

Employee Benefits (IAS 19)

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1. Objective and scope of IAS 19

IAS 19 prescribes the accounting and disclosure requirements for employee benefits. Its core objective is:

- **To recognise a liability** when an employee has provided service in exchange for benefits to be paid in the future.
- **To recognise an expense** when the entity consumes the economic benefit arising from that service.

1.1 Scope

IAS 19 applies to all employee benefits except:

- **Share-based payments** (covered by IFRS 2).
- **Reporting by employee benefit plans themselves** (covered by other standards).

It covers benefits provided to:

- Employees
- Former employees
- Their dependants (in some plans)

2. Key definitions

2.1 Employee benefits

Employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees or for the termination of employment.

They include:

- **Short-term employee benefits**
- **Post-employment benefits**
- **Other long-term employee benefits**
- **Termination benefits**

2.2 Categories of employee benefits

1. **Short-term employee benefits. Definition:** Benefits expected to be settled wholly within 12 months after the end of the reporting period in which employees render the related service. **Examples:**
 - Wages and salaries
 - Short-term paid absences (annual leave, sick leave)
 - Profit-sharing and bonuses (if payable within 12 months)
 - Non-monetary benefits (medical care, housing, cars) for current employees

2. **Post-employment benefits. Definition:** Benefits payable after completion of employment. **Examples:**
 - Pensions
 - Post-employment medical care
 - Life insurance after retirement
 - Lump-sum retirement gratuities
3. **Other long-term employee benefits. Definition:** Benefits (other than post-employment and termination benefits) that are not short-term. **Examples:**
 - Long-service leave
 - Jubilee or long-service awards
 - Long-term disability benefits
 - Deferred compensation payable more than 12 months after service
4. **Termination benefits. Definition:** Benefits provided in exchange for the termination of employment, rather than for service. **Examples:**
 - Redundancy packages
 - Voluntary separation payments
 - Payments under restructuring plans

3. Short-term employee benefits

3.1 Recognition

An entity recognises:

- **A liability** when an employee has rendered service in exchange for benefits to be paid.
- **An expense** when the service is rendered.

Because settlement is within 12 months, amounts are **not discounted**.

3.2 Measurement

Short-term employee benefits are measured at the **undiscounted amount** expected to be paid.

Example 1 — Accrued salaries

Facts:

- Monthly salary: R20 000 per employee.
- December salaries (for work done in December) are paid on 5 January.
- At 31 December, salaries for December are unpaid.

Accounting:

- **31 December (accrual):**
 - Dr Employee benefit expense R20 000

- Cr Salaries payable (liability) R20 000
- **5 January (payment):**
 - Dr Salaries payable R20 000
 - Cr Bank R20 000

Example 2 — Short-term bonus

Facts:

- Management expects to pay a bonus of R300 000 for the current year.
- The bonus is payable within 12 months after year-end.
- At year-end, the entity has a present obligation (based on contract or past practice).

Accounting at year-end:

- Dr Employee benefit expense R300 000
- Cr Bonus payable R300 000

4. Post-employment benefits

Post-employment benefits are provided under **post-employment benefit plans**, which are classified as:

- **Defined contribution plans**
- **Defined benefit plans**

4.1 Defined contribution plans

4.1.1 Definition

A **defined contribution plan** is a post-employment benefit plan under which:

- The entity pays fixed contributions into a separate fund.
- The entity has **no legal or constructive obligation** to pay further contributions if the fund does not hold sufficient assets to pay all benefits.

The risk (investment, actuarial) is borne by the employee.

4.1.2 Recognition and measurement

When an employee has rendered service:

- The entity recognises the **contribution payable** as:
 - A **liability** (if unpaid), and
 - An **expense** (unless capitalised as part of an asset).

Measurement is straightforward: the expense equals the **contribution due** for the period.

Example 3 — Defined contribution pension plan

Facts:

- Employer contributes 10% of gross salary to a pension fund.
- Employee's annual salary: R240 000.
- Contribution for the year: $10\% \times R240\,000 = R24\,000$.
- At year-end, R4 000 is unpaid.

Accounting during the year:

- Dr Employee benefit expense R24 000
- Cr Pension contributions payable R24 000

At payment of R20 000 during the year:

- Dr Pension contributions payable R20 000
- Cr Bank R20 000

At year-end (R4 000 still unpaid):

- Liability of R4 000 remains in the statement of financial position.

4.2 Defined benefit plans

4.2.1 Definition

A **defined benefit plan** is any post-employment benefit plan other than a defined contribution plan.

Under such plans:

- The entity's obligation is to provide agreed benefits (e.g., a pension formula based on final salary and years of service).
- The entity bears actuarial and investment risk.

4.2.2 Key concepts

- **Defined Benefit Obligation (DBO):** Present value of the entity's obligation to pay future benefits, based on service to date.
- **Plan assets:** Assets held by a long-term employee benefit fund that are available to pay benefits.
- **Net defined benefit liability (or asset):**

$$\text{Net liability (asset)} = \text{DBO} - \text{Fair value of plan assets}$$

- **Actuarial assumptions:** Estimates of demographic and financial variables (mortality, turnover, salary growth, discount rate, etc.).

4.2.3 Measurement — Projected Unit Credit Method

IAS 19 requires the **projected unit credit method** to measure defined benefit obligations.

Key steps:

1. **Attribute benefit to periods of service**
 - Each period of service gives rise to an additional unit of benefit entitlement.
 - Benefits are attributed to periods using the plan's formula and the projected salary (if benefits are salary-linked).
2. **Project future benefits**
 - Estimate the amount of benefit payable at retirement (or other date), considering:
 - Future salary increases
 - Length of service
 - Mortality and turnover
3. **Discount to present value**
 - Use a **discount rate** based on market yields on high-quality corporate bonds (or government bonds where corporate markets are not deep).
4. **Determine DBO**
 - Sum the present value of benefits attributed to service up to the reporting date.
5. **Determine net defined benefit liability (asset)**
 - DBO minus fair value of plan assets.

4.2.4 Components of defined benefit cost

IAS 19 splits the total defined benefit cost into components recognised in different parts of the financial statements:

1. **Service cost (profit or loss)**
 - **Current service cost:** Increase in DBO resulting from employee service in the current period.
 - **Past service cost:** Change in DBO from plan amendments or curtailments.
 - **Gains or losses on settlement:** Arising when the obligation is settled.
2. **Net interest (profit or loss)**
 - Calculated on the net defined benefit liability (or asset) at the beginning of the period using the discount rate.
3. **Remeasurements (other comprehensive income)**
 - Actuarial gains and losses on the DBO.
 - Return on plan assets (excluding amounts included in net interest).
 - Changes in the effect of the asset ceiling.

Remeasurements are recognised in **other comprehensive income (OCI)** and **are not recycled** to profit or loss in subsequent periods.

4.2.5 Example 4 — Simple defined benefit plan (conceptual)

Facts:

- Plan promises a lump-sum benefit of R5 000 for each year of service, payable at retirement.
- Employee has 5 years of service at year-end.
- Discount rate: 6%.
- No plan assets yet.

Step 1: Determine total benefit earned to date

- Benefit per year: R5 000
- Years of service: 5
- Total benefit at retirement (based on service to date):

$$5 \times R5000 = R25000$$

Step 2: Discount to present value

Assume retirement is 20 years from now (for simplicity):

- Present value of R25 000 in 20 years at 6%:

$$PV = \frac{25000}{(1 + 0.06)^{20}}$$

This present value is the **DBO** at year-end.

Step 3: Recognition

- The increase in DBO from the previous year to current year is **current service cost** (plus any interest effect).
- Recognise:
 - Dr Employee benefit expense (current service cost + net interest)
 - Cr Defined benefit obligation

Please also refer to Chapter 29, which covers Accounting and Reporting by Retirement Benefit Plans (IAS 26), for more details about reporting by the fund itself.

5. Other long-term employee benefits

5.1 Nature

These benefits are similar to defined benefit plans in measurement, but they are **not post-employment** and are **not termination benefits**.

Examples:

- Long-service awards (e.g., cash bonus after 20 years of service)
- Long-term disability benefits
- Deferred compensation payable after more than 12 months

5.2 Recognition and measurement

- Measured using the **same principles** as defined benefit plans (projected unit credit method, discounting, actuarial assumptions).
- However, **all changes** in the obligation (including remeasurements) are recognised in **profit or loss**, not OCI.

Example 5 — Long-service award

Facts:

- Employees receive R10 000 after 10 years of service.
- At year-end, an employee has completed 6 years.
- The benefit is expected to be paid 4 years later.
- Discount rate: 7%.

Step 1: Attribute benefit

- Total benefit: R10 000
- Service period: 10 years

➔ Benefit attributed per year: R1 000

After 6 years, the benefit attributed to date:

$$6 \times R1000 = R6000$$

Step 2: Discount to present value

- Present value of R6 000 payable in 4 years at 7%:

$$PV = \frac{6000}{(1 + 0.07)^4}$$

This is the **liability** at year-end.

Step 3: Recognition

- Dr Employee benefit expense (current service cost + interest)
- Cr Long-service award liability

All actuarial gains/losses are recognised in **profit or loss**.

6. Termination benefits

6.1 Definition

Termination benefits are employee benefits provided in exchange for the termination of employment, rather than for service. They arise from:

- An entity's decision to terminate employment before normal retirement date, or
- An offer to encourage voluntary redundancy.

6.2 Recognition

An entity recognises a termination benefit liability and expense at the **earlier** of:

1. When the entity can no longer withdraw the offer of those benefits; and
2. When the entity recognises a restructuring provision that includes termination benefits.

Key points:

- Termination benefits are recognised **immediately** when the entity is demonstrably committed (e.g., detailed formal plan, communicated to affected employees).
- They are not spread over future service periods.

6.3 Measurement

- Measured at the **best estimate** of the expenditure required to settle the obligation.
- If payment is expected more than 12 months after the reporting date, the amount is **discounted**.

Example 6 — Redundancy programme

Facts:

- On 1 December, an entity announces a restructuring plan.
- 50 employees will be made redundant on 31 March next year.
- Each will receive R50 000.
- The plan is detailed and communicated; the entity cannot realistically withdraw it.
- Year-end: 31 December.

Recognition at 31 December:

- Total termination benefits:

$$50 \times R50000 = R2500000$$

- If payment is within 12 months, discounting may not be required (depending on materiality).

Accounting:

- Dr Termination benefit expense R2 500 000
- Cr Termination benefit liability R2 500 000

7. Presentation of employee benefits

7.1 Statement of financial position

Employee benefit balances appear as:

- **Short-term employee benefit liabilities** (e.g., salaries payable, bonuses payable).
- **Post-employment benefit obligations:**
 - Net defined benefit liability (or asset).
 - Defined contribution liabilities (unpaid contributions).
- **Other long-term employee benefit liabilities.**
- **Termination benefit liabilities.**

For defined benefit plans:

- Present **net defined benefit liability (asset)** (DBO minus plan assets).

7.2 Statement of profit or loss and other comprehensive income

1. **Profit or loss:**
 - Short-term employee benefit expense.
 - Defined contribution plan expense.
 - Service cost (current and past) for defined benefit plans.
 - Net interest on net defined benefit liability (asset).
 - Other long-term employee benefit expense.
 - Termination benefit expense.
2. **Other comprehensive income (OCI):**
 - Remeasurements of net defined benefit liability (asset):
 - Actuarial gains and losses.
 - Return on plan assets (excluding interest).
 - Changes in asset ceiling.

Remeasurements in OCI are **not reclassified** to profit or loss in subsequent periods.

8. Disclosure requirements

IAS 19 requires extensive disclosures, especially for defined benefit plans, to help users understand:

- The **characteristics** of the plans.
- The **amounts recognised** in the financial statements.
- The **risks** arising from the plans.

8.1 Defined benefit plans — key disclosures

Entities must disclose:

- **General description** of the type of plan.
- **Reconciliation** of:
 - Opening and closing DBO.
 - Opening and closing fair value of plan assets.
- **Amounts recognised** in:
 - Profit or loss (service cost, net interest).
 - OCI (remeasurements).
- **Actuarial assumptions**, including:
 - Discount rate.
 - Future salary increases.
 - Mortality rates.
 - Employee turnover.
- **Sensitivity analysis** for significant actuarial assumptions (e.g., impact of a 1% change in discount rate).
- **Risk exposures**, such as:
 - Longevity risk.
 - Discount rate risk.
 - Inflation risk.
- **Funding arrangements**, including:
 - Expected contributions to the plan in the next annual period.
 - Any asset ceiling effects.

8.2 Other long-term and termination benefits

For these, disclosures typically include:

- Nature of the benefits.
- Amounts recognised in profit or loss.
- Movements in the related liabilities.

9. Summary and exam-style focus points

To anchor IAS 19 for exam and practical use, focus on:

1. **Classification:**
 - Short-term vs post-employment vs other long-term vs termination.
 - Defined contribution vs defined benefit.
2. **Measurement:**
 - Short-term: **undiscounted** amounts.

- Defined contribution: **expense = contribution**.
- Defined benefit and other long-term: **projected unit credit method**, discounting, actuarial assumptions.
- 3. **Presentation:**
 - Split defined benefit cost into **service cost, net interest, and remeasurements**.
 - Remeasurements go to **OCI** (for defined benefit plans) and are **not recycled**.
- 4. **Termination benefits:**
 - Recognise when the entity is **demonstrably committed**.
 - Measure at best estimate, discount if long-term.
- 5. **Disclosure:**
 - Reconciliations of DBO and plan assets.
 - Key assumptions and sensitivity analyses.

10. 20 Multiple Choice Questions (with Solutions)

1. IAS 19 primarily deals with the accounting for:

- A. Share-based payments
- B. Employee benefits
- C. Leases
- D. Revenue from contracts

➔ Answer: B

2. Which of the following is *not* an employee benefit category under IAS 19?

- A. Short-term employee benefits
- B. Post-employment benefits
- C. Other long-term employee benefits
- D. Equity-settled benefits

➔ Answer: D

3. Short-term employee benefits are expected to be settled:

- A. Within 6 months
- B. Within 12 months after the reporting period
- C. Within 24 months
- D. At retirement

➔ Answer: B

4. Defined contribution plans place actuarial and investment risk on:

- A. The employer
- B. The employee
- C. The government
- D. The auditor

➔ **Answer: B**

5. Under a defined contribution plan, the expense recognised is:

- A. The present value of future benefits
- B. The fair value of plan assets
- C. The contribution due for the period
- D. The actuarial gain or loss

➔ **Answer: C**

6. Defined benefit plans require the use of which measurement method?

- A. Straight-line method
- B. Projected unit credit method
- C. Effective interest method
- D. Cost model

➔ **Answer: B**

7. The defined benefit obligation (DBO) represents:

- A. The present value of future benefits earned to date
- B. The fair value of plan assets
- C. Total contributions paid
- D. Total benefits paid during the year

➔ **Answer: A**

8. Remeasurements of defined benefit plans are recognised in:

- A. Profit or loss
- B. Other comprehensive income
- C. Retained earnings
- D. Revenue

➔ **Answer: B**

9. Which of the following is *not* included in remeasurements?

- A. Actuarial gains and losses
- B. Return on plan assets (excluding interest)
- C. Past service cost
- D. Changes in the asset ceiling

➔ Answer: C

10. Past service cost arises from:

- A. Changes in actuarial assumptions
- B. Plan amendments or curtailments
- C. Changes in discount rates
- D. Employee turnover

➔ Answer: B

11. Net interest on the net defined benefit liability is calculated using:

- A. The average salary growth rate
- B. The discount rate
- C. The inflation rate
- D. The risk-free rate

➔ Answer: B

12. Other long-term employee benefits are measured using:

- A. The same principles as defined benefit plans
- B. Undiscounted amounts
- C. Fair value model
- D. Straight-line method

➔ Answer: A

13. Remeasurements for other long-term employee benefits are recognised in:

- A. OCI
- B. Profit or loss
- C. Retained earnings
- D. Deferred income

➔ Answer: B

14. Termination benefits are recognised when:

- A. Employees accept the offer
- B. The entity is demonstrably committed to termination
- C. The restructuring is completed
- D. The board approves the annual financial statements

➔ Answer: B

15. Termination benefits expected to be paid after more than 12 months must be:

- A. Ignored
- B. Capitalised
- C. Discounted
- D. Recognised in OCI

➔ Answer: C

16. Which of the following is an example of a short-term employee benefit?

- A. Pension payments
- B. Long-service awards
- C. Annual leave
- D. Post-retirement medical aid

➔ Answer: C

17. Which of the following is an example of a post-employment benefit?

- A. Sick leave
- B. Housing allowance
- C. Retirement pension
- D. Bonus payable within 12 months

➔ Answer: C

18. Plan assets must be:

- A. Owned directly by the employer
- B. Held by a legally separate fund
- C. Included in inventory
- D. Measured at cost

➔ Answer: B

19. The net defined benefit liability equals:

- A. DBO + plan assets
- B. Plan assets – DBO
- C. DBO – plan assets
- D. Contributions – benefits paid

➔ **Answer: C**

20. Sensitivity analysis disclosures are required for:

- A. Defined contribution plans
- B. Defined benefit plans
- C. Short-term employee benefits
- D. Termination benefits

➔ **Answer: B**

11. Comprehensive Question Bank (with Solutions)

Question 1 — Classification of Employee Benefits

An entity provides the following benefits:

1. Annual leave
2. Post-retirement medical aid
3. Long-service awards payable after 15 years
4. Redundancy payments under a restructuring plan

Required: Classify each benefit under IAS 19.

Solution 1

1. Annual leave — **Short-term employee benefit**
2. Post-retirement medical aid — **Post-employment benefit**
3. Long-service awards — **Other long-term employee benefit**
4. Redundancy payments — **Termination benefit**

Question 2 — Short-Term Employee Benefits (Accrual)

Employees earn salaries of R500 000 for December, payable on 5 January.

Required: Provide the year-end journal entry.

Solution 2

Dr Employee benefit expense	R500 000	
Cr Salaries payable		R500 000

Question 3 — Short-Term Bonus

A bonus of R300 000 is expected to be paid within 12 months. The entity has a constructive obligation based on past practice.

Required: State how the bonus is recognised.

Solution 3

Recognise a liability and expense for the **undiscounted amount**:

Dr Employee benefit expense	R300 000	
Cr Bonus payable		R300 000

Question 4 — Defined Contribution Plan

An employer contributes 12% of employee salaries to a pension fund. Annual salaries total R2 000 000. At year-end, R50 000 is unpaid.

Required: Calculate the expense and year-end liability.

Solution 4

- ➔ Contribution = $12\% \times R2\,000\,000 = R240\,000$
- ➔ Expense = **R240 000**
- ➔ Liability = **R50 000** unpaid

Question 5 — Defined Benefit Plan: Basic DBO Calculation

A plan promises R4 000 per year of service, payable at retirement. Employee has 10 years of service. Retirement is 15 years away. Discount rate = 6%.

Required: Calculate the present value of the benefit earned to date.

Solution 5

- ➔ Benefit at retirement = $10 \times R4\,000 = R40\,000$
- ➔ $PV = 40\,000 \div (1.06)^{15}$
- ➔ $PV \approx \mathbf{R20\,860}$ (rounded)

Question 6 — Components of Defined Benefit Cost

List the three components of defined benefit cost and where each is recognised.

Solution 6

1. **Service cost** — Profit or loss
2. **Net interest** — Profit or loss
3. **Remeasurements** — OCI (not recycled)

Question 7 — Past Service Cost

A plan amendment increases benefits, resulting in an increase in DBO of R120 000.

Required: Explain how past service cost is recognised.

Solution 7

Recognised **immediately** in profit or loss:

Dr Employee benefit expense	R120 000	
Cr Defined benefit obligation		R120 000

Question 8 — Net Interest Calculation

- Opening net defined benefit liability = R500 000
- Discount rate = 5%

Required: Calculate net interest expense.

Solution 8

Net interest = $500\,000 \times 5\%$ = **R25 000**

Question 9 — Remeasurements

Provide three examples of remeasurements under IAS 19.

Solution 9

1. Actuarial gains/losses
2. Return on plan assets (excluding interest)
3. Changes in asset ceiling

Question 10 — Other Long-Term Employee Benefits

Employees receive R15 000 after 20 years of service. One employee has 8 years of service. Discount rate = 7%. Payment expected in 12 years.

Required: Calculate the present value of the benefit earned to date by that employee.

Solution 10

- ➔ Benefit attributed = $15\,000 \times (8/20) = R6\,000$
- ➔ $PV = 6\,000 \div (1.07)^{12}$
- ➔ $PV \approx R2\,974$

Question 11 — Recognition of Termination Benefits

An entity announces a detailed restructuring plan on 1 December. Employees will be retrenched on 31 March. The plan is communicated and cannot be withdrawn.

Required: State when termination benefits are recognised.

Solution 11

Recognise on **1 December**, when the entity becomes demonstrably committed.

Question 12 — Discounting Termination Benefits

Termination benefits of R800 000 will be paid in 18 months. Discount rate = 6%.

Required: Calculate the present value.

Solution 12

- ➔ $PV = 800\,000 \div (1.06)^{1.5}$
- ➔ $PV \approx R742\,000$

Question 13 — Defined Benefit Plan Reconciliation:

Data:

- Opening DBO = R900 000
- Current service cost = R120 000
- Interest cost = R45 000
- Benefits paid = R60 000
- Actuarial loss = R30 000

Required: Calculate closing DBO.

Solution 13

- ➔ Closing DBO = $900\,000 + 120\,000 + 45\,000 - 60\,000 + 30\,000$
- ➔ Closing DBO = **R1 035 000**

Question 14 — Plan Assets Reconciliation

Data:

- Opening plan assets = R700 000
- Contributions = R100 000
- Benefits paid = R60 000
- Return on assets (interest) = R35 000
- Remeasurement gain = R20 000

Required: Calculate closing plan assets.

Solution 14

- ➔ Closing assets = $700\,000 + 100\,000 - 60\,000 + 35\,000 + 20\,000$
- ➔ Closing assets = **R795 000**

Question 15 — Net Defined Benefit Liability

Using Q13 and Q14 above:

- DBO = R1 035 000
- Plan assets = R795 000

Required: Calculate net defined benefit liability.

Solution 15

- ➔ Net liability = $1\,035\,000 - 795\,000 = \mathbf{R240\,000}$

Question 16 — Journal Entry for Defined Benefit Cost

Data:

- Current service cost = R100 000
- Net interest = R20 000
- Contributions paid = R90 000

Required: Provide the relevant journal entries.

Solution 16

1. Recognise service cost and interest:

Dr Employee benefit expense	120 000	
Cr Defined benefit obligation		120 000

2. Record contribution payment:

Dr Defined benefit obligation	90 000	
Cr Bank		90 000

Question 17 — Sensitivity Analysis

Explain why IAS 19 requires sensitivity analysis for defined benefit plans.

Solution 17

Because key assumptions (discount rate, salary growth, mortality) significantly affect the DBO, users need to understand how changes in assumptions impact the obligation.

Question 18 — Asset Ceiling

Explain the asset ceiling rule.

Solution 18

A surplus in a defined benefit plan can only be recognised to the extent that the entity can realise the surplus through refunds or reduced future contributions.

Question 19 — Short-Term vs Other Long-Term Benefits

Annual leave accumulates and can be carried forward for 3 years.

Required: Classify the benefit.

Solution 19

It is an **other long-term employee benefit**, because settlement is not wholly within 12 months.

Question 20 — Disclosure Requirements

List four key disclosures required for defined benefit plans.

Solution 20

1. Description of the plan
 2. Reconciliation of DBO and plan assets
 3. Actuarial assumptions
 4. Sensitivity analysis
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