

Valuation of Leave Under AS 15 (revised 2005)

The following is the brief version of an opinion given by the Expert Advisory Committee of the Institute in response to query sent by a member. This is being published for the information of readers.

A. Facts of the Case

1. A company is a premier professional electronics company under the Ministry of Defence, Government of India, having its shares listed on the major stock exchanges in India. The turnover of the company for the financial year 2005-06 is Rs. 3,536 crore.
2. The querist has stated that the employees of the company are entitled to three types of leave: annual leave (AL), sick leave (SL) and casual leave (CL). Casual leave is credited to employees in April and can be utilised during the financial year. No carry-over of the casual leave is permitted, and hence, according to the querist, is not being considered for the purpose of valuation under Accounting Standard (AS) 15 (revised 2005), 'Employee Benefits', issued by the Institute of Chartered Accountants of India (ICAI).
3. SL is credited at the rate of 20 days (half-pay) on the first day of April to all employees. AL is credited based on the number of years of service, as follows:

Service less than 6 years	22 days
Service of 6 – 12 years	24 days
Service of 12 – 18 years	27 days
Service above 18 years	30 days

The credit is given in two instalments, 50% on 1st April and the balance on 1st October.
4. Employees are allowed to carry forward the unutilised leave relating to both annual and sick leave. The maximum number of AL balance that can be carried forward as on 31st March is 300 days. There is no limit to the number of days of sick leave that can be carried forward. While AL is encashable during service, SL is not. The employees are entitled to encash the entire balance of AL subject to retaining one-year's entitlement. On retirement, including voluntary retirement (not on resignation), balance of SL, subject to a maximum of 300 days (150 days full pay) can be encashed.
5. The querist has stated that under the pre-revised AS 15, 'Accounting for Retirement Benefits in the Financial Statements of Employers', the company ascertained the liability relating to AL and SL on an actuarial basis, and the incremental liability was debited to the profit and loss account. No funding is done towards this provision. The revised AS 15 defines short-term employee benefits as "**employee benefits (other than termination benefits) which fall due wholly within twelve months after the end of the period in which the employees render the related service**" (paragraph 7). As mentioned above, the employees of the company are entitled to *avail* the entire leave (AL / SL) balance to their credit. Hence, the company is of the opinion that provision needs to be made for the entire balance at the credit of the employee (emphasis supplied by the querist).
6. AS 15 (revised 2005) also brings out that short-term employee benefits, inter alia, include "short-term compensated absences (such as paid annual leave) *where the absences are expected to occur within twelve months after the end of the period in which the employees render the related employee service*" (paragraph 8(b)) (emphasis supplied by the querist).
7. The querist, vide his subsequent letter, informed the Committee that the company has started implementing the provisions

of AS 15 (revised 2005) from 1/4/2006 and the quarterly results have been prepared following AS 15 (revised 2005). The querist has further mentioned that even though the Council of the Institute has decided to postpone the effective date of AS 15 (revised 2005) to accounting years commencing on or after 7/12/2006, since the earlier application of the proposed Accounting Standard by enterprises is always encouraged, the company may like to continue to follow AS 15 (revised 2005) from 1st April, 2006 onwards.

B. Query

8. The querist has sought the opinion of the Expert Advisory Committee on the following issues:

- (i) Whether the company should treat the leave benefits as short-term employee benefits and debit the profit and loss account with the entire amount of leave credited to the employees account during the year (as mentioned earlier) since encashment/availment is possible in line with paragraph 7 of AS 15 (revised 2005) or the company needs to continue the actuarial valuation of leave balances as on 31st March and provide for the incremental liability, since in practice all the employees do not encash/avail the leave.
- (ii) Whether the company will need to follow differential treatment for AL/SL, since AL is encashable during service, but SL is encashable only on retirement, though both can be availed fully during service (emphasis supplied by the querist).

C. Points considered by the Committee

9. The Committee, while answering this query, has restricted itself to the issues raised in paragraph 8 above and has not touched upon any other issue arising from the Facts of the Case, such as accounting treatment

that should have been provided from the angle of pre-revised AS 15, transitional provisions, treatment of casual leaves, etc.

10. The Committee notes that the definition of the term 'short-term employee benefits' as reproduced in paragraph 5 above states as below:

"Short-term employee benefits are employee benefits (other than termination benefits) which fall due wholly within twelve months after the end of the period in which the employees render the related service."

11. The Committee also notes that paragraph 8 of AS 15 (revised 2005) provides as below:

"8. Short-term employee benefits include items such as:

- ...
- (b) short-term compensated absences (such as paid annual leave) where the absences are expected to occur within twelve months after the end of the period in which the employees render the related employee service;

..."

12. On the basis of the above, the Committee is of the view that short-term employee benefits include only those compensated absences which accrue to the employees and are expected to be availed (or encashed, as the case may be) within twelve months after the end of the period in which the employees render the related service. Thus, those compensated absences which can be and are also expected to be carried forward for any further period cannot be termed as 'short-term employee benefits'. In this context, the Committee also notes the definition of the term 'Other long-term employee benefits' as contained in AS 15 (revised 2005), which is reproduced below:

"Other long-term employee benefits are employee benefits (other than post-employment benefits and termination

benefits) which do not fall due wholly within twelve months after the end of the period in which the employees render the related service."

13. The Committee notes from the Facts of the Case that the AL and SL entitlement of the employees of the company can be carried forward for more than twelve months after the end of the period in which employees render the related service, which can be either availed or encashed, as the case may be. Therefore, the benefit arising to the employees on account of AL and SL falls within the category of 'other long-term employee benefits'. However, in case the past trend indicates that the employees will settle the benefit accruing to them on account of AL and SL within the twelve months after the end of the period in which the employees render the related service, the same would fall within the category of 'short-term employee benefits'. However, this does not seem to be the case in the case of the company.
14. With respect to the recognition and measurement of other long-term employee benefits, the Committee notes that AS 15 (revised 2005) provides that the same should be measured on actuarial basis using the Projected Unit Method. The Standard contains detailed requirements in

this regard in paragraphs 129 and 130.

15. The Committee is further of the view that whether the leaves are encashed or availed, both are considered as employee benefits within the provisions of AS 15 (revised 2005). Therefore, the provisions of the said Standard would apply in both the cases. However, their measurement basis may be different, which would be taken care of in the actuarial valuation of the employee benefits.

D. Opinion

16. On the basis of the above, the Committee is of the following opinion on the issues raised by the querist in paragraph 8 above:
 - (i) The annual leave and sick leave benefit should be treated as 'other long-term employee benefits' in accordance with the provisions of AS 15 (revised 2005) and should be provided for on actuarial basis as explained in paragraph 14 above.
 - (ii) Since AL and SL, both fall within the category of 'other long-term employee benefits', the treatment would be the same for both kinds of leaves. However, their measurement basis may be different which would be taken care of in the actuarial valuation. □

Notes:

1. The Opinion is only that of the Expert Advisory Committee and does not necessarily represent the Opinion of the Council of the Institute.
2. The Compendium of Opinions containing the Opinions of Expert Advisory Committee has been published in twenty-four volumes, which are available for sale at the Institute's office at New Delhi and its regional council offices at Mumbai, Chennai, Kolkata and Kanpur.
3. Recent opinions of the Committee are available on the website of the Institute at URL: http://www.icai.org/icairoot/resources/resource_index.jsp

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