

# Technical Accounting Alert

## **Prepayments of a Minimum Funding Requirement (Amendments to IFRIC 14)**

### **Introduction**

On 26 November 2009, the International Financial Reporting Interpretations Committee published 'Prepayments of a Minimum Funding Requirement (Amendments to IFRIC 14)'. This is expected to be issued as an amendment to Interpretation 14.

The Amendments to IFRIC 14 address unintended consequences that can arise from the previous requirements when an entity prepays future contributions into a defined benefit pension plan.

### **Background**

IFRIC 14 sets out guidance on when an entity recognises an asset in relation to an IAS 19 surplus for defined benefit plans that are subject to a Minimum Funding Requirement (MFR).

Put broadly, IFRIC 14 limits any asset that will be recovered in the form of reduced future contributions to the excess of future service costs over the MFR contributions. One effect of this can be that asset recognition can be precluded even when an entity pays its contributions before they are due (prepayments of MFR contributions). IFRIC 14 therefore had the effect that a voluntary prepayment was recognised as an expense in some cases. This was an unintended consequence from the drafting of the original Interpretation rather than a desired outcome.

In the IASB's view, a prepayment of MFR contributions over service cost provides an economic benefit to the reporting entity if it reduces future MFR contributions. Accordingly the IASB decided to amend IFRIC 14's guidance on the amount that can be recognised as an asset to reflect that view.

### **The Amendments**

The main amendment is to paragraph 20 of IFRIC 14 and addresses voluntary prepayments that reduce MFR contributions for future service. This prepaid amount is included as one part of the calculation of the economic benefit that relates to a reduction in future contributions. The excess of future service costs over the MFR contributions is then calculated as if there had been no prepayment. This second amount is added to the prepaid amount. Reference should be made to the revised version of IFRIC 14 for more detail on the Amendments.

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### **Effective date**

The Amendments to IFRIC 14 are effective for accounting periods beginning on or after 1 January 2011. Earlier application is permitted.

### **Transition**

An entity shall apply the Amendments to IFRIC 14 from the beginning of the earliest comparative period presented in the first financial statements in which the entity applies IFRIC 14.

If the entity had previously applied IFRIC 14 before it applies the amendments, it shall recognise the adjustment resulting from their application in retained earnings at the beginning of the earliest comparative period presented. The IASB has done this on cost-benefit grounds because of the way that the amount of the defined benefit asset limit interacts with the deferred recognition of actuarial gains and losses (the IASB thought that revising these amounts retrospectively over the life of the plan would be costly and of little benefit to users).

### **Grant Thornton comment**

Prior to the publication of the Amendments to IFRIC 14, a surplus created by a voluntary prepayment of a minimum funding requirement contribution was in some circumstances treated as an expense, despite the fact that the entity making the prepayment would derive future benefit from it. The Amendments to IFRIC 14 remove this unintended consequence and are consistent with the definition of an asset in the Framework for the Preparation and Presentation of Financial Statements. We therefore welcome their publication.

### **Further information**

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