

## IFRS Briefing Sheet

Exposure Draft *Prepayments of a Minimum Funding Requirement – Proposed amendments to IFRIC 14 IAS 19-The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*

June 2009, **Issue 136**

This IFRS Briefing Sheet summarises the International Accounting Standard Board's (IASB, or Board) Exposure Draft (ED) *Prepayments of a Minimum Funding Requirement – Proposed amendments to IFRIC 14 IAS 19-The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*, which was issued on 28 May 2009. Comments are due by 27 July 2009.

The ED proposes to amend IFRIC 14 by removing unintended consequences arising from the treatment of prepayments when there is a minimum funding requirement (MFR).

The ED proposes that prepayment of contributions in certain circumstances be recognised as an asset rather than an expense.

### Summary

The proposed amendment is intended to address the accounting treatment for prepayments made when there also is a MFR. Current requirements of IFRIC 14 state that a surplus in a plan created by a prepayment is not regarded as "an economic benefit available as a reduction in future service" if the future minimum funding contribution required in respect of future accrual of benefits exceed the future IAS 19 *Employee Benefits* service cost. Therefore, under current IFRIC 14 a prepayment would be recognised as an expense.

Under the proposed amendment such prepayment would be recognised as an asset, on the basis that an entity has a future economic benefit from the prepayment as a result of reduced cash outflows in future years in which payments would otherwise be required. The IASB believes that prepayments would reduce future contributions (i.e., cash outflows) that cover both future service costs *and* future excess of MFR contributions over service cost.

Accordingly, the ED proposes to amend paragraph 20 of IFRIC 14 to specify that there is an asset to be recognised when there is a prepayment of the MFR contributions. However, the ED also proposes that the economic

benefit available as a reduction in future service cannot be less than zero; therefore when estimated MFR contributions exceed the estimated future service cost, a liability would not be recognised nor would any prepayment asset be reduced, if applicable.

The ED provides an example illustrating the effect of a prepayment when estimated MFR contributions exceed the estimated future service cost. The following illustrates a similar example to the one included in the ED:

- Entity A is required to fund Plan C so that there is no deficit determined in accordance with an MFR
- MFR contributions are made to cover service cost in each period
- Plan C also has an IAS 19 surplus of 40 that cannot be refunded to the entity under any circumstances
- the surplus of 40 can be used for reductions in future contributions
- ignore discount rate and expected return on plan asset assumption
- the plan does not continue after five years
- for each year in the next five-year period:
  - minimum contribution required to cover service costs is 15
  - expected service cost is 10.

The entity makes a prepayment of 30, increasing its surplus at the beginning of 20X1 to 70. The prepayment of 30 reduces the future contributions it expects to make in the following two years, as follows:

Year	20X1	20X2	20X3	20X4	20X5
Service cost	10	10	10	10	10
Minimum funding requirement	0	0	15	15	15

Following the amended paragraph 20 of IFRIC 14 in the ED, Entity A would recognise an asset of 30 calculated as follows:

Prepayment of MFR contributions		30
For periods for which no prepayment has been made:		
Estimated future service cost (10 in each of years 20X1-20X5)	50	
Estimated minimum funding contributions required (15 in years 20X1-20X5)	(75)	
Economic benefit available as a reduction in future contributions	(25)	0
Recoverable asset to be recognised		30

### Effective Date and Transition

Current IFRIC 14 requirements are effective for annual periods beginning on or after 1 January 2008, except for EU member states since the EU-endorsed IFRIC 14 is mandatory from 1 January 2009.

The ED proposes that the amended interpretation would apply from the beginning of the earliest comparative period presented in the first financial statements in which the entity applied IFRIC 14; any initial adjustment arising from the application of the amendments would be recognised in retained earnings at the beginning of that period. The effective date has not been decided yet.

If you would like further information on any of the matters discussed in this issue of *IFRS Briefing Sheet*, please talk to your usual local KPMG contact or call any of KPMG firms' offices.

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