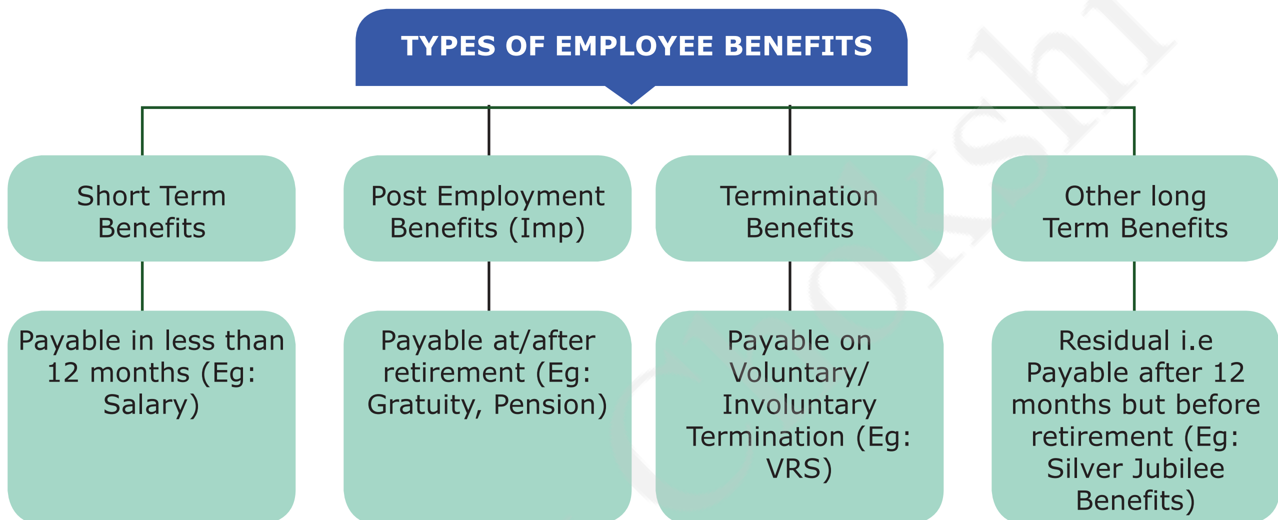
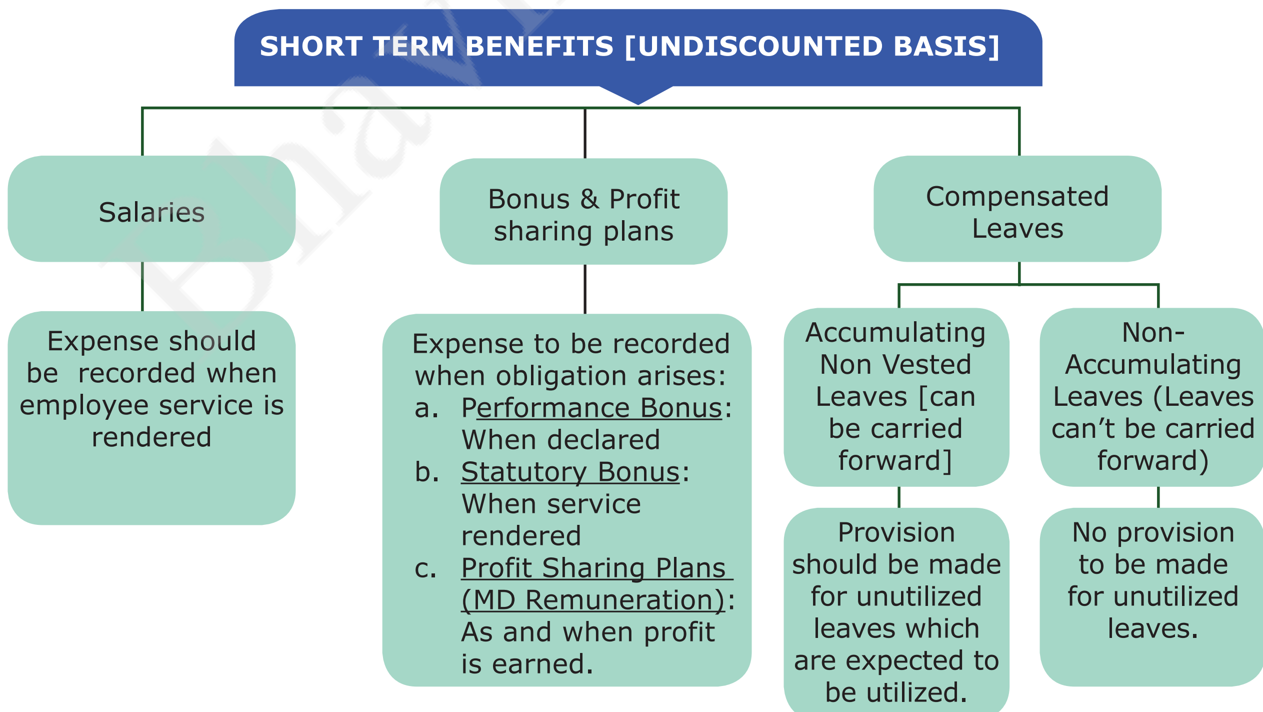
AS 15 - EMPLOYEE BENEFITS

(I) Employee Benefits - Types

AS 15 covers all employee benefits (legal and constructive) except share-based payments which are covered under guidance note for ESOP.



(II) Short Term Benefits



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Vested: *Employees can carry forward leaves and can claim encashment for unutilised leaves*

Non Vested: *Employees can carry forward leaves but can not claim encashment for unutilised leaves*

Example*: Salary : 1,000 p.m., Leave Entitlement : 30 days p.a., Carry forward permitted (Non vested) : 1 year, Actual Leaves taken : 10 days.*

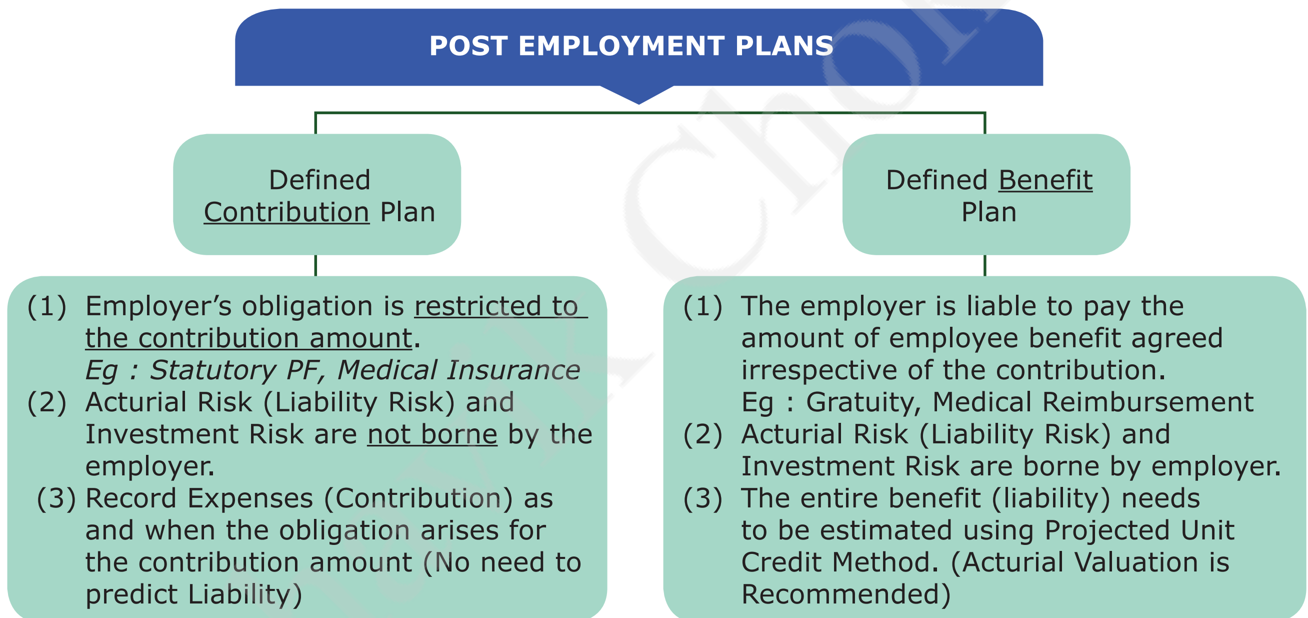
Based on Past Experience, it is expected that the employee will utilize only 15 days out of 20 days carried forward.

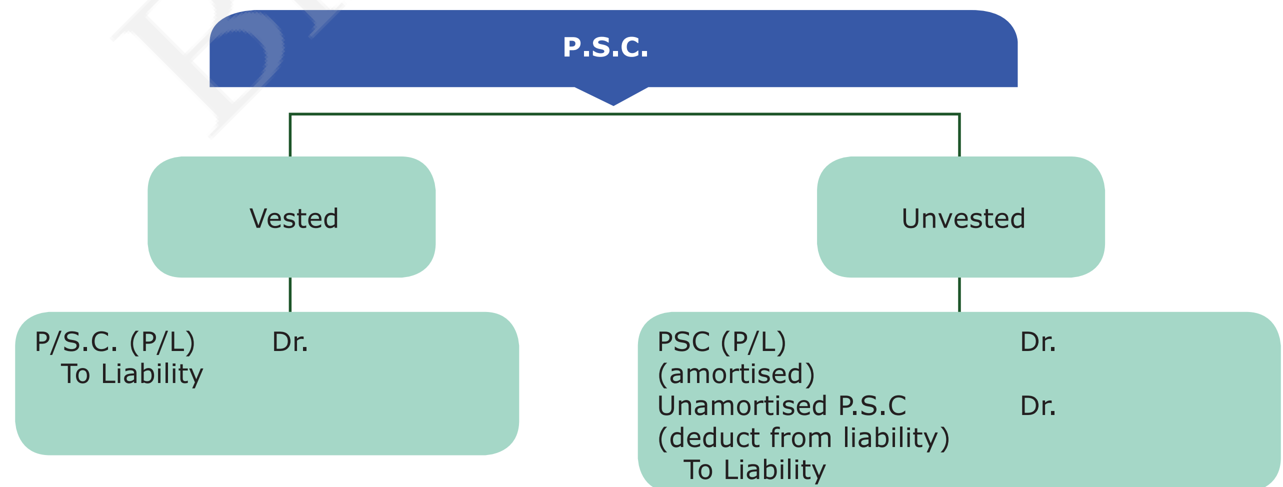
Therefore, provision for Leave Salary should be created at:

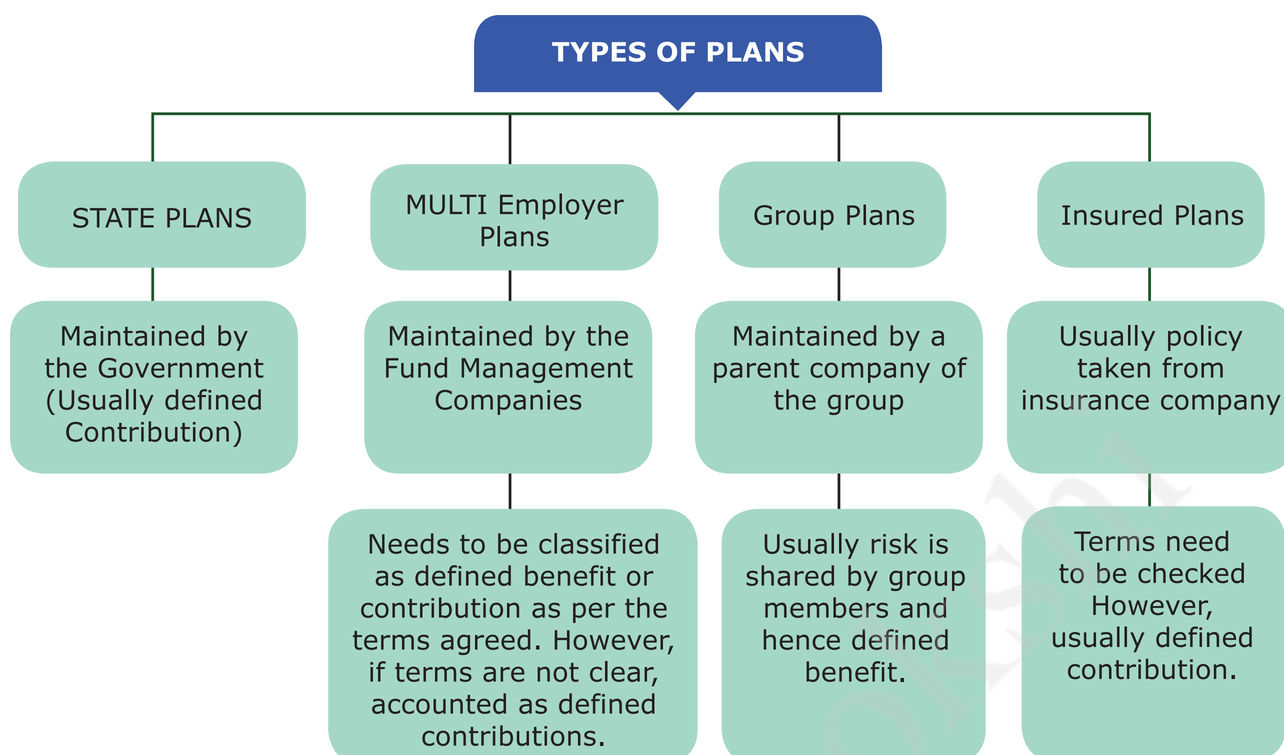
Leave Salary (P/L) a/c	Dr.	500	
To Provision for Leave Salary a/c			500

$1{,}000 \times \frac{15}{30}$

(III) Post-Employment Plans







(IV) Key Terms - Defined Benefit Liability Measurement

(1) **Current service cost [C.S.C]** - It is the increase in the liability due to employee service in the current year

(2) **Interest:** It is the increase in the liability that arises due to passage of time (opening liability × Discount Rate).

(3) **Past Service Cost:** The changes in liability due to increase in Plan Benefits (Plan Amendment)

(4) **Actuarial Gains/Losses:** These are changes which arise because an actuary alters his assumptions. Example - Last Drawn Salary.

(5) **Curtailment (Redundancies):** Refers to a material reduction in the number of employees covered under a plan or reduction in the benefits payable under the plan. The Gain/Loss on Curtailment (Redundancies) should be taken to P/L.

*Detailed Example : Mr. X is the only employee of X Ltd who was recruited at the beginning of the current year. He has been promised a lump sum payment at the time of retirement at $\frac{1}{2}$ **× Last Salary × Completed Years**. At the end of Year 1, Actuary has made the following assumptions:*

(i) Last salary : 10,000

(ii) Estimated Years of Service : 5 years (1 served, 4 yet to be served)

(iii) Discount rate : 10% (Government Bond Rate)

The plan is unfunded and has no plan assets. Calculate expenses and liability for each year

Workings

1. Benefit Attributable to Each Years Service = 1/2 × 10,000 × 1
   = 5,000

   As an employee works for the 1st Year, an expense of 5,000 accrues. However, as the expense would be paid on retirement, we will have to record it on a present value basis i.e.

   Defined Benefit Expense (P/L) a/c Dr. 3,415
   To Defined Benefit Liability a/c 3,415
   [5000 x 0.683 (PVF (10%, 4Y)]

   Further, as each year passes, the opening obligation is one more year closer and hence interest cost will also be recorded

   Further, as each year's service contributes to the employee getting additional benefit, current service cost is also recorded.

   This can be as follows:

YR	Opening	Interest @ 10%	C.S.C	Closing
1	–	–	3,415 [5,000 × 0.683]	3,415
2	3,415	342 [3,415 × 10%]	3,755 [5,000 × 0.751]	7,512
3	7,512	751	4,130 [5,000 × 0.826]	12,393
4	12,393	1,239	4,545 [5,000 × 0.909]	18,177
5	18,177	1,823	5,000 [5,000 × 1]	25,000
		4,155	20,845	

2. Continuing the above example till the end of Year 3, if at the end of Year 3 the Actuary changes his assumptions on the last drawn salary to 15000, then the benefit attributable to each year of service would be 1/2 × 15,000 × 1 = 7,500.

   Hence the Current Service Cost as well as the Balance Sheet Liability will be based on the benefit of 7,500. However, the opening balance cannot be restated as the changes are due to changes in Accounting Estimates.

   The difference in the Balance Sheet number is due to changes in Actuarial Assumptions and hence it should taken as a gain/Loss on changes in Actuarial Assumptions in Profit & Loss.

YR	OP	Int @ 10%	C.S.C	Changes in Actuarial Assumption	Closing
3	7,512	751	6,195 [7,500 × 0.826]	4,127	18,585 [1/2 × 15,000 × 3] × 0.826

3. Continuing the above example, if the entity amends the plan in the 4th year and the revised plan is 3/4 × Last Salary × Completed Years, then the benefit attributable to each year's service would be 3/4 × 15,000 × 1 = 11,250.
   The CSC and the Balance Sheet Liability should be based on the revised plan. The Balancing Figure is Past Service Cost and this should be taken in the statement of P/L in the Year when the plan is amended in case of vested benefits. In case of unvested, we will spread over the vesting period.

YR	OP	Int @ 10%	C.S.C	P.S.C	Closing
4	18,585	1,859	10,226 [11,250 × 0.909]	10,235*	40,905 [3/4 × 15,000 × 4] × 0.909

$$*\left[\left(\frac{3}{4}-\frac{1}{2}\right)\times 15{,}000\times 3\times 0.909\right]$$

(V) Plan Assets

These are assets which are earmarked investments which can be used primarily for settling defined benefit liabilities. These are assets (like government bonds) and include qualified insurance policies. The following points need to be considered for Plan Assets:

(i) Should be measured at Fair Value

(ii) Need to be deducted from the liability in order to show deficit/surplus

(iii) Actual Return and Expected Return (Discount Rate) on Plan Assets

Return = Interest Income + Dividend Income +/- Realised gain/losses +/- Unrealised gain/losses – Expenses – Taxes

Expected Return is the long-term return on plan assets predicted by Actuary. This rate should be taken as the discount rate for liabilities as well.

The Actual Return refers to the Actual amount earned during the year. The difference between Actual Return and Expected Return should be shown as ***Changes in Return which would be shown in Acturial Gains / Losses***

Alternatively, we can include the expected return (Opening Plan Assets × Discount Rate) and take the changes in return as a balancing figure in the Plan Assets Working. The expected return would be shown as a reduction from interest expense in the P/L whereas changes in return should be shown as a separate line item while calculating defined benefit expense.

(VI) Presentation in Balance Sheet

The net deficit/surplus (Liability –Asset) should be shown in the Balance Sheet subject to

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an Asset Ceiling in case of a surplus.

(VII) Summary

EXPENSE (P/L)	
Net Interest	
On Liability	xx
(-) On Assets	(xx)
C.S.C	xx
P.S.C (vested/unvested)	xx
(-) Gain on Curtailment	xx
Changes in Actuarial Assumptions (Liability)	(xx)
Changes in Return On Plan Assets	
Changes in Asset Ceiling	
EXPENSE (EBE)	xx

LIABILITY		PLAN ASSETS	
Opening (Acturial)	xx	Opening (Fair Value)(+)	xx
(+) Interest	xx	Interest	xx
(+) C.S.C	xx	(Expected Return)	xx
(+) P.S.C	xx	(-) Benefits Paid	(xx)
(-) Curtailment	(xx)	(+) Contribution	xx
(-) Benefits Paid	(xx)	+ Changes in Return (Actuarial gain/loss)	xx
+ Changes in Actuarial Assumptions	xx		
Closing (Acturial)	xx	Closing (Fair Value)	xx

Balance Sheet	
Closing Liability	xx
(-) Closing Asset	(xx)
Deficit/(Surplus)	xx
(-) Unamortized P.S.C	(xx)
Net Amount in Balance Sheet	xx

(VIII) Other Long Term Benefits

The accounting for these plans is exactly the same as the post-employment

(IX) Termination Benefits (VRS and Retrenchment)

These benefits can be recorded only once the obligation to termination arises.

Further, only that part of the benefit which is exclusively linked to termination can be recorded as termination benefits. If any part of the compensation is linked to employee's future service, then that part should be recorded as service cost and not termination cost.

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