

Provision for un-encashable portion of Half Pay Leave (HPL) as per AS 15 / Ind AS 19

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

A. Facts of the Case

1. A company (hereinafter referred to as the 'company' or 'corporation') has the following policy towards provision for encashment of Privilege Leaves (PL) and Half Pay Leaves (HPL) as per Accounting Standard (AS) 15 'Employee Benefits' / Indian Accounting Standard (Ind AS) 19, 'Employee Benefits':
 - i. The company's employees are governed by the Industrial DA pay pattern (IDA).
 - ii. As per the rules of the corporation, an employee is eligible for 30 days privilege leaves (PL) in a year and 20 days half pay leaves (HPL) in a year.
 - iii. The privilege leaves (PL) can be accumulated up to the maximum limit of 300 days which are encashable on superannuation.
 - iv. The privilege leaves in excess of 300 days due to the employees are encashable during the service period which is paid to the employees and is directly charged to expenditure under the head salary, wages & benefits.
 - v. Half pay leaves (HPL) are un-encashable during the service period. However, the HPL are encashable on superannuation only to the extent of the privilege leaves to the credit of executives employees falling short of maximum limit of 300 days. The benefit of HPL encashment on superannuation has not been extended to the non-executives employees.

Note: As on 31-03-2017, total employees in the corporation are 1232 consisting of 223 executive employees and 1009 non-executives employees.
- vi. Employee-wise leave balances along with other personal details (executive and non-executive employees) are shared with the actuarial valuer as below:
 - In case of executive employees, PL and HPL up to the maximum limit of 300 days and
 - In case of non-executive employees, only PL up to the maximum limit of 300 days.

Based on the valuation provided from the actuarial valuer, provision is created for leave encashment (PL and HPL).
2. The querist has also stated that the company has adopted Indian Accounting Standards (Ind ASs) w.e.f. 1st April, 2017.

B. Query

3. In view of the above, the querist has sought the opinion of the Expert Advisory Committee as to whether the provision for the un-encashable half pay leaves (whether executives or non-executives employees) should be created similar to the encashable portion as part of cost of services rendered during the period in which the service was rendered which resulted the entitlement.

C. Points considered by the Committee

4. The Committee, while answering the query, has considered only the issue raised in paragraph 3 above and has not examined any other issue that may arise from the Facts of the Case, such as, accounting treatment for privilege leave benefits, classification of half pay leaves as 'short-term' or 'other long-term' employee benefits and their measurement etc. Further, the Committee presumes from the Facts of the Case that the half pay leaves in the extant case can be carried forward and

availed upto the retirement/superannuation of the employees (both executives and non-executives employees).

5. At the outset, the Committee wishes to point out that from an accounting angle, the nature of un-encashable leave is similar to that of the encashable leave insofar as the former provides a right to an employee to receive salaries and wages for the period for which he/she avails leave as during that period he/she does not render any services to the employer. The Committee is of the view that accumulating half pay leave creates an obligation on the enterprise because any unused entitlement increases the employee's entitlement to avail leave in future periods. Thus, a provision should be recognised for all these benefits and recorded as part of the cost of service rendered during the period in which the service was rendered which resulted the entitlement. In this regard, without examining the classification of accumulating half-pay leaves into 'short-term' and 'other long-term' employee benefits, the Committee further notes the following paragraphs of Accounting Standard (AS) 15 'Employee Benefits'/Indian Accounting Standard (Ind AS) 19, 'Employee Benefits', notified under the Companies Rules, 2006/Companies (Indian Accounting Standards) Rules, 2015 as below:

AS 15:

“Short-term Employee Benefits

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;

...”

“Short-term Compensated Absences

11. *An enterprise should recognise the expected cost of short-term employee benefits in the form of compensated absences under paragraph 10 as follows:*

(a) in the case of accumulating compensated absences, when the employees render service that increases their entitlement to future compensated absences; and

(b) in the case of non-accumulating compensated absences, when the absences occur.”

“13. Accumulating compensated absences are those that are carried forward and can be used in future periods if the current period's entitlement is not used in full. Accumulating compensated absences may be either vesting (in other words, employees are entitled to a cash payment for unused entitlement on leaving the enterprise) or non-vesting (when employees are not entitled to a cash payment for unused entitlement on leaving). An obligation arises as employees render service that increases their entitlement to future compensated absences. The obligation exists, and is recognised, even if the compensated absences are non-vesting, although the possibility that employees may leave before they use an accumulated non-vesting entitlement affects the measurement of that obligation.”

“16. Non-accumulating compensated absences do not carry forward: they lapse if the current period's entitlement is not used in full and do not entitle employees to a cash payment for unused entitlement on leaving the enterprise. This is commonly the case for maternity or paternity leave. An enterprise recognises no liability or expense until the time of the absence, because employee service does not increase the amount of the benefit.”

“Other Long-term Employee Benefits

127. Other long-term employee benefits include, for example:

- (a) long-term compensated absences such as long-service or sabbatical leave;

...”

Ind AS 19:

“Short-term employee benefits

- 9 Short-term employee benefits include items such as the following, if expected to be settled wholly before twelve months after the end of the annual reporting period in which the

employees render the related services:

- (a) wages, salaries and social security contributions;
- (b) paid annual leave and paid sick leave;
- ...

“11 When an employee has rendered service to an entity during an accounting period, the entity shall recognise the undiscounted amount of short-term employee benefits expected to be paid in exchange for that service:

- (a) as a liability (accrued expense), after deducting any amount already paid. If the amount already paid exceeds the undiscounted amount of the benefits, an entity shall recognise that excess as an asset (prepaid expense) to the extent that the prepayment will lead to, for example, a reduction in future payments or a cash refund.**
- (b) as an expense, unless another Ind AS requires or permits the inclusion of the benefits in the cost of an asset (see, for example, Ind AS 2, *Inventories*, and Ind AS 16, *Property, Plant and Equipment*).”**

“Short-term paid absences

13 An entity shall recognise the expected cost of short-term employee benefits in the form of paid absences under paragraph 11 as follows:

- (a) in the case of accumulating paid absences, when the employees render service that increases their entitlement to future paid absences.**
- (b) in the case of non-accumulating paid absences, when the absences occur.”**

“15 Accumulating paid absences are those that are carried forward and can be used in future periods if the current period’s entitlement is not used in full. Accumulating paid absences may be either vesting (in other words, employees are entitled to a cash payment for unused entitlement on leaving the entity) or non-vesting (when employees are not entitled to a cash payment for unused entitlement on leaving). An obligation arises as employees render service that increases their entitlement to future paid absences. The

obligation exists, and is recognised, even if the paid absences are non-vesting, although the possibility that employees may leave before they use an accumulated non-vesting entitlement affects the measurement of that obligation.”

“18 Non-accumulating paid absences do not carry forward: they lapse if the current period’s entitlement is not used in full and do not entitle employees to a cash payment for unused entitlement on leaving the entity. This is commonly the case for sick pay (to the extent that unused past entitlement does not increase future entitlement), maternity or paternity leave and paid absences for jury service or military service. An entity recognises no liability or expense until the time of the absence, because employee service does not increase the amount of the benefit.”

“Other long-term employee benefits

153 Other long-term employee benefits include items such as the following, if not expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related service:

- (a) long-term paid absences such as long-service or sabbatical leave;
- ...

From the above, the Committee notes that as per the above-reproduced paragraphs of Accounting Standard (AS) 15, ‘Employee Benefits’/Indian Accounting Standard (Ind AS) 19, ‘Employee Benefits’, obligation exists in respect of short-term accumulating compensated absences irrespective of whether these are vesting or non-



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vesting and is required to be recognised. Similarly, paragraph 13 of AS 15 and paragraph 153 of Ind AS 19 require to provide for a liability in respect of other long-term compensated absences. Accordingly, the Committee is of the view that irrespective of whether accumulating half-pay leaves in the extant case can be classified as 'short-term employee benefits' or as 'other long-term employee benefits', a liability on account of compensated absences should be recognised as per the requirements of AS 15 and Ind AS 19, which should be reviewed at each reporting date to recognise the effects of changes in estimates in this regard.

D. Opinion

6. On the basis of the above, the Committee is of the opinion that irrespective of whether un-encashable accumulating half-pay leaves in the extant case can be classified as 'short-term employee benefits' or as 'other long-term employee benefits', a liability on account of these should be provided as per the requirements of AS 15/Ind AS 19, which should be reviewed at each reporting date to recognise the effects of changes in estimates in this regard, as discussed in paragraph 5 above.

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 Opinion is based on the facts supplied and in the specific circumstances of the querist. The Committee finalised the Opinion on June 5-6, 2018. The Opinion must, therefore, be read in the light of any amendments and/or other developments subsequent to the issuance of Opinion by the Committee.
3.	The Compendium of Opinions containing the Opinions of Expert Advisory Committee has been published in thirty five volumes. A CD of Compendium of Opinions containing thirty five volumes has also been released by the Committee. These are available for sale at the Institute's office at New Delhi and its regional council offices at Mumbai, Chennai, Kolkata and Kanpur.
4.	Recent opinions of the Committee are available on the website of the Institute under the head 'Resources'.
5.	Opinions can be obtained from EAC as per its Advisory Service Rules which are available on the website of the ICAI, under the head 'Resources'. For further information, write to eac@icai.in . ■

