EFRAG
European Financial Reporting Advisory Group

The cost and benefits of implementing the amendments to IFRIC 14 *Prepayments of a Minimum Funding Requirement*

Introduction

1 Following discussions between the various parties involved in the EU endorsement process, the European Commission decided in 2007 that more extensive information than hitherto needs to be gathered on the costs and benefits of all new or revised Standards and Interpretations as part of the endorsement process. It has further been agreed that EFRAG will gather that information in the case of the amendments to IFRIC 14 *Prepayments of a Minimum Funding Requirement* (the Amendments).

2 EFRAG first considered how extensive the work would need to be. For some Standards or Interpretations, it might be necessary to carry out some fairly extensive work in order to understand fully the cost and benefit implications of the Standard or Interpretation being assessed. However, in the case of the Amendments, EFRAG's view is that the cost and benefit implications can be assessed by carrying out a more modest amount of work. (The results of the consultations EFRAG has carried out seem to confirm this.) Therefore, as explained more fully in the main sections of the report, the approach EFRAG has adopted has been to carry out an initial assessment of the likely costs and benefits of implementing the revision in the EU, to consult on the results of that initial assessment, and to finalise the assessment in the light of the comments received.

EFRAG's endorsement advice

3 EFRAG also carries out a technical assessment of all new and revised Standards and Interpretations issued by the IASB and IFRIC against the so-called endorsement criteria and provides the results of those technical assessments to the European Commission in the form of recommendations as to whether or not the Standard or Interpretation assessed should be endorsed for use in the EU. As part of those technical assessments, EFRAG gives consideration to the costs and benefits that would arise from implementing the new or revised Standard or Interpretation in the EU. EFRAG has therefore taken the conclusion at the end of this report into account in finalising its endorsement advice.

A summary of the amendments to IFRIC 14

4 IAS 19 *Employee Benefits* sets out how to account for various types of employee benefits. In the case of defined benefit plans, IAS 19 requires an entity to estimate the value of the present obligations it has in respect of the promises it has made and the value of any assets held in the plan to fund those obligations. IAS 19 permits entities some flexibility to make certain specific adjustments to the value of the present defined benefit obligations. It then requires entities to compare the value of the plan assets and the adjusted value of the present defined benefit obligations and:

(a) if the adjusted value of the obligations is higher, recognise the difference on the balance sheet as a liability;

(b) if the value of the plan assets is higher, recognise the difference on the balance sheet as an asset *to the extent that the amount involved is available to the entity in the form of refunds from the plan and/or reductions in future contributions to the plan*.

IFRIC 14 provides some guidance on how to interpret the italicised text.

5 One of the issues IFRIC 14 clarifies is how the requirements of IAS 19 shall be applied when the defined benefit plan is subject to a minimum funding requirement (MFR). An MFR normally stipulates a minimum amount or level of contributions that must be made to a plan over a given period. However, an unintended consequence of IFRIC 14 was identified when an entity subject to a minimum funding requirement makes an early payment of contributions. Under certain circumstances, the entity making such a prepayment of a MFR would be required to recognise an expense.

6 The Amendment eliminates this unintended consequence and treats this prepayment, like any other prepayment, as an asset (because making such a prepayment should reduce the amount of MFR contributions that would otherwise need to be made in the future).

Effective date

7 Entities are required to apply the Amendments for annual periods beginning on or after 1 January 2011. Earlier application is permitted but must be disclosed.

EFRAG's initial analysis of the costs and benefits of the amendments to IFRIC 14

8 EFRAG carried out an initial assessment of the costs and benefits expected to arise for preparers and for users both in year one and in subsequent years from implementing the Amendments in the EU.

9 The tentative conclusions reached about additional costs for preparers as a result of that initial assessment were that implementing the Amendments is likely to provide some reduced costs, but only some preparers will be affected by them and the reduction is likely to be insignificant.

10 EFRAG also tentatively concluded that the Amendments are not likely to involve users in any additional costs.

11 As a result, EFRAG's overall tentative conclusion was that the benefits to be derived from implementing the Amendments in the EU are likely to exceed the costs involved.

12 EFRAG published its initial assessment and supporting analysis on 14 December 2009 and invited comment on the material by 20 January 2010. In response, EFRAG received five comment letters and all agreed with EFRAG's initial assessment and had no additional comments, although two stated it had not carried out a detailed examination of the effects involved EFRAG's final analysis of the costs and benefits of the amendments to IFRIC 14.

EFRAG's final analysis of the costs and benefits of the amendments to IFRIC 14

13 Based on its initial analysis and on stakeholders' views on that analysis, EFRAG's detailed final analysis of the costs and benefits of implementing the Amendments in the EU is presented in the paragraphs below.

Costs for preparers

14 The Amendments will change the accounting only for voluntary prepayments of a minimum funding requirement. The accounting for pensions is already complex, and the Amendments do not reduce or increase that complexity. Thus EFRAG thinks the effort required by entities to estimate the value of their present obligations they have with respect to pensions or the value of any assets held in a plan to fund those obligations will be about the same.

15 However, EFRAG does believe that some preparers may more readily determine the accounting treatment of a prepayment because reduced analysis of future service costs and future funding requirements will be needed to make the accounting determination. This reduced analysis is expected to lead to some cost savings, but it is likely to be insignificant and only apply to the few entities that are affected by the Amendments. As a result, EFRAG thinks the Amendments will reduce costs for some preparers but the cost savings are likely to be insignificant.

Costs for users

16 EFRAG is not aware of any aspect of the Amendments that will increase the costs users will incur in analysing the financial statements.

Benefits for preparers and users

17 EFRAG's assessment is that the Amendments will result in an improvement in the quality of the information provided because certain voluntary prepayments of a minimum funding requirement will be reported as assets and will no longer be reported as an expense.

Conclusion

18 EFRAG's overall assessment is therefore that:

(a) implementing the Amendments is likely to provide some reduced costs, but only some preparers will be affected by them and the reduction is likely to be insignificant;

(b) the Amendments are not likely to involve users in any additional costs; and

(c) the Amendments are likely to result in benefits for both users and preparers that are affected by the Amendments.

19 EFRAG's assessment is therefore that the benefits arising from implementation of the Amendments in the EU are likely to exceed the costs of implementation.

20 During its consultation process, EFRAG did not become aware of any other factors that should be taken into account in assessing the costs and benefits of implementing the revised standard in the EU.

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EFRAG, Chairman
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