

Introduction and Invitation to Comment

In this exposure draft the International Accounting Standards Board proposes to amend IAS 19 *Employee Benefits*. Ambiguous definitions of negative past service costs and curtailments have resulted in diverse accounting for plan amendments that reduce existing benefits. This proposed amendment clarifies that when a plan amendment reduces benefits for future service, the reduction relating to future service is a curtailment and any reduction relating to past service is negative past service cost. The Board also proposes to delete a reference to materiality in paragraph 111 of IAS 19.

The Board invites comments on the proposed amendments to IAS 19. It would particularly welcome answers to the questions set out below. Comments are most helpful if they indicate the specific paragraph, contain a clear rationale and, when applicable, provide a suggestion for alternative wording.

The Board is not requesting comments on matters in IAS 19 not addressed in the exposure draft.

Questions

1. Do you agree that IAS 19 should be amended to clarify that when a plan amendment reduces benefits for future service, the reduction relating to future service is a curtailment and any reduction relating to past service is negative past service cost? If not, why?
2. Do you agree that the Board should delete the following sentence from paragraph 111 of IAS 19: ‘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.’? If not, why?

Proposed Amendments to IAS 19 *Employee Benefits*

In the Standard, the definition of past service cost in paragraph 7, and paragraphs 97, 98 and 111 are amended (new text is underlined, deleted text is struck through).

7 ...

Past service cost is the ~~increase~~ change 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~~ when benefits are introduced or improved) or negative (~~where~~ when existing benefits are reduced).

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

[Example not amended]

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) underestimates and overestimates of discretionary pension increases ~~where~~ when an entity 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 entity 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 entity recognised 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).

111 A curtailment occurs when an entity either:

- (a) is demonstrably committed to make a ~~material~~ significant reduction in the number of employees covered by a plan; or
- (b) amends the terms of a defined benefit plan ~~such so~~ that a ~~material-significant~~ 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. When this is the case, an entity accounts for a curtailment at the same time as for a related restructuring.

111A When a plan amendment reduces benefits, only the effect of the reduction for future service is a curtailment. The effect of any reduction for past service is a negative past service cost.

In the Basis for Conclusions on IAS 19 *Employee Benefits*, paragraph 61 is amended and paragraph 62 is deleted (new text is underlined, deleted text is struck through).

61 Some commentators on E54 argued that such ‘negative plan amendments’ should be treated as negative past service cost by being recognised as deferred income and amortised into the income statement over the working lives of the employees concerned. The basis for this view is that ‘negative’ amendments reduce employee morale in the same way that ‘positive’ amendments increase morale. Also, a consistent treatment avoids the abuses that might occur if an entity could improve benefits in one period (and recognise the resulting expense over an extended period) and then reduce the benefits (and recognise the resulting income immediately). The Board agreed with this view. Therefore, IAS 19 as amended in 200X requires an entity to treat amendments that reduce benefits for past service as negative past service cost. Accordingly, ~~the new~~ IAS 19 treats both ‘positive’ and ‘negative’ plan amendments related to past service in the same way.

62 ~~[Deleted]—The distinction between negative past service cost and curtailments would be important if:~~

- ~~(a) a material amount of negative past service cost were amortised over a long period (this is unlikely, as the new IAS 19 requires that negative past service cost should be amortised until the time when those (reduced) benefits that relate to prior service are vested); or~~
- ~~(b) unrecognised past service cost or actuarial gains exist. For a curtailment these would be recognised immediately, whereas they would not be affected directly by negative past service cost.~~

~~The Board believes that the distinction between negative past service cost and curtailments is unlikely to have any significant effect in practice and that any attempt to deal with exceptional cases would result in excessive complexity.~~

Basis for Conclusions on proposed amendments to IAS 19 *Employee Benefits*

This Basis for Conclusions accompanies, but is not part of, the draft amendments.

Curtailments and negative past service costs

- BC1 Under IAS 19, plan amendments that reduce existing benefits meet the definitions of both a curtailment and negative past service costs. The International Financial Reporting Interpretations Committee (IFRIC) asked the International Accounting Standards Board to clarify when entities should account for those plan amendments as a curtailment instead of as negative past service costs.
- BC2 IAS 19 requires recognition of curtailments when they occur, together with any related actuarial gains and losses that the entity had not previously recognised. An entity recognises negative past service costs over the average period until the reduced portion of the benefits becomes vested. Members of the IFRIC reported that practices for the recognition of gains or losses on plan amendments that reduce existing benefits differ, and that such differences lead to material differences in amounts that entities recognise in profit or loss.
- BC3 The Board noted that its preliminary decisions in phase 1 of the post-employment benefits project would align the treatment of negative past service costs and curtailments, thus reducing the need to distinguish between them. However, it proposes this amendment because economic events in recent years have resulted in more plan amendments. Pending the outcome of phase 1, the distinction between negative past service cost and curtailments affects how entities account for these plan amendments.
- BC4 In the Board's view, interpreting paragraph 98(e) as excluding only reductions in benefit for *future* service from the definition of past service cost would be consistent with the reason for amending the proposal for negative plan amendments in E54, ie to treat 'positive' and 'negative' plan amendments in the same way (see paragraph 61 of the Basis for Conclusions on IAS 19). Accordingly, the proposed amendments clarify that the definition of past service cost includes reductions in benefits for past service, even if these result from plan amendments that also reduce future benefits.
- BC5 The Board also decided to eliminate the statement about materiality in the last part of paragraph 111 because it is unnecessary. The similar statement in IAS 1 *Presentation of Financial Statements* applies to all standards, including IAS 19.