

# REPORT

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Committee CIPFA/LASAAC LOCAL AUTHORITY CODE BOARD

Venue Edinburgh, Barcelo Carlton, North Bridge Street

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Subject Benefits Payable During Employment and Termination Benefits Sections of Draft IFRS-Based Code

## 1. INTRODUCTION

1.1. At its meeting held on 15 April 2008, CIPFA/LASAAC agreed the format and structure of the IFRS-based Code of Practice.

1.2. This report considers the Benefits Payable During Employment and Termination Benefits sections of the draft IFRS-based Code of Practice on Local Authority Accounting. CIPFA/LASAAC is asked to approve the sections or suggest amendments.

## 2. SUMMARY OF COMPLIANCE WITH STANDARDS / IMPACT

|                                 |  |
|---------------------------------|--|
| IFRS Compliance / Adaptations   | One interpretation concerning the non-availability of the 'corridor' option for recognising actuarial gains and losses (detailed in paragraph 3.2).  |
| IPSASB Compliance / Adaptations | An adaptation of <i>IAS 19</i> contained in <i>IPSAS 25</i> concerning long-term disability benefits has been adopted (detailed in paragraph and 3.4). An <i>IPSAS 25</i> adaptation of <i>IAS 19</i> concerning the discount rate has not been adopted (paragraph 3.3). |
| i-FReM Compliance / Adaptations | Full compliance, no adaptations (detailed in paragraph 3.5).   |
| Changes to SORP                 | Yes (detailed in paragraphs 3.6 to 3.8).   |
| Impact on Taxation              | Yes, there could be a significant impact on taxation on transition to IFRS (detailed in  |

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| paragraph 3.9). |
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### 3. DRAFT CODE

- 3.1. The accounting requirements for benefits payable during employment and termination benefits are detailed in *IAS 19 Employee Benefits*. *IAS 19* also covers post retirement benefits, including pension benefits. This will be covered in a separate Code section (6.2). The sections comply fully with *IAS 19* but include one interpretation.
- 3.2. *IAS 19* permits alternative approaches to the recognition of actuarial gains and losses. The first is that only those actuarial gains and losses falling outside an agreed corridor are recognised in the Income and Expenditure Account; the second is that all actuarial gains and losses are recognised in reserves (ie in the Statement of Total Recognised Gains and Losses (STRGL)). Only the second of these approaches is permitted; that is the use of the corridor approach is not available. This is also the current SORP/FRS 17 requirement and the i-FREM contains a similar interpretation.
- 3.3. *IPSAS 25 Employee Benefits* is based on *IAS 19*, which requires entities to apply a discount rate based on yields on high quality corporate bonds; the requirement in *IPSAS 25* is to apply a rate that reflects "the time value of money". The adaptation was adopted to enable countries where there is not a deep market in high quality corporate bonds to select the most appropriate discount rate in the local circumstances. There is a deep market in corporate bond in the UK and the adaptation has not been included in the Code.
- 3.4. *IAS 19* contains a presumption that the measurement of long-term disability payments is not subject to the same degree of uncertainty as the measurement of post employment benefits. For certain public sector organisations, notably the armed services, long-term disability payments might be highly financially significant. As a response to this, *IPSAS 25* has interpreted *IAS 19* and includes the *IAS 19* 'presumption' as a 'rebuttable' assumption; and where the assumption is rebutted permits some or all long-term disability payments to be accounted for in the same way as post employment benefits. The situation the *IPSAS 25* interpretation seeks to address might also be significant for the police service and the fire and rescue services and has been adopted by the Code.
- 3.5. None of the i-FReM adaptations and interpretations of *IAS 19* are relevant to the Benefits Payable During Employment and Termination Benefits sections of the draft Code. Some i-FReM adaptations and interpretation might be relevant to the Post Employment Benefits section of the draft Code and these will be considered further in that section of the draft Code in due course.
- 3.6. Some of the matters covered by these two sections of the draft Code are not addressed by the SORP or UK accounting standards. Neither *FRS 17 Retirement Benefits* nor the SORP, cover short-term employee benefits or other long-term employee benefits, except for 'long-term disability benefits' (called 'incapacity benefit' in the SORP/*FRS17*).
- 3.7. Long-term disability benefits (which are referred to in the SORP as 'incapacity benefits') are regarded as a type of defined benefit pension benefit in the SORP/FRS 17. In *IAS 19* they are not classed as a 'post retirement benefits' but rather as 'Other long-term employee benefits'. The difference is that under *IAS 19* the net total expense is charged to the Income and Expenditure Account; whereas under the SORP/*FRS 17*, the difference between the expected cost and

amount actually incurred is treated as an actuarial gain or loss and charged to the STRGL. While under the Code long-term disability benefits are usually accounted for on 'other long-term benefits', in certain circumstances the Code permits them to be accounted for as 'post retirement benefits' (see paragraph 3.4).

- 3.8. *FRS 17* includes termination benefits as one type of past service cost, whereas *IAS 19* deals with the matter separately from past service costs. Under the SORP past service costs are recognised in the Income and Expenditure Account on a straight-line basis over the period in which the increase in benefit vests. Termination benefits would usually vest immediately and so would be charged to Income and Expenditure Account immediately. *IAS 19* also requires termination benefits to be charged to the Income and Expenditure Account immediately, so no practical impact arises from the differences between the *IAS 19* and *FRS 17*.
  - 3.9. There is likely to be a significant impact on taxation arising from the effect of providing for accumulating short-term benefits on transition to IFRS. The main impact would come from providing for untaken annual leave at the balance sheet date, but the impact of providing for untaken flexi-time and time in lieu at the balance sheet date may also be significant for some authorities. A separate agenda paper examines this matter in detail.
  - 3.10. The draft sections of the Code covering Benefits Payable During Employment and Termination Benefits are included as Appendix A. Transitional arrangements will be considered together for all three *IAS 19* based Code sections when the post employment benefit section of the Code has been drafted.
4. RECOMMENDATION

**CIPFA/LASAAC is asked to approve the Benefits Payable During Employment and Termination Benefits sections of the IFRS-based Code of Practice on Local Authority Accounting, or comment on areas where further analysis or changes are requested.**