## DEWAN P.N. CHOPRA & CO.

# AUDIT UPDATE

# THE IMPACT OF COVID-19 ON EMPLOYEE BENEFIT EXPENSES

The COVID-19 pandemic may affect the many companies' employee benefits expenses. That can impact on the following:

a. Changes to Remuneration Policies

b. Updating Estimates including actuarial assumptions

c. Impact on Share Based Payments

## Changes to Remuneration Policies

Some companies may offer their employees paid absence in addition to any sick or annual leave entitlement. If new paid absence entitlements do not accrue through past service and do not accumulate, then it is unlikely that a company would recognise a liability for these paid absences. Instead, it would expense the cost as absences are taken. Companies will need to consider, more generally, whether they have any legal or constructive obligations to its employees as a result of these events.

If a company implements a restructuring plan that includes employee redundancies, then it recognises an expense and a corresponding liability for termination benefits at the earlier of when it:

- Recognizes a restructuring provision under Ind AS 37 Provisions, Contingent Liabilities and Contingent Assets that includes the payment of termination benefits; and

- Can no longer withdraw the offer of those benefits.

A company recognises a restructuring provision when it has a formal plan with sufficient detail of the restructuring and has raised a valid expectation in those affected by the plan – i.e. it has either started to implement the plan or has announced the main features to those affected by it.

## Updating Estimates, Including Actuarial Assumptions

Companies may need to consider the potential impact on estimates, including actuarial assumptions used in measuring employee benefits.

During periods of mandatory quarantine or lockdowns, employees could be required to use existing employee entitlements – e.g. sick or annual leave entitlements. Therefore, companies may need to consider the impact on the measurement of employee benefits – e.g. they may need to revise estimates of the likelihood and timing of employees using these entitlements.

There could also be an impact on certain demographic and financial assumptions used to measure these benefits – e.g. the discount rate used to measure the present value of employee benefit obligations.

Companies preparing interim financial statements should consider whether net defined benefit obligations/assets need to be remeasured. Under Ind AS 19 / AS - 15 Employee Benefits, re-measurements are recognised in the period when they arise; therefore, if adjustments at the interim reporting date are considered to be material, then they will need to be recorded at that date. An updated measurement of plan assets and obligations is required when a plan amendment, curtailment or settlement is recognised. In addition, significant market fluctuations may trigger the need for an updated actuarial valuation.

Practically, many companies obtain actuarial valuations a few months before the reporting date. This is acceptable if the valuation is adjusted for material subsequent events up to the reporting date. Therefore, companies should consider the timing of their actuarial valuation reports and whether they reflect material events between the valuation and reporting date.

## Impact on Share-Based Payments

Companies with share-based payments whose vesting depends on achieving non-market performance conditions – e.g. earnings per share targets – may need to revise their estimate of the number of instruments expected to vest, which would impact the charge in the income statement over the remaining vesting period. However, expectations of achieving market performance conditions – e.g. achieving a specified total shareholder return and non-vesting conditions – and grant-date fair value are not revised.

Modifications to share-based payment arrangements will need to be assessed as to whether they are either beneficial or non-beneficial to the employee and accounted for accordingly. For example, if plans are modified such that market conditions are easier to achieve, then this may constitute a beneficial modification which increases the value of the award in the hands of the employee. In this case, the incremental fair value is recognised over the modified vesting period.

## Actions for Management to Take Now

- Consider the appropriate accounting for new employee benefit arrangements – e.g. new remuneration policies.
- Assess when to recognize an expense and corresponding liability for termination benefits.
- Update estimates, including actuarial assumptions used to measure employee benefits, as appropriate.
- In preparing interim financial statements, consider the need for updated actuarial valuation reports and whether any plan re-measurements should be recognized.
- For any actuarial valuation reports obtained before the reporting date, consider how to reflect material events occurring between the valuations and reporting dates.
- Update the estimate of the number of awards that will vest for achieving non-market performance conditions in share-based payment arrangements.
- Evaluate whether modifications to share-based payment arrangements are non-beneficial or beneficial.