rs. 4,500. On 31.03.20X2, fair value of plan assets is Rs.15,000 and PV of obligation was Rs. 14,972. Actuarial losses on obligation was Rs. 60 on 31.03.20X2. Find the net actuarial gain/losses on 31.03.20X2 based on the following estimates:

Interest and dividend income	9.00%
Realised and unrealized gain on plan assets	1.50%
Administration costs	(1.00%)

Annual Ex. Return = 9.50%

Six monthly Rate = $\left(\sqrt{1+0.095} - 1\right) \times 100 = 4.64\%$

Plan Asset A/c

1/4 To Bal.	10000	30/9 By Bank	1500
30/9 To Bank	4500		
31/3 To Ex. Return			
10000 × 9.5%	950		
3000 × 4.64%	139		
31/3 To Act. gain	911	31/3 By Bal.	15000

4.3 PAST SERVICE COST (PSC)

modification

Meaning of PSC - Change in the present value of the defined benefit obligation resulting from a plan amendment is known as past service cost (PSC).

- PSC is divided into two parts:
  - (a) Amortised Past service cost - which is to be recognized immediately to the extent benefits are already vested. (P&L)
  - (b) Unamortised Past Service cost – to be recognized on straight line basis over the remaining period until the benefits are vested. (thora thora P&L me Jayega)

- Example of Past Service Costs: due to the recent amendments in Gratuity Act, 1972 there is substantial increase in the gratuity liability of the company (i.e. from 10 lacs to 20 lacs). Such increase in liability would be regarded as Past Service Cost.

Example: 3

An enterprise operates a pension plan that provides a pension of 2% on final salary for each year of service. The benefit will be vested after 5 years of service. On 1.1.2005, the enterprise improves the pension to 2.5% of the final salary for each year of service starting from 1.1.2001 at the date of improvement the Present Value of additional benefits for service from 1.1 .2001 to as follows:

- Employees with more than 5 years of service at 1.1.2005 — Rs. 2,00,000 Vested
- Employees with less than 5 years of service (Average period until vesting = 3 years) — Rs. 1,20,000

Suggest the accounting treatment

120000 / 3 = 40000 P&L every year

Solution:-

1) Amortised PSC means additional Benefits payable to employees with more than 5 years of service = 200000

It is to be Immediately Recog. in P&L

2) Un-amortised PSC means additional Benefits Payable to employees with less than 5 years i.e Unvested Benefits. = Rs 120000

It is to recognised in next 3 years.

1/1/05 Amort. PSC 2
Unam. PSC 1.2
To DBO Payable 3.20

1/1/05 P&L 2
To Amort PSC

4.4 CURTAILMENT AND SETTLEMENT

- Curtailment or Settlement is a transaction that **eliminates all further legal or constructive obligations for part or all of the benefits provided under defined benefit plan.**
- In a simple language, if Defined Benefit Obligation plan is modified in such a way that **employees will not get benefit,** rather benefit originally planned is being reduced, it is called curtailment.
- However, settlement amount may have to be given by entity as a compensation against curtailment of benefits.
- An enterprise should recognize gains or losses on the curtailment when the curtailment occurs.

Journal Entry:

Defined benefit Liability A/c Dr. (Curtailment Amt.)

To un-amortised past service cost a/c
To Bank A/c (Settlement)
To Gain on Curtailment A/c (Balancing Fig)

- **Gain on curtailment** shall be transfer to Statement of **P&L under Employee Benefit Expense.**

Example: 4

An enterprise discontinues a business segment and the employees of this segment will earn no further benefits. This is curtailment without a settlement. Immediately before the curtailment the details were.

	Before Curtailment	After Curtailment
PV of obligation	1,000	900
FV of plan assets	820	820
Unrecognized past service cost	50	45

The curtailment reduces the obligation to Rs. 900 and URPSC to Rs.45. Suggest the accounting treatment.

DBO Payable Dr. 100
To Un-am.PSC 5
To Gain on Curt 95 (P&L)

5. SHORT-TERM EMPLOYEE BENEFITS

(NO ACTURIAL ASSUMPTION)

(i) Accounting for short-term employee benefits is generally straight forward short-term employee benefit obligations **are measured on an undiscounted basis.**

(ii) It involves no actuarial assumptions to be made, hence there is no accounting required for any actuarial gain/loss.

(iii) Short-term employee benefits are broadly classified into four categories:

- **(a)** regular period benefits (e.g., wages, salaries);
- **(b)** short-term compensated absences (e.g., paid annual leave, maternity leave, sick leave etc.);
- **(c)** profit sharing and bonuses payable within twelve months after the end of the period in which employee render the related services and
- **(d)** non-monetary benefits (e.g., medical care, housing, cars etc.)

5.1 SHORT-TERM COMPENSATED ABSENCES

An employer normally compensates an employee on account of his absence either by granting privilege leave (vacation leave), or sick leave, or maternity or paternity leave etc. These compensated balances fall under two categories and recognize the expected cost in the form of paid absences as follows:

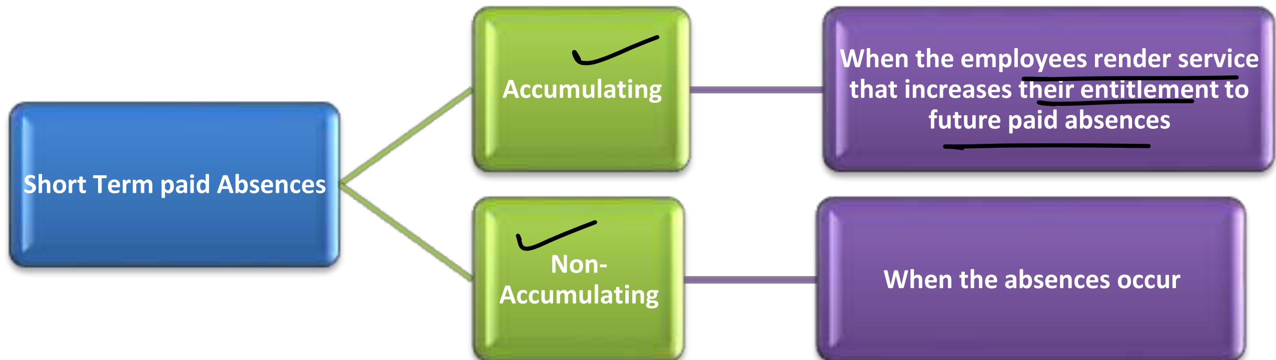
(1) Accumulating paid absences -

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.

(2) Non-accumulating paid absences -

Non-accumulating compensated absences (e.g., maternity leave) do not carry forward and are not directly linked to the services rendered by employees in the past. Therefore, an enterprise recognizes no liability or expense until the time of the absence.

In other words, the cost of non-accumulating absences should be recognized as and when they arise.



Treatment of Accumulating Paid Absences:

These are the absences that are carried forward and can be used in future periods if the employee is not able to use them in current reporting period of the employer. They can be either:

(i) **Vesting:** In this case, employees are entitled to a cash-payment for the unutilised entitlement at the time of leaving the entity.

(ii) **Non-vesting:** In this case, employees are not entitled to a cash payment for unused entitlement on leaving.

Measurement: An entity shall measure the expected cost of accumulating compensated absences as the additional amount that the entity expects to pay as a result of the unused entitlement that has accumulated at the end of the reporting period.

> **Example:**
> An enterprise has 100 employees, who are each entitled to five working days of leave for each year. Unused leave may be carried forward for one calendar year. The 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 20X4, 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 leave in 20X5 and that the remaining eight employees will take an average of six and a half days each.
> How much is the expected liability due to leaves?
> **Ans.:** The enterprise expects that it will pay an additional 12 days of pay as a result of the unused entitlement that has accumulated at 31 December 20X4 (one and a half days each, for eight employees). Therefore, the enterprise recognises a liability, as at 31 December 20X4, equal to 12 days of pay.

1.5 × 8 = 12

1 × 2 = 2
100 × 2 = 200

5.2 PROFIT-SHARING AND BONUS PLANS

An enterprise should recognise cost of profit-sharing and bonus payments 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.

Therefore, an entity recognises the cost of profit-sharing and bonus plans not as a distribution of profit but as an expense.

> **Example**
> 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.

6. TERMINATION BENEFITS

1) Termination Benefits are employee benefits payable as a result of either an enterprise's decision to terminate an employee's employment before the normal retirement date (OR) an employee's decision to accept voluntary redundancy in exchange for those benefits (e.g., payments under VRS).

2) Termination benefits are recognized by an enterprise as a liability and an expense only when the enterprise has
   a) a detailed formal plan for the termination which is duly approved, and
   b) a reliable estimate can be made of the amount of the obligation.

3) Where the termination benefits fall due within twelve months after the balance sheet date, an undiscounted amount of such benefits should be recognized as liability in the balance sheet with a corresponding charge to Profit & Loss Account.

4) However, when the termination benefits fall due more than twelve months after the balance sheet date, such benefits should be discounted using an appropriate discount rate.

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

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

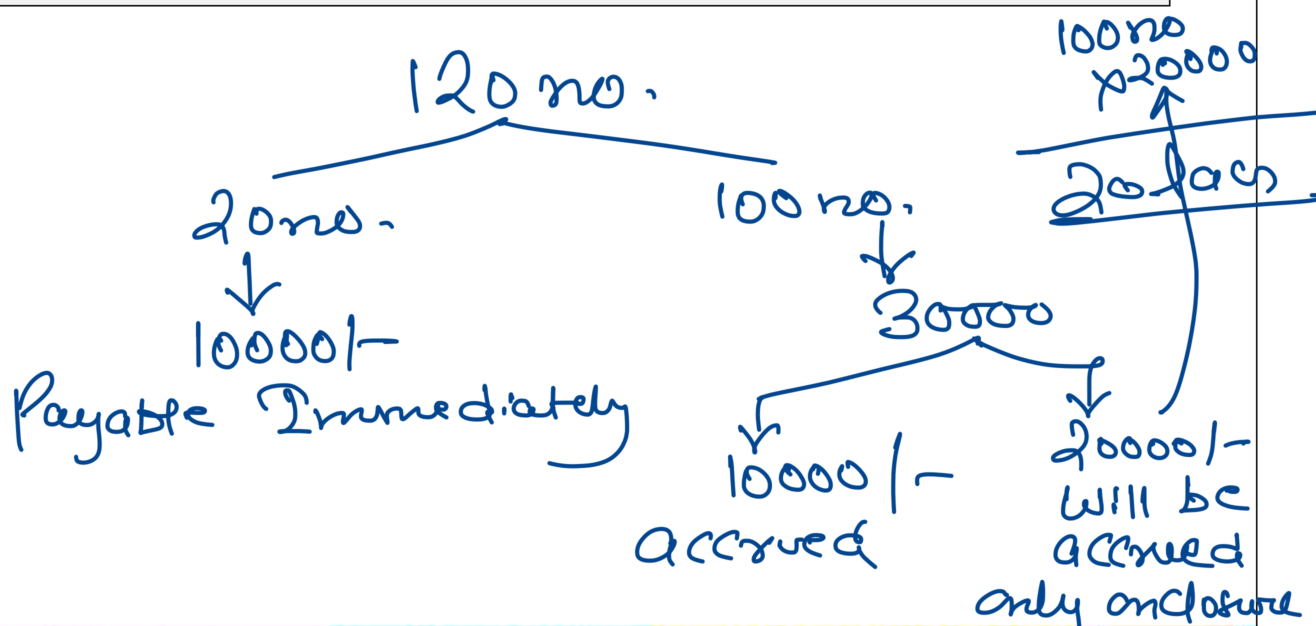
There are 120 employees at the factory. At the time of announcing the plan, the entity expects 20 of them to leave before closure. Therefore, the total expected cash outflows under the plan are Rs. 3,200,000 (ie 20 × Rs10,000 + 100 × Rs 30,000). As required by paragraph 160, the entity accounts for benefits provided in exchange for termination of employment as termination benefits and accounts for benefits provided in exchange for services as short-term employee benefits.

Termination benefits

The benefit provided in exchange for termination of employment is Rs 10,000. This is the amount that an entity would have to pay for terminating the employment regardless of whether the employees stay and render service until closure of the factory, or they leave before closure. Even though the employees can leave before closure, the termination of all employees' employment is a result of the entity's decision to close the factory and terminate their employment (ie all employees will leave employment when the factory closes). Therefore, the entity recognises a liability of Rs 1,200,000 (ie 120 × Rs10,000) for the termination benefits provided in accordance with the employee benefit plan at the earlier of when the plan of termination is announced and when the entity recognises the restructuring costs associated with the closure of the factory.

Benefits provided in exchange for service.

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



SECTION B - QUESTIONS

(Questions of Study Material, RTPs, MTPs and Past Exams to be Practiced in the Class)

Series 100

LONG TERM AND POST EMPLOYEMENT BENEFITS

Q.AS15.SM.101 (Defined Benefit Obligation) Exam

An employee Roshan has joined a company XYZ Ltd. in the year 20X1. The annual emoluments of Roshan as decided is ₹14,90,210. The company also has a policy of giving a lump sum payment of 25% of the last drawn annual salary of the employee for each completed year of service if the employee retires after completing minimum 5 years of service. The salary of the Roshan is expected to grow @ 10% per annum. The company has inducted Roshan in the beginning of the year and it is expected that he will complete the minimum five year term before retiring. Thus he will get 5 yearly increment.

What is the amount the company should charge in its Profit and Loss account every year as cost for the Defined Benefit obligation? Also calculate the current service cost and the interest cost to be charged per year assuming a discount rate of 8%.

(P.V factor for 8% - 0.735, 0.794, 0.857, 0.926, 1)

Solution

Calculation of Defined Benefit Obligation (DBO)

Expected last drawn salary	₹ 14,90,210 x 110% x 110% x 110% x 110% x 110%	**₹24,00,000**
Defined Benefit Obligation (DBO)	₹ 24,00,000 x 25% x 5	**₹30,00,000**

Amount of ₹ 6,00,000 will be charged to Profit and Loss Account of the company every year as cost for Defined Benefit Obligation.

Calculation of Current Service Cost

Year	Equal apportioned amount of DBO [i.e. ₹ 30,00,000/5 years]	Discounting @ 8% PV factor	Current service cost (Present Value)
a	b	c	d = bx c
1	6,00,000	0.735 (4 Years)	4,41,000
2	6,00,000	0.794 (3 Years)	4,76,400
3	6,00,000	0.857 (2 Years)	5,14,200
4	6,00,000	0.926 (1 Year)	5,55,600
5	6,00,000	1 (0 Year)	6,00,000

Calculation of Interest Cost to be charged per year

	Opening balance	Interest cost	Current service cost	Closing balance
a	b	C =b×8%	d	e = b + c + d
1	0	0	4,41,000	4,41,000
2	4,41,000	35,280	4,76,400	9,52,680,

3	9,52,680	76,214	5,14,200	15,43,094
4	15,43,094	1,23,447	5,55,600	22,22141
5	22,22,141	1,77,859*	6,00,000	30,00,000

*Due to approximations used in calculation, this figure is adjusted accordingly

Q.AS15.SM.102 (Actuarial Gains/Losses)

Omega Limited belongs to the engineering industry. The company received an actuarial valuation for the first time for its pension scheme which revealed a surplus of ₹6 lakhs. It wants to spread the same over the next 2 years by reducing the annual contribution to ₹2 lakhs instead of ₹5 lakhs. The average remaining life of the employees is estimated to be 6 years. You are required to advise the company on the following items from the viewpoint of finalization of accounts, taking note of the mandatory accounting standards.

Solution

According to AS 15 (Revised 2005) 'Employee Benefits', actuarial gains and losses should be recognized immediately in the statement of profit and loss as income or expense. Therefore, surplus amount of ₹6 lakhs is required to be credited to the profit and loss statement of the current year.

Q.AS15.SM.103 (Plan Assets and Return on Plan Assets)

The following data apply to 'X' Ltd. defined benefit pension plan for the year ended 31.03.20X2 calculate the actual return on plan assets:

Benefits paid	**2,00,000**
Employer contribution	2,80,000
Fair market value of plan assets on 31.03.20X2	11,40,000
Fair market value of plan assets as on 31.03.20X1	8,00,000

SOLUTION

	₹
Fair value of plan assets on 31.3.20X1 (Opening Bal.)	8,00,000
Add: Employer contribution	2,80,000
Less: Benefits Paid	(2,00,000)
(A)	**8,80,000**
Fair market value of plan assets at 31.3.20X2 (B)	11,40,000
Actual return on plan assets (B-A)	2,60,000

Q.AS15.SM.104 (Plan Assets and Return on Plan Assets)

As on 1st April, 20X1 the fair value of plan assets was ₹1,00,000 in respect of a pension plan of Zeleous Ltd. On 30th September, 20X1 the plan paid out benefits of ₹19,000 and received inward contributions of ₹49,000. On 31st March, 20X2 the fair value of plan assets was ₹1,50,000 and present value of the defined benefit obligation was ₹1,47,920. Actuarial losses on the obligations for the year 20X1- 20X2 were ₹600. On 1st April, 20X1, the company made the following estimates, based on its market studies, understanding and prevailing prices

	%
Interest & dividend income, after tax payable by the fund	9.25
Realised and unrealised gains on plan assets (after tax)	2.00
Fund administrative costs	(1.00)
Expected Rate of Return	10.25

You are required to find the expected and actual returns on plan assets.

Solution

Computation of Expected and Actual Returns on Plan Assets

		₹
Return on ₹ 1,00,000 held for 12 months at 10.25%		10,250
Return on ₹ 30,000 (49,000-19,000) held for six months at 5% (equivalent to 10.25% annually, compounded every six months)		1,500
Expected return on plan assets for 20X1-20X2		**11,750**
Fair value of plan assets as on 31 March, 20X2		1,50,000
Less: Fair value of plan assets as on 1 April,20X1	1,00,000	
Contributions received	49,000	(1,49,000)
		1,000
Add: Benefits paid		19,000
Actual return on plan assets		**20,000**

Alternatively, the above question may be solved without giving compound effect to rate of return.

Q.AS15.SM.105 (Plan Assets and Return on Plan Assets) Try (Similar to Q 104)

The fair value of plan assets of Anupam Ltd. was ₹ 2,00,000 in respect of employee benefit pension plan as on 1st April, 20X1. On 30th September, 20X1 the plan paid out benefits of ₹25,000 and received inward contributions of ₹55,000. On 31st March, 20X2 the fair value of plan assets was ₹3,00,000. On 1st April, 20X1 the company made the following estimates, based on its market studies and prevailing prices

	%
Interest and dividend income (after tax) payable by fund	10.25
Realized gains on plan assets (after tax)	3.00
Fund administrative costs	(3.00)
Expected rate of return	**10.25**

Calculate the expected and actual returns on plan assets as on 31st March, 20X2, as per AS 15.

SOLUTION

Computation of Expected Returns on Plan Assets as on 31st March, 20X2, as per AS 15

	₹
Return on opening value of plan assets of ₹2,00,000 (held for the year) @ 10.25%	20,500
Add: Return on net gain of ₹30,000 (i.e. ₹55,000 – ₹ 25,000) during the year i.e. held for six months @ 5% (equivalent to 10.25% annually, compounded every six months)	1,500
Expected return on plan assets as on 31st March, 20X2	**22,000**

Computation of Actual Returns on Plan Assets as on 31st March, 20X2, as per AS 15

	₹	₹
Fair value of Plan Assets as on 31st March, 20X2		3,00,000
Less: Fair value of Plan Assets as on 01/04/X1	(2,00,000)	
Add: Contribution received on 30/09/X1	55,000	**(2,55,000)**
		45,000
Add: Benefits paid as on 30th September, 20X1		25,000
Actual returns on Plan Assets as on 31st March, 20X2		**70,000**

Q.AS15.SM.106 (Curtailment and Settlement)

Rock Star Ltd. discontinues a business segment. Under the agreement with employee's union, the employees of the discontinued segment will earn no further benefit. This is a curtailment without settlement, because employees will continue to receive benefits for services rendered before discontinuance of the business segment. Curtailment reduces the gross obligation for various reasons including change in actuarial assumptions made before curtailment. If the benefits are determined based on the last pay drawn by employees, the gross obligation reduces after the curtailment because the last pay earlier assumed is no longer valid.

Rock Star Ltd. estimates the share of unamortized service cost that relates to the part of the obligation at ₹18 (10% of ₹180). Calculate the gain from curtailment and liability after curtailment to be recognised in the balance sheet of Rock Star Ltd. on the basis of given information:

(a) Immediately before the curtailment, gross obligation is estimated at ₹6,000 based on current actuarial assumption.
(b) The fair value of plan assets on the date is estimated at ₹5,100.
(c) The unamortized past service cost is ₹180.
(d) Curtailment reduces the obligation by ₹600, which is 10% of the gross obligation.

Solution

Gain from curtailment is estimated as under:

	₹
Reduction in gross obligation	600
Less: Proportion of un-amortised past service cost	(18)
Gain from curtailment	**582**

The liability to be recognised after curtailment in the balance sheet is estimated as under:

	₹
Reduced gross obligation (90% of ₹ 6,000)	5,400
Less: Fair value of plan assets	(5,100)
Less: Un-amortised past service cost (90% of ₹180)	300
Liability to be recognised in the balance sheet	(162)
Liability to be recognised in the balance sheet	**138**

Q.AS15.SM.107

A company has a scheme for payment of settlement allowance to retiring employees. Under the scheme, retiring employees are entitled to reimbursement of certain travel expenses for class they are entitled to as per company rule and to a lump-sum payment to cover expenses on food and stay during the travel. Alternatively, employees can claim a lump sum amount equal to one month pay last drawn.

The company's contentions in this matter are:

I. Settlement allowance does not depend upon the length of service of employee. It is restricted to employee's eligibility under the Travel rule of the company or where option for lump-sum payment is exercised, equal to the last pay drawn.
II. Since it is not related to the length of service of the employees, it is accounted for on claim basis.

State whether the contentions of the company are correct as per relevant Accounting Standard. Give reasons in support of your answer.

DBO

Answer:

The present case falls under the category of **defined benefit scheme** under Para 49 of AS 15 (Revised) "Employee Benefits". The said para encompasses cases where payment promised to be made to an employee at or near retirement presents significant difficulties in the determination of periodic charge to the statement of profit and loss. The contention of the Company that the settlement allowance **will be accounted for on claim basis is not correct** even if company's obligation under the scheme is uncertain and requires estimation. In estimating the obligation, assumptions may need to be made regarding future conditions and events, which are largely outside the company's control. Thus,

1) Settlement allowance payable by the company is a defined retirement benefit, covered by AS 15 (Revised)
2) **A provision should be made every year** in the accounts for the accruing liability on account of settlement allowance. The amount of provision should be calculated according to **actuarial valuation.**
3) Where, however, the amount of provision so determined is not material, the company can follow some other method of accounting for settlement allowances.

Q.ASIS.OM.108: (CA FINAL) (Exam)

Balance of Present Value of Defined Benefit Obligations	15,00,000
Balance of Plan Assets	10,00,000
Actuary Report Specifies:	
Current Service Costs	3,00,000
Interest Cost	20,000
Contributions to Plan Assets at the Mid of Year	1,50,000
Benefit Paid at the mid of year	2,40,000
Expected Return	12% p.a.
Closing Value of Present Value of Defined Benefit Obligations	17,00,000
Closing Value of Plan Assets at Fair Value	10,20,000

Six monthly 5.83%

Journalise, Prepare ledgers and Extracts of Balance sheet and Profit and Loss account along with disclosures.

Solution:

DBO Payable a/c

To Bank 240000 (Benefits)	Opng 1500000
	By CSC 300000
	By I.C. 20000
	Actuarial Loss 120000 B/F
Closg 1700000	

Plan Asset

Opng 1000000	Bank 240000
Bank 150000	Actuarial Loss 4753 B/F
Ex. Return 114753 (a) 120000 (b) (5247)	
	Closg 1020000

Series 200

SHORT TERM EMPLOYEE BENEFITS

Q.ASIS.SM.201

Whether an entitlement to earned leave which can be carried forward to future periods is a short -term employee benefit or a long-term employee benefit

Solution

Paragraph 7.2 of the Standard defines 'Short-term' benefits as employee benefits (other than termination benefits) which fall due wholly within twelve months after the end of the period in which the employees render the related service. Paragraph 8(b) of the Standard illustrates the term 'Short -term benefits' to include "short term compensated absences (such as paid annual 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".

Paragraph 7.2 of the Standard uses "falls due" as the basis, paragraph 8(b) of the Standard uses "expected to occur" as the basis to illustrate classification of short term compensated absences. A reading of paragraph 8(b) together with paragraph 7.2 would imply that the classification of short -term compensated absences should be only when absences have "fallen due" and are also "expected to occur".

In other words, where employees are entitled to earned leave which can be carried forward to future periods, the benefit would be a 'short-term benefit' provided the employee is entitled to either encash or utilise the benefit during the twelve months after the end of the period when the employee became entitled to the leave and is also expected to utilise the leave.

Where there are restrictions on encashment and/or availment, clearly the compensated absence has not fallen due and the benefit of compensated absences is more likely to be a long-term benefit. For example, where an employee has 100 days of earned leave which he is entitled to an unlimited carry forward, but the rules of the enterprise allow him to encash/utilise only 30 days during the next twelve months, the benefit would be considered as a 'long-term' benefit. In some situations, where there is no restriction but the absence is not expected to wholly occur in the next twelve months, the benefit should be considered as 'long-term'. For example, where an employee has 400 days carry forward earned leave and the past pattern indicates that the employees are unlikely to avail / encash the entire carry forward during the next twelve months, the benefit would not be 'short-term'

Whilst it is necessary to consider the earned leave which "falls due", the pattern of actual utilisation/encashment by employees, although reflective of the behavioural pattern of employees, does determine the status of the benefit, i.e., whether 'short-term' or 'long-term'. The value of short-term benefits should be determined without discounting and if the benefit is determined as long-term, it would be recognised and measured as "Other long-term benefits" in accordance with paragraph 129 of the Standard.

The categorisation in 'short-term' or 'long-term' employee benefits should be done on the basis of the overall behavioural pattern of all the employees of the enterprise and not on individual basis.

Q.ASIS.SM.202

In case an enterprise allows unutilised employee benefits, e.g., medical care, leave travel, etc., to be carried forward, whether it is required to recognise a provision in respect of carried forward benefits.

Solution

A provision should be recognised for all benefits (conditional or unconditional) which an employee becomes entitled to as a result of rendering of the service and should be recorded as part of the cost of service rendered during the period in which the service was rendered which resulted the entitlement. In estimating the cost of such benefit the probability of the employee availing such benefit should be considered.

Q.AS15.SM.203:

Exam

Mr. Rajan is working for Infotech Ltd. Consider the following particulars:

Annual salary of Mr. Rajan = ₹ 30,00,000

Total working days in 20X0-X1 = 300 days

Leaves allowed in 20X0-X1 as per company policy = 10 days

Leaves utilized by Mr. Rajan in 20X0-X1 = 8 days

The unutilized leaves are settled by way of payment and accordingly, carry forward of such leaves to the subsequent period is not allowed.

Compute the total employee benefit expense for Infotech Ltd. in respect of 20X0-X1.

Avg.= 30,00,000 / 300 = 10,000

2×10000 = 20000

SOLUTION

Mr Rajan is entitled to a salary of ₹ 30,00,000 for 300 total working days.

Thus, per day salary works out to ₹ 30,00,000 ÷ 300 days = Rs. 10,000 per day

In the year 20X0-20X1, Mr. Rajan availed 8 out of 10 leaves allowed by the company.

Accordingly, leaves unutilized = 10 – 8 = 2 days

In line with the company policy, Infotech Ltd. will pay Mr. Rajan for the unutilized leave.

Thus, total expense for 20X0-20X1 = ₹ 30,00,000 + (2 days unutilized leaves x ₹ 10,000 per day) = ₹ 30,20,000.

SECTION C – MCQ's

(MCQ's from ICAI Material)

1. *Gratuity and Pension would be examples of:*
   - (a) Short-term employee benefits
   - (b) Long-term employee benefits
   - (c) Post-employment benefits.
   - (d) None of the above.

2. *Non-accumulating compensating absence is commonly referred to as:*
   - (a) Earned Leave
   - (b) Sick Leave
   - (c) Casual leave
   - (d) All of the above

3. *The plans that are established by legislation to cover all enterprises and are operated by Governments include:*
   - (a) Multi-Employer plans
   - (b) State plans
   - (c) Insured Benefits
   - (d) Employee benefit plan

4. *Best estimates of the variable to determine the eventual cost of postemployment benefit is referred to as*
   - (a) Employer's contribution
   - (b) Actuarial assumptions
   - (c) Cost to Company
   - (d) Employee's contribution

5. *Actuarial gains / losses should be:*
   - (a) Recognised through reserves
   - (b) Charged over the expected life of employees
   - (c) Charged immediately to Profit and Loss Statement
   - (d) Do not charged to Profit and Loss Statement

ANSWERS	1	2	3	4	5
	c	c	b	b	c

Student Notes:-

Student Notes:-