

IAS Plus Update.

IASB proposes amendments to IFRIC 14

On 28 May 2009, the International Accounting Standards Board (IASB) issued an exposure draft (ED) ED/2009/4 *Prepayments of a Minimum Funding Requirement*. The ED proposes to modify IFRIC 14 *IAS 19 – the Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* so as to remedy an unintended consequence of the Interpretation whereby entities are in some circumstances not permitted to recognise as an asset prepayments of minimum funding contributions.

The IASB has requested comments on the proposals by 27 July 2009.

Background

IFRIC 14 was issued in July 2007 to address three issues:

- when refunds or reductions in future contributions should be regarded as 'available' in the context of paragraph 58 of IAS 19 *Employee Benefits*;
- how a minimum funding requirement might affect the availability of reductions in future contributions; and
- when a minimum funding requirement might give rise to a liability.

If an entity is subject to minimum funding requirements for contributions relating to future benefits, IFRIC 14 limits the economic benefits available in the form of reductions in future contributions (for the purposes of IAS 19.58) to the present value of:

- (a) the estimated future service cost in each year; less
- (b) the estimated minimum funding contributions required in respect of the future accrual of benefits in that year.

To the extent that minimum funding contributions required in respect of the future accrual of benefits exceed service cost calculated under IAS 19 in any given year, IFRIC 14 specifies that the present value of that excess reduces the amount of the asset available as a reduction in future contributions.

The issue

These requirements of IFRIC 14 unintentionally reduce the benefit that would otherwise arise from voluntary prepayment of minimum funding contributions. This is most easily demonstrated by an example (adapted from the ED – see overleaf).

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Assume that Entity A is required to pay minimum funding contributions to cover the service cost in each period determined in accordance with the minimum funding requirement. Entity A currently has an IAS 19 surplus of CU35 that cannot be refunded in any circumstances, but that could be used to reduce future contributions. The minimum contributions required to cover future service are CU15 each year for the next five years. The expected service cost in each year is CU10.

For simplicity, this example assumes that the discount rate and expected return on assets are 0 per cent, and there is no unrecognised amount. The example also assumes that the plan does not continue after five years.

Entity A 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 Entity A expects to make in the following two years, as follows.

Year	20X1	20X2	20X3	20X4	20X5
Service cost (in CU)	10	10	10	10	10
Minimum funding requirement contribution (in CU)	0	0	15	15	15
Excess of service cost over minimum funding requirement (in CU)	10	10	–	–	–
Excess of minimum funding requirement over service cost (in CU)	–	–	(5)	(5)	(5)

Under IFRIC 14 as currently worded (see previous page), at the beginning of 20X1, Entity A would recognise a plan asset of CU5 (i.e. the CU20 available from years 20X1 and 20X2 reduced by the excess minimum funding requirements in years 20X3-20X5), even though the total prepayment is CU30. The additional amount would be recognised immediately as an expense at the beginning of 20X1.

The proposed solution

The ED proposes to amend IFRIC 14.20 so that, if there is a minimum funding requirement for contributions relating to future service, the economic benefit available as a reduction in future contributions (and, therefore, the surplus that should be recognised as an asset) would be comprised of:

- (a) the amount of any prepayment of the minimum funding requirement contributions (i.e. 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
- (b) the amount of any economic benefit available as a reduction in future contributions determined as the lower of (i) the surplus in the plan excluding any prepayment in (a); and (ii) the estimated future service cost in each period less the estimated minimum funding requirement contributions that would be required for future service in that period if there were no prepayment of those contributions as described in (a).

Continuing on the previous example, under the ED Entity A would recognise a recoverable plan asset of CU30 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 may be recognised because, if there were no prepayment, the estimated minimum funding requirement contributions (CU75) that would be required for future service exceed the estimated future service cost (CU50). No liability or reduction in the prepayment asset would be recognised for this excess because it relates to future services.

Effective date and transition

The effective date of the new requirements will be determined when the final amended Interpretation is issued. The ED proposes that the amendments would be applied from the beginning of the earliest comparative period presented in the financial statements in which the entity first applied IFRIC 14. Any initial adjustment arising from the application of the ED would be recognised as an adjustment to retained earnings at the beginning of that period.

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