Institute of Actuaries of India

Subject SA4 – Pensions & Other Employee Benefits

May 2008 Examination

INDICATIVE SOLUTION

Introduction

The indicative solution has been written by the Examiners with the aim of helping candidates. The solutions given are only indicative. It is realized that there could be other points as valid answers and examiners have given credit for any alternative approach or interpretation which they consider to be reasonable.

Q.1

(a) The answer is expected to be in descriptive form embedding the following points;

- The existence of a pension scheme with tax concessions does not by itself ensure that individuals will get appropriate and adequate pension benefits. There is a need that adequate resources are available backing these promises.

- Following are some of the main points to be considered for enhancing security of members' benefits:

i) ***Benefit restrictions :***

- Who can participate? Eg., the employed, self-employed etc.
- Who can benefit? Eg., the individual, financial dependants etc.
- Level and form of benefits that should be available such as
    - Pension in normal health from normal retirement age or early or late
    - Pension on ill-health
    - Spouse's pension on death either in service or retirement
    - Children and dependants' benefits
    - Restriction on level of lump sum if provided
    - Transfer of benefits from one scheme to another
    - Deferred benefits on withdrawal with some revaluation etc.

- Minimum levels in order to offer protection to individuals, eg. if contracted out of EPS
- Maximum levels to avoid abuse of any tax or other financial incentives offered by the government

ii) ***Regulation :***

- Pension providers may be Pension Fund Managers, Life insurers or employers
- May be regulated either by Pension Fund Regulator or Insurance Regulator or both

- Use of Trust Law in case of employer sponsored schemes
    - Appointment of independent or professional trustees
    - Minimum number of trustees
    - Member nominated trustees
    - Removal of trustees
    - Minimum frequency of meetings
    - Regular meetings and minutes
    - Trust Deed and Rules
    - Specialists advice in legal, investment, actuarial administrative etc. areas
    - Investment principles and use of fund managers
    - Control of trust assets
    - Financing benefits – agreement of funding principles with the sponsor
    - Benefit administration – members' records and accounts
    - Exercise of discretionary powers in special cases
- Regulations for competent management with good procedures and record keeping
- Provision for debt to be placed on the provider if scheme assets are insufficient

iii) Financing provision :

- Measures to ensure security of benefit provision
    - If funded in advance, the security of accumulated assets
    - If unfunded, means to ensure that benefits are provided to eligible members/beneficiaries
- Who contributes – individual, employer, the government or some combination – to ensure contributions are received
- Minimum/maximum level of contributions
- Minimum/maximum levels of assets relative to benefits promised

iv) ***Assets :*** Assets are important so far as security of benefits is concerned.

In respect of assets following aspects help to enhance security :

- Separation of pension assets from those of sponsor
- Regular checks on adequacy of the assets relative to the liabilities
- Investment in the sponsoring provider (self-investment) to be restricted and disclosed
- Admissibility of assets
- Restriction on investments should cover
    - the kinds of investments held
    - the balance between different types of investments
    - the maximum exposure in one company or group of companies
    - the maximum exposure in an industry
    - the maximum investment in illiquid assets
    - the use of futures and options
    - the extent of any exposure to foreign currency

v) ***Funding:*** Funding of a scheme enhances security. The extent of funding is important. If funding is weak, then it is worthless whereas if funding is strong then it may be too onerous for the sponsor.

- In case of funding method and basis is important
    - Basis and method may be prescribed/non-prescribed
- A minimum or statutory funding may be required particularly in case of contracted out schemes

vi) ***Professional Reporting :*** Appointment of professionals such as an actuary, auditor etc. who have adequate powers to ask for any information relating to the scheme and in certain circumstances have statutory duty to report to the provider/regulator

- Audited accounts – annual

- Actuarial reporting – annual
- Professional bodies regulating the advisers
- Shortfall on wind-up
- Restriction on size of transfer values

vii) ***Disclosures :*** Disclosure of information by the sponsor or intermediaries about the scheme enhances security. It puts indirect pressure on the provider/sponsor :

- Basic information about the scheme on joining the scheme in the form of scheme booklet/pamphlet
- Benefit illustration disclosing benefits available under different circumstances
- Information about details of immediate/deferred benefits available to members
- An annual or more frequent fund statement
- Members to be provided – a statement of investment principles
    - Details of assets and
    - Annual report and accounts
- Regular disclosure to potential beneficiaries of the adequacy of funds and the ways in which those funds are managed and invested

- Disclosure about changes in scheme such as
    - increase of charges by fund managers
    - changes in investment principles
    - in case of employer sponsored scheme – increase of retirement age, reduction in employer contribution in case of DC scheme, reduction in accrual rate in case of DB scheme etc.

viii) ***Government:*** Government has to put a regulator to oversee schemes.

Government may also take following steps to enhance security of benefit provision:

- Government guarantee
- Central discontinuance or compensation fund – a levy to be charged from all schemes to compensate members of an insolvent scheme that has been a victim of fraud or otherwise
- Government guarantee fund to take over assets and liabilities if pension provider is insolvent
- Insolvency insurance to be mandatory

1 (b)

i) Asset sectors of a pension scheme and their main characteristics

- ***Equities***

This has been historically regarded as the most suitable sector for pension schemes

… because of the expected real return over the long term which is suitable for salary-linked liabilities

… and because empirical evidence shows they tend to produce better returns than other classes over the long term.

Reasonably large and diverse market,

Market values are volatile

The dividend stream has historically been relatively stable as many companies adopt a policy of stable dividends. Recently, the dividend yield has been low.

- ***Property***

Expected stable(ish) real return, suitable for salary-linked liabilities

Dealing costs and running costs are quite high

For investing directly in property it is necessary to do so in relatively large units…

…. Which are not always very marketable,

Provides diversity from equities,
Direct investment in property is usually inappropriate except for large schemes
Indirect investment can be made through property funds.

- ***Central & State Government securities***

Government Securities (GS) will provide a guaranteed nominal return (if held to redemption and reinvestment is made on the same terms).
Provide a high income stream …
… which can be used to match pensions in payment that either have no or fixed increases.
GS are highly marketable with low dealing costs.
There is a massive market.
Yields are influenced by government policy.

- ***Other fixed interest securities***

Similar to Government Securities so far as nature of return is concerned as they also provide a nominal return.
The yields are slightly higher than GS.
The marketability is, however, low compared to GS.

The terms may also be lower, say, not beyond 10 – 15 years.
They have a comparatively small market.
They are comparatively risky also.

- ***Cash***

Cash is often held for tactical reasons rather than as an investment
Highly liquid asset with a stable market value.

ii)

Equities are likely to produce a significant real return in the long term, which makes them broadly suitable for liabilities linked to salary and price inflation.

There is likely to be a loose match between earnings inflation and equity returns since:

- If price inflation is high, profit growth is likely to be high in nominal terms and companies will try to maintain the real value of their dividends. Earnings inflation is also likely to be high as workers try to maintain the real value of their earnings.
- If the economy is successful (i.e. grows quickly and finds new markets), dividends are likely to grow quickly, and higher pay settlements are likely to result.

(Or in other words, real dividend growth and salary growth are both a consequence of real productivity growth).

However, equity returns are very volatile. Equity market value and dividend growth is influenced by factors other than inflation and real productivity growth. In the short term (eg. year by year) there is often little correlation between equity return and salary growth. Equities are therefore not always a good match for liabilities linked to salary. If equities are held then some volatility is likely to arise between the asset and the liability values.

In practice, the fact that market values are volatile does not normally matter to most final salary schemes. It can, however, be a disadvantage to a final salary scheme in the following scenarios :

- a scheme for which there is a high chance of discontinuance in the short term
- a scheme which is not well funded and a further reduction in the funding level could result in an unexpected and high cash injection being required from the employer
- a company is concerned that its accounts will show a volatile pension scheme funding level.

The volatility of equities can also be a disadvantage for money purchase schemes in relation to assets that are soon to be disinvested to purchase an annuity.

Historical evidence shows that equities have generally produced better returns than the other asset classes over long time periods. Equities may be held with the expectation of higher returns.

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Q 2.

a)

The information to be required will include the following;

- Whether the company has Provident Fund and if so whether self-administered or by EPFO and details of the scheme.
- Whether the company has Superannuation scheme and if so whether, DB or DC and Trustee self-managed or through a life insurer and details of the scheme.
- Whether the company has Gratuity scheme, if yes then the details of the benefits and whether funded and if funded whether Trustee self-managed or through a life insurer and details of the scheme.
- Any other kind of employee benefit scheme such as post retirement medical or any other, the details and whether funded.
- Details of the accumulated leave plan if any and whether funded.
- If any actuarial report/s obtained on any of the above plans and if so, copy/ies of the same.
- Have the above schemes been reported in financial statements under Indian accounting Standards and whether any actuarial reports obtained under FAS 87 or IAS 19 or IFRS 17 or any other.

b)

- The retirement benefits in India are not regulated, though most of the provisions have laws and Income Tax rules impacting the same. There is no statutory requirement for benefit illustrations to be provided under DC schemes to the member/beneficiary.
- However the Indian actuarial profession has put in place guidance note 14 for the actuary to follow in case he/she is required to prepare benefits illustration. The brief aspects of this guidance note are;

Actuary's Responsibility:

-The actuary should be satisfied that, in his or her opinion, the illustrations are meaningful and realistic for individual members at all relevant ages.
-The assumptions used should be consistent and reasonable keeping in view the provisions contained in other Guidance Notes relevant to the illustrations under the defined contribution pension schemes.
-Existing assets and future contributions (if any) taken into account in the illustration should be measured on basis consistent with the assumptions used.
-The actuary should describe or illustrate how the result will differ if the assumptions used are not borne out.
-The actuary should describe or illustrate how income draw down benefits will differ if the assumptions used (including annuity purchase rates) are not borne out.
-If the illustration shows different investment returns for different categories of investment, the relative risks of these different classes of investment should be explained.
-Benefit illustrations may be in real or monetary terms. For illustrations in monetary terms, an explanation of how the illustrated benefits should be adjusted to allow for inflation should be provided.
-Administrative expenses charged to a scheme member's account, if any should be taken into account.

Report

-The actuary should use his or her best endeavour to ensure that the illustration is presented to the ultimate recipient in a complete and balanced way.

-If a specific calculation method (that is one required by a regulatory or other appropriate authority) has been used, then the illustration should make this clear. -Where illustrations do not follow a particular regulatory method, the actuary should consider whether it is appropriate to draw attention to this in the illustration and to make clear that the illustration is not suitable for comparing with projections prepared on other specified basis.

-The illustration should contain a statement of the principal assumptions used to calculate the illustrated benefits.

-The actuary should provide sufficient information to allow the ultimate recipient of the illustration to relate the benefits shown to his or her current income. The illustrated benefit may be a monetary amount, in real terms, or a percentage of projected salary.

-The illustration should make clear what death benefits and what level of pension increases in payment have been included in the illustrated benefits.

-In addition to providing basic information, the illustration should make clear:

- which of the member's funds have been included in the illustrated benefits.

-what level of future contributions has been assumed (including increases to future contributions);

-whether any adjustment has been made to future contributions, for example to cover the cost of insured death benefits; and

-if any asset values used are not market values, why these values have been used?

-Income draw down illustrations should explain the way in which the absence of the normal cross-subsidy from early deaths under an

annuity contract may affect the benefits eventually secured when an annuity is purchased.

-All illustrations should include appropriate risk warnings and advise the ultimate recipient to obtain regular updates of the illustration.

Comparison of Defined Benefit and Defined Contribution Benefits

-Particular care should be taken in preparing an illustration that will be used to compare defined benefits and benefits from defined contributions, since it is possible that a scheme member will make an irrevocable choice of future benefit arrangements based on such an illustration.

-The actuary should provide sufficient information to enable the scheme member to understand the difference between defined benefit and defined contribution as regards the relative risk borne by the employer and the employee. The assumptions used to project the defined benefit and defined contribution benefits should be consistent.

-An illustration prepared for this purpose should show separately the illustrated benefits from existing assets and the illustrated benefits from future contributions, if any, so the recipient can compare both current accrued benefits and ultimate retirement benefits assuming service continues to the illustrated retirement age.

-The actuary should ensure that the illustration draws the scheme member's attention to other benefits that may be advantageous to that member and which differ significantly between the arrangements being compared.

c)

Fringe Benefit Tax (FBT) and Approved Superannuation Fund

Contribution to an "approved superannuation fund"

A - Background

1. The Minister of Finance (MoF) introduced the Finance Bill, 2005 in Parliament on 28 Feb 2005 announcing amongst other things the concept of Fringe Benefit Tax (FBT). The Bill has become Law as Finance Act, 2005 (FA 2005) in May 2005 effective financial year beginning 01 04 2005 or after.
2. In respect of FBT the FA 2005 inserts Chapter XIIH in the Income Tax Act 1961 introducing section 115W to the Income Tax Act, 1961

3. The FBT is "additional Income Tax" @30.00 % on the value of Fringe Benefits payable whether or not the Employer is liable to pay Income Tax otherwise [Sect 115WA(2)].

4. Definition of FBT (115WB):

"Fringe Benefits means any consideration for employment provided by way of;

a) Any privilege, service, facility or amenity, directly or indirectly, provided by an employer, whether by way of re-imbursement or otherwise, to his employees (including former employee or employees);

b) Any free or concessional ticket provided by the employer for private journeys of his employees or their family members; and

c) Any contribution made by the employer to an approved superannuation fund for employees."

- Contributions to the mandatory Provident Fund and mandatory gratuity benefits are not included under FBT.

5. The FBT @30.00% is applicable on the total amount of contribution to the approved superannuation fund paid in excess of Rs.1,00,000/- for each employee (sec 115WC (1b)).

B - Contributions to an "Approved Superannuation Fund" - Issues and implications for Employer and Employees

1. **Approved Superannuation Funds** – What do these mean for the Employer and for the Employees?

- Provision of Superannuation benefits; mandated by Income Tax Act to be in the nature of life annuity (with or without certain element) with commutation (with a cap) is optional i. e. not mandated by Law but when provided for is regulated under Income Tax Act, 1961.

- FBT applies to approved superannuation funds but does not apply superannuation funds which are not "approved".

The approved superannuation funds in pre-FBT regime;

Elements	**Employer**	**Employees**
Contribution	Treated as business expense with a cap of 15% of the salary (27% for PF + Superannuation)	Not treated as perquisites and hence not taxed.
Investment Income of the Fund (assets are regulated)	Tax free	Tax free
Benefits - commutation	-	Tax free
Benefits – annuity/pension	-	Treated as taxable income

2. **Effect of FBT:**

    i. 30% of the contribution, say 15% of the salary, i.e. 4.50% of the salary is on the employer. However, up to the contribution of Rs.1,00,000/- for each employee no FBT.

    ii. All other aspects for the employer remain unchanged.

    iii. Employees are not affected.

3. **Issues and implications;**

Case 1: Existing Superannuation Funds (DB or DC or hybrid) other than under sec. 35 of EPS, '95:

Issues: additional tax @30.00% of the contribution in excess of Rs.1,00,000/- for each employee will affect the financials i. e. it will enhance losses or reduce profits or if marginally profitable then losses.

Options available to employers

1. **Do nothing**

    Implications for the employer: Bear additional FBT burden.

2. Close the existing pension scheme for future contributions and pay cash allowance to the extent of existing contribution:

Implications for the Employer;

(i) Saving on FBT

(ii) Approval required from Income Tax authorities for closing the scheme/fund to future contributions.

(iii) Issues; HR and procedural consequential to the decision to close the fund to future contributions.

Implications for the employees:

i. The cash allowance is taxable, hence net gain may be less than the amount of contribution
ii. No benefit of tax -free investment accumulation
iii. No benefit of tax-free commutation lump sum amount.
iv. The employee is free to utilize the amount in any manner.

What should an employer do?

i. Depends on his financial condition.
ii. Depends on employees' attitude; if young then may prefer to take cash rather than wait for pension.

Case 2: Employer having an approved superannuation fund under section 35 of EPS 95

Issues;

i. All consequences of case 1
ii. If not having exemption then under EPS, '95 and contribution not under FBT

Case 3: Start-up companies or companies not having any superannuation arrangement but wanting to do so:

Options available to employer;

1. Offer the pension benefits under an approved superannuation fund and pay FBT on the contribution (DB or DC)
2. Pay cash allowance equal to the intended contribution with the upper cap of 15% with implications for the employees as under;

i. The cash allowance is taxable, hence net gain may be less than the amount of contribution
ii. No benefit of tax -free investment accumulation
iii. No benefit of tax-free commutation lump sum amount.
iv. The employee is free to utilize the amount in any manner.

C - Alternative/s to approved superannuation fund:

1) Have a superannuation fund but not an approved one –

- The contribution though may be allowed as an expense for P/L under AS 15 (rev.2005) may not be allowed as such for Tax purposes.
- The accumulations may be taxed and commutation may not be tax-free.
- The contribution in excess of Rs.1,00,000/- for each employee may still attract FBT under section 115WB (2) (E) of the Income Tax Act, 1961.

2) Have an unfunded, un-approved, though "reserved" superannuation scheme –

- Create a scheme applicable to all or specified class of employees
- The scheme has objective to purchase pension/annuities from insurer on exit from employment or to pay lump sum if the accumulation is small (a pre-determined limit).
- The scheme will be x% of the salary accumulated at y% to be available to pay lump sum or purchase annuity as the case may be.

Implications for the Employer;

- No FBT, since no funding
- Need to be reserved for P/L and disclosed in the Balance Sheet

- As reserved and disclosed, will count as expense under AS 15.
- Can easily be included in CTC for compensation counting.
- Since not actually paid in the year of service, Income Tax may not allow as expense for Tax computation, but when actually paid should then count as expense for Income Tax.
- Benefits when paid will count as taxable and thus may not count as perquisite for employee tax in the year of service, when reserved.

d (i)

The Guidance Note issued by the Accounting Standards Board [ASB] of the Institute of Chartered Accountants of India [ICAI] read in conjunction with Para 26 [b] of Accounting Standard 15 (rev.2005) treats exempted provident funds with an embedded interest rate guarantee as Defined Benefit Plans. Accordingly the relevant provisions of AS15 (rev2005) relating to measurement principles and disclosure requirements will apply to such plans. Hence the need arises to value and report the interest rate guarantee as part of the Present Value of Obligations (PVO) under AS15R.

d (ii)

The steps involved in applying stochastic model approach for valuing the interest rate guarantee are as follows:

- Obtain the (continuously compounded) Zero coupon gilt yield curve on the balance sheet date over the decrement –adjusted expected working life time of the members of the exempt provident fund.
- Using the Zero coupon yield curve in conjunction with any appropriate stochastic interest rate projection model, project the short-rates [one-year forward rates] over the decrement adjusted working lifetime. The short rates need to be adjusted for the yield-spread as defined under the closed-form approach.

- Under each of the interest rate paths, determine the present values of the shortfalls and the present value of the surpluses. A shortfall will arise in the year(s) in which the projected interest rate falls below the guaranteed interest rate and "surplus" will arise in the year(s) in which the projected interest rate is above the guaranteed interest rate. The PVO of Interest Guarantee will be equal to the Present Value of the Shortfalls minus the Present Value of the Surpluses. The "surpluses" will be valued only if the enterprise can retain the investment returns in excess of the guaranteed rate.
- Rank order the "PVOs of Interest Guarantee" values obtained for the various interest rate paths starting with the "largest" PVO and ending with the "smallest" PVO. Select an appropriate point in the tail of this rank-ordered distribution and compute the CTE [Conditional Tail Expectation] at that point. The "PVO of Interest Guarantee" will be equal to this CTE.
- The CTE(p) is defined as the arithmetic mean of the largest 100(1-p) % PVOs from the rank-ordered PVO distribution. For example, a 95% CTE will be the arithmetic mean of the largest 5% of the PVOs.
- The CTE approach is relevent because it is consistent with the approach recommended in "GN22: Reserving for Guarantees in Life Assurance Business" issued by the Institute of Actuaries of India

e (i)

A scheme sponsor has financial obligations in respect of the accrued liabilities. In particular, we can view the sponsor as having a financial responsibility to back the liabilities. This is called sponsor covenant and can be defined as the combination of i) the ability and ii) the willingness of the sponsor to pay (or the ability of the trustees to require the sponsor to pay) sufficient contributions to ensure that the scheme's benefits can be paid as the fall due

e (ii)

The are two scenarios in which the sponsor may be viewed as having obligation to back the scheme;

a) on an ongoing basis – in many schemes the sponsor may be having legal obligation to finance the benefits and/or there may be statutory requirement to contribute a minimum level of contribution.

b) on discontinuance – on winding up if there is deficit the same can be viewed as an unsecured debt on the sponsor. however the sponsor can only meet this debt if it has sufficient resources after meeting the debt ranking above it.

e (iii)

The term credit risk is often used in conjunction with bonds. In this context it is the possibility of the bondholder suffering a loss because the company defaults on the bond's coupon and/or redemption payment. Thus credit risk can be used as an analogy for sponsor covenant.

e (iv)

In all circumstances **except** the following sponsor covenant should be considered;

- The scheme is very well funded, therefore no reliance is placed on the sponsor covenant.
- The sponsor covenant is strong enough to be deemed as certain.
- The sponsor covenant is so weak as to be deemed nil.
- The sponsor has no further liability.

f)

- The Trustees of the company B should look after the interest of all the members which includes the transferring members.
- If the benefits to be received under company A depend on the size of the transfer value paid across, the company B trustees will be looking to pay a transfer value that is fair to the transferring members whilst not leaving the scheme in a significantly worse position than it was before. "Fair" in this context will usually mean the value of the past service rights on a realistic basis.
- The management of the company B on the other hand may well be more interested in the financial implication of the whole deal and looking to pay as low a transfer value as possible whilst receiving as high a price as possible for the company.
- A low transfer value may not satisfy the trustees' objectives as above.

g)

The objectives of an employer might be to;

- Attract and retain good quality employees by providing benefits that employees perceive to be attractive, that represent good value for money and are in line with major competitors.
- Offer protection to employees in retirement or to dependents on death.
- Control costs eg predictability, stability, flexibility.
- Make the scheme simple to administer and communicate to employees
- Take advantage of tax concessions if any.
- Aid or complement other business needs eg mergers or redundancies.
- Integrate with state retirement provisions.

h)

(i) The accounting standard does not define the term "employee", however para 6 states that an employee may provide services to an enterprise on a full-time, part-time, permanent, casual or temporary basis and the term would also include the whole-time directors and other management personnel. The standard is therefore applicable to all forms of employer-employee relationships and there is no requirement for any formal employer-employee relationships. Generally "outsourcing contracts" may not meet the definition of employer-employee relationship. However such contracts need to be carefully examined to distinguish between a "contract of service" and "contract for service". A "contract for service" implies a contract for rendering services eg professional or technical services which is subject to limited direction and control where as a "contract of service" implies a relationship of an employer and employee and the person is obliged to obey orders in the work to be performed and as to its mode and manner of performance.

(ii)

The Standard defines "short-term" benefits as employee benefits (other than termination benefits) which **fall due** wholly within 12 months after the end of the period in which the employees render the related service. The Standard further illustrates the term "short – term benefits" to include short term compensated absences (such as paid annual leave) where the absence are expected to occur within twelve months after the end of the period in which the employees render the related employee service. This illustration implies that the classification of short term compensated absences should be only when absences have "fallen due" and are also "expected to occur". In other words where employees are entitled to earned leave which can be carried forward to future periods the benefits would be a "short-term benefit" provided the employee is entitled to either encash/utilize the benefits during the twelve months after the end of the period when he became entitles to the leave and is also expected to do so. Where there are restrictions on encashment/availment, clearly the compensated absence has not fallen due and the benefits of compensated absence is more likely to be a long-term benefit.

(iii)

A key distinction between DB and DC is that in the case of DB plans the actuarial risk (that benefits will cost more than expected) and investment risk fall, in substance, on the enterprise. If actuarial or investment experience are worse than expected, the enterprise's obligation may be increased. Where a gratuity scheme is covered under an insurance policy, the payments to the insurance company under the policy would not be considered as DC if the actuarial risk and investment risk is borne by the enterprise. In the case of group gratuity scheme the employer makes funding through a Gratuity Trust to an amount maintained at an Insurance Company. The Insurance Company takes care of the investment of the funds in accordance with the pattern prescribed by the Income Tax Act. The return on such funds is passed on as interest from time to time. The Gratuity claims as per rules of the employer are withdrawn from the fund and paid to the employees through the Gratuity Trust. An actuarial valuation is generally conducted by the Insurance company as on date of commencement and also at yearly intervals to assess the present value of the gratuity liability and to indicate the fund required to meet the liability. Such a scheme would consequently be a DB plan. The assets held by the Insurer would be required to be considered by the enterprise while recognizing the amount of DB liability in the Balance Sheet.

(iv)

The fair value of the trust assets net of liabilities out of which the obligations are to be settled directly would be deducted from the present value of the DB obligation and the net total would be recognized in the Balance Sheet The assets and liabilities of the trust individually would not appear in the separate financial statements of the enterprise.

(v)

The term market yields at the balance sheet date on government bonds means the market yields of appropriate currency and term consistent with the currency and estimated term of the post-employment benefit obligations. The market yield on government bonds vary from time to time and are affected by a number of factors including prevalent interest. The purpose of using the words "market yields at the balance sheet date" is to ensure that

yields prevalent on that date are considered instead of a long-term average rate, based on past experience over a number of years or any other rate during the financial year.

(vi)

Accounting policies refer to the specific Accounting Principles and the methods of applying those Principles in the preparation and presentation of financial statements. Accordingly any change in the application of the principles of accounting under AS 15 (rev.2005) as compared to AS 15 would be a change in Accounting Policy and should be dealt with as per requirements of AS 5. Whether application of AS 15 (rev.2005) would result in change in Accounting Policy or a change in accounting estimate would depend on facts and circumstances of such case. For example where an enterprise measures post-employment benefits using Projected Unit Credit method as against the Aggregate method in the past, such a change would be a change in accounting policy.

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