Australian Government
Australian Accounting Standards Board

Staff Paper

Project:	**Not-for-Profit Private Sector Financial Reporting Framework**	**Meeting:**	M185
Topic:	**Tier 3 – Employee Benefits**	**Agenda Item:**	11.3
		Date:	7 February 2022
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Objective of this paper

1 The objective of this staff paper is for the Board to **decide** its preliminary views on Tier 3 reporting requirements for a not-for-profit (NFP) private sector entity's employee benefits for inclusion as part of a discussion paper (DP).

Background and reasons for bringing this paper to the Board

2 At its 4 August 2021 meeting, the Board decided to consider the classification, recognition and measurement requirements concerning employee benefits for NFP private sector entities at a future meeting. Addressing employee benefits as part of a DP recognises the complexity of the accounting requirements in AASB 119 *Employee Benefits* and expects that it is common for a smaller NFP private sector entity to have leave provisions. Developing preliminary views in this regard will help the Board obtain feedback on whether its proposed views should be further developed as part of a future Exposure Draft.

3 The scope of this paper covers the considerations for all employee benefits with a focus on the recognition and measurement requirements (R&M) for short-term employee benefits (i.e. short-term paid absences) and other long-term employee benefits. Stakeholders from previous outreach activities had identified the R&M requirements for short-term paid absences and other long-term employee benefits as the key areas that demand simplification for Tier 3 private sector entities.

4 This paper does not cover defined benefit plans (DBP). Staff noted from previous outreach, DBP is uncommon for private sector entities in Australia. [1] Only a few entities (e.g. public sector entities) still have active DBP.

5 Staff have not addressed related employee benefits disclosures in any detail as part of this paper. Staff think this is contingent on the Board's preliminary view on Tier 3 employee benefits recognition and measurement accounting policies, and in acknowledgement of the discussion paper stage of the Board project. However, staff have assumed that some disclosure about an entity's employee benefits arrangements would be warranted regardless of the Board's decision on employee benefits recognition and measurement policy, for example, the

1 For example, May 2021 NFP Project Advisory Panel (PAP) and outreach activities for IASB ED/2021/3 *Disclosure Requirements in IFRS Standards – A Pilot Approach* which proposed amendments to IAS 19.

amount and nature for each type of employee benefits-related cost and provision occurred during the reporting period.

Structure of this paper

6 This paper is structured as follows:

(a) summary of staff recommendations (paragraph 7);

(b) current requirements under Australian Accounting Standards (paragraphs 8-20);

(c) summary of approaches taken by selected other jurisdictions (paragraphs 21-22);

(d) IASB review of *IFRS for SMEs* (paragraphs 23-23);

(e) feedback from Australian stakeholders (paragraphs 24-26);

(f) findings from academic research and other literature (paragraph 27);

(g) findings from staff review of a sample of financial statements (paragraphs 28-30);

(h) options for simplification (paragraphs 31-34);

(i) possible options and analysis for short-term paid absences (Table 1);

(ii) possible options and analysis for other long-term employee benefits (Table 2);

(i) evaluation of options against the Tier 3 principles (paragraph 35); and

(j) staff recommendations (paragraph 36).

36Summary of staff recommendations

7 Staff recommend that the Tier 3 reporting requirements should require Tier 3 private sector NFP entities to:

- for short-term paid absences (e.g. annual leave), maintain the current recognition requirements[2] with simplified measurement of treating all short-term paid leave obligations as 'current' and measure all short-term paid absence obligations (e.g. annual leave) at their nominal value (i.e. not discounted for the time value of money); and
- for other long-term employee benefits (e.g. long-term paid absences including long-service leave (LSL) and sabbatical leave), retaining the current recognition requirements for other long-term employee benefits[3] but with simplification for measurement to allow Tier 3 NFP private entities to apply the same probability that payment will be required to be paid over the life of the provision, and to use long-term government bonds at the reporting date for PV calculation.

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2 The current R&M requirements for short-term paid absences is recognising the expected cost (undiscounted amount) of an accumulating paid absence when the employee performs a service that increases their right to future paid absences, if the leave provisions are expected to be settled in the next twelve months, otherwise recognising the benefit obligations at the present value (PV) of estimated future cash flow. See paragraphs 10-13 for more details.

3 That current R&M requirement for other long-term employee benefits is recognising the expected cost when the employee performs a service that increases their right to future benefit and the measurement should reflects the probability that payment will be required at the length of time for which payment is expected to be made. See paragraphs 15-16 for more detail.

Current requirements under Australian Accounting Standards

AASB 119 Employee Benefits *– a high-level summary*

General recognition and measurement principle for all employee benefits

8 An entity shall recognise the cost of all employee benefits to its employees who have become entitled as a result of service rendered to the entity during the reporting period:

(a) as a liability, after deducting amounts that have been paid to the employees or as a contribution to an employee benefit (e.g. superannuation) fund. If the amount paid exceeds the obligation arising from service before the reporting date, an entity shall recognise that excess as an asset to the extent that the prepayment will lead to a reduction in future payments or a cash refund.

(b) as an expense, unless another Australian Accounting Standard (AAS) requires the cost to be recognised as part of the cost of an asset such as inventories or property, plant and equipment.

9 For employee benefits that are not expected to be settled wholly before twelve months after the end of the annual reporting period in which the employee renders the related service, an entity shall recognise the benefit obligations at the PV of the estimated future cash outflows made by the employer for services provided by employees up to the reporting date. The discount rate used in the PV calculation is determined by reference to market yields at the end of the reporting period on high-quality corporate bonds (or government bonds for currencies where there is no deep market in such high-quality corporate bonds).

Short-term employee benefits

10 AASB 119 paragraph 8 defines short-term employee benefits as employee benefits (other than termination benefits) that are expected to be settled wholly before twelve months after the end of the annual reporting period in which the employee renders the related service, which includes wages, salaries and social security contributions; paid annual leave and sick leave; profit-sharing and bonuses; and non-monetary benefits (e.g. medical care, housing, cars and free or subsidised goods or services for current employees).

11 Accounting for short-term paid absences depends on whether the leave obligations are accumulating and vesting. The expected cost (undiscounted amount) of an accumulating paid absence is recognised when the employee performs a service that increases their right to future paid absences, regardless of whether the entitlement is vesting or non-vesting. The expected cost of non-accumulating paid absence is recognised when the absences occur (paragraph 13 of AASB 119).

12 A non-vesting entitlement (e.g. sick leave) is only included as a liability at the reporting date if it is probable the entity will be required to pay the employee for the entitlement in the future.[4]

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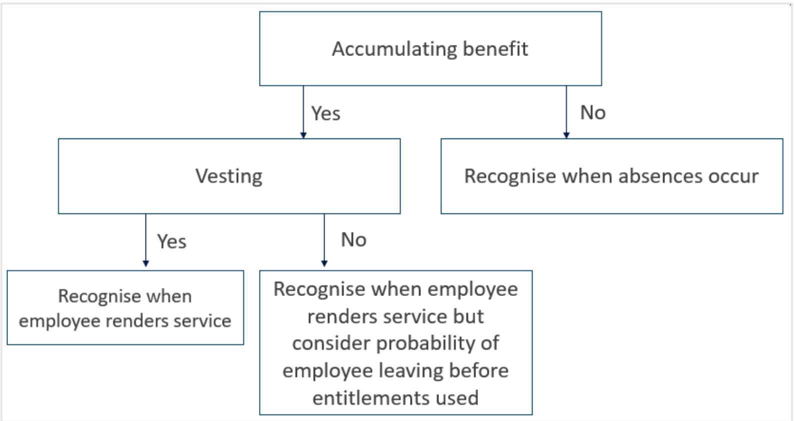
4 There is an assumption in AASB 119 that an employee uses the most-recent sick leave accrued first, and only uses sick leave accrued from previous years if they need more sick leave than their current year entitlement. Therefore, a sick leave obligation is likely to be material only if there is a formal or informal understanding that unused paid sick leave may be taken as paid annual leave (paragraph 17 of AASB 119).

Staff understand that, in Australia, most employees are entitled to accumulating and non-vesting sick leave and generally do not exceed their sick leave entitlements in any one reporting period. As a result, sick leave entitlements are generally not recognized as a liability but recognized as an expense when taken by the employee.

13 The following flowchart summarises when a short-term paid absence should be recognised:



Post-employment benefits (defined contribution plan) – paragraphs 50-52 of AASB 119

14 The general R&M requirements for a defined contribution plan broadly align with the general requirements for all employee benefits (as described in paragraphs 8-9 above).

Other long-term employee benefits – paragraphs 153-157 of AASB 119

15 Other long-term employee benefits refer to all employee benefits other than short-term employee benefits, post-employment benefits and termination benefits, for example, long-term paid absences (e.g. LSL or sabbatical leave); jubilee or other long-service benefits; long-term disability benefits; profit-sharing and bonuses; and deferred remuneration.

16 The general R&M requirements for other long-term employee benefits broadly align with the general requirements for all employee benefits (as described in paragraphs 8-9 above). If the level of benefit depends on the length of service, an obligation arises when the service is rendered. Measurement of that obligation reflects the probability that payment will be required at the length of time for which payment is expected to be made.

Termination benefits– paragraphs 159-170 of AASB 119

17 Termination benefits result from either an entity's decision to terminate employment or an employee's decision to accept an entity's offer of voluntary redundancy.[5]

18 A liability and expense for termination benefits should be recognised at the earlier of a) when the entity can no longer withdraw the offer of those benefits; and b) when the entity recognises costs for a restructuring that is within the scope of AASB 137 *Provisions, Contingent Liabilities and Contingent Assets* and involves the payment of termination benefits.

19 Measurement of a termination benefit depends on when the termination will occur. If payment is expected to be less than twelve months from reporting date, then the liability is calculated based on the nominal value of benefits in the same way as other short-term benefits; otherwise, the liability is calculated by discounting the estimated cash flows in the same way as other long-term benefits.

5 To recognise a liability for termination benefits, an entity must be demonstrably committed to either terminating the employment of employees before their normal retirement date or providing termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits do not include employee benefits resulting from termination of the employment at the employee's request without an entity's offer, or as a result of mandatory retirement arrangements, as those benefits are post-employment benefits.

AASB 1060 General Purpose Financial Statements – Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities – *Tier 2 disclosures*

20 AASB 1060 does not require specific disclosure about short-term employee benefits or other long-term employee benefits. Entities are required to disclose the amount and nature of their obligation for each category of termination benefits and the extent of funding at the reporting date. For defined contribution plans, AASB requires entities to disclose the amount recognised in profit or loss as an expense for defined contribution plans.[6]

Summary of approaches taken by selected other jurisdictions

21 Like AASB 119, several of the jurisdictions analysed for the purposes of this staff paper[7] have the same general principles for all employee benefits as described in paragraphs 8-9 above, with the exception that:

(a) UK Charities SORP requires liability for annual leave and paid sick leave recognised at the amount not discounted for the time value of money (i.e. entities expect employees to take their leave entitlement within twelve months);

(b) New Zealand's PBE SFR – A (NFP) is silent on whether employee benefit liabilities beyond twelve months need to be measured at their PV; and

(c) New Zealand's PBE SFR – A (NFP) and UK Charities SORP have no specific R&M requirements for other long-term employee benefits (e.g. long-service leave). [8]

22 In contrast to AASB 119 and other jurisdictions, Singapore CAS requires details on employee benefits expense (e.g. amount and nature for each type of employee benefits, such as wages, paid leave, termination benefits) shall be disclosed in the notes to financial statements. However, there are no specific R&M requirements for employee benefits-related expenses and provisions. HK SME-FRF & SME-FRS has no specific section on requirements for employee benefits.[9]

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6 AASB 1060 also includes disclosure requirement for defined benefit plans, which are out of scope of this paper.

7 For the purposes of this staff paper, the NFP employee benefits requirements for the following jurisdictions were considered:

(a) International Financial Reporting Standard for Small and Medium-sized Entities (*IFRS for SMEs*).

(b) New Zealand Public Benefit Entity Simple Format Reporting – Accrual (Not-For-Profit) (NZ PBE SFR – A (NFP)).

(c) Financial Reporting Standard 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* (UK FRS 102).

(d) Financial Reporting Standard 105 *The Financial Reporting Standard applicable to the Micro-entities Regime* (UK FRS 105).

(f) Accounting and Reporting by Charities: Statement of Recommended Practice applicable to charities preparing their accounts in accordance with the Financial Reporting Standard applicable in the UK and Republic of Ireland (UK Charities SORP).

(g) Singapore Charities Accounting Standard (Singapore CAS).

(h) Hong Kong Small and Medium-sized Entity Financial Reporting Framework and Financial Reporting Standard (HK SME-FRF & SME-FRS).

8 NZXRB staff confirmed that there is no legal requirement in NZ to recognise LSL. LSL was not considered to be a transaction frequently entered into by smaller NFP entities and therefore no requirements were included in the NZ Tier 3 Standard.

9 Staff noted that HK SME-FRF & SME-FRS includes an illustrative example which suggests that entities may refer to the R&M requirements for Provisions when accounting for employee benefit related obligations.

IASB Review of IFRS for SMEs

23 As part of its second comprehensive review of the *IFRS for SMEs* Standard, the IASB is currently assessing whether to align the *IFRS for SMEs* Standard with IFRS Standards. Staff have not noted any specific comments received or decisions made by the IASB about R&M requirements for short-term paid absences or other long-term employee benefits-related topics.

Feedback from Australian stakeholders

24 Several NFP Project Advisory Panel (PAP) members considered that the requirement to measure certain employee benefits at PV is challenging for Tier 3 NFP entities that may lack the skills to do so. Members suggested that, having regard to the materiality of the balances, Tier 3 reporting requirement should consider allowing Tier 3 NFP entities to measure annual leave obligations at their nominal amounts. In addition, some members observed making probability judgments (for example, when annual leave might be taken) to be challenging for preparers, especially during the COVID-19 pandemic.

25 In the May 2021 meeting, NFP PAP members expressed mixed views on the accounting for paid leave. A member suggested that consideration be given to not requiring entities to recognise personal employee benefit liabilities. A member considered that LSL is unlikely to be material for Tier 3 NFP private sector entities, as employees will often change employers before that entitlement vests. For measurement, a panel member noted their view that LSL should be discounted to PV. A panel member also observed that the ability to port LSL in Victoria adds significant challenges to the liability measurement.

26 In the January 2022 meeting, NFP PAP members provided the following feedback in relation to possible Tier 3 accounting simplification for employee benefits (also described in paragraphs 31-33 below):

(a) For short-term paid leave, PAP members generally supported the option of maintaining the current recognition requirement for short-term paid leave, with simplified measurement of treating all short-term paid absence obligations (e.g. annual leave) as 'current', measured at their nominal value (not discounted for the time value of money). One member commented that this option allows users to assess the going concern and solvency of the entity and provides a better picture of the liabilities that a Tier 3 NFP entity has to their employees.

(b) For other other-term employee benefits, PAP members generally supported the option of retaining the current recognition requirements for other long-term employee benefits but offering simplification for measurement, with some mixed views whether to require long term employee benefits to be discounted or probability calculations.

(i) Many members considered it important to include probability calculations when measuring LSL. This is particularly important for smaller entities funded by grants which may be impacted by a large expenditure (e.g. LSL), and entities may be required to allocate grant funding to match LSL expenditure.

(ii) Some panel members considered that the challenge in recognising LSL for Tier 3 entities is calculating the probability for LSL. One member observed some entities might only recognise LSL provisions when it is confirmed that an employee is entitled to LSL. However, panel members noted that this should not be the correct approach.

(iii) While some members supported the requirement to calculate the PV of future cash flow, a few members considered that PV calculation should not be required as it may not be material when compared to probability calculations which can be material to the entity.

Findings from academic research and other literature

27 Academic research suggests that disclosure about NFP entities' employee benefits-related entitlement would better reflect the entity's financial position.[10] Preparers and auditors who participated in the study have noted the impact of COVID-19 on sick leave and annual leave. These two types of leave are increasingly cumulative and constitute material amounts.

Findings from staff review of a sample of financial statements

28 Staff reviewed a random non-representative sample (20) of the 2020 financial statements of entities with reported revenues between $500,000 – $3 million to understand the prevalence of employee benefit-related provisions by entities of this size.[11] The reviewed financial statements included both general purpose financial statements and those described as special purpose financial statements. The staff findings are summarised below:

Observation (Out of a sample size of 20 financial reports)	**No.**
Entity reports employee benefit related provisions	15
Provision for current leave obligations	15
Annual and other short-term leave	15
Current LSL	8
Provision for non-current leave obligations	9
Non-current annual leave	0
LSL	9
Provision for termination benefits	1
Entity does not recognise any employee-benefit related liabilities	6

29 Fifteen entities appear to apply the R&M requirements in AASB 119 when recognising leave entitlements. Based on the notes to their financial statements, employee provisions for the fifteen entities reported employee benefit-related liabilities, employee benefits have been measured at the amounts expected to be paid when liability is settled. Eight out of nine entities reported non-current leave obligations specified that provisions greater than twelve months were measured at the PV of the estimated future cash outflows to be made for those benefits.

30 The staff reviews could suggest that:

(a) provisions for current leave obligations and LSL are not uncommon for smaller NFP private sector entities;

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10 Gilchrist, J.D., West, A., and Zhang, Y. (2021), *Decision Usefulness: A re-examination of the information needs of non-profit GPFR users*, working paper, presented at the AASB 2021 Research Forum, https://aasb.gov.au/media/5oelznke/rf2021-gilchrist_et_al_decisionusefulnesspaper.pdf

11 The sample GP set is the same as that considered in the September 2021 staff paper on Tier 3 reporting requirements for changes in accounting policies, accounting estimates and errors.

(b) entities normally expect annual leave to be settled within twelve months from the reporting date; and

(c) most of the entities that report LSL appear to be able to calculate the PV of the estimated future cash outflows to be made for those benefits.

These findings should be interpreted with caution due to the limited sample size.

Options for simplification

31 For short-term paid absences, with reference to the flowchart in Agenda Paper 11.1 (Appendix A) for this meeting on approaches to simplification, staff have identified the following options for recognition (and related classification and measurement) simplification for Tier 3 reporting requirements:[12]

(a) **Option 1**: Treat all short-term paid absences as 'non-accumulating', recognising expenses when absences occur, supplemented by disclosure of information about the entity's employee leave entitlements.

(b) **Option 2**: Maintain the current recognition requirement for short-term paid absences, with simplified measurement of treating all short-term paid absences obligations as 'current', measuring all short-term paid absence (e.g. annual leave) obligations at their nominal value (i.e. not discounted for the time value of money).

32 For other long-term employee benefits:

(a) **Option 1**: Treat other long-term employee benefits as an omitted topic for Tier 3 reporting requirements.[13]

(b) **Option 2**: Retain the current recognition requirements for other long-term employee benefits but simplify measurement.

33 Under option 2 for long-term employee benefits, possible simplification for measurement could be:

(a) **Simplification to the probability measurement:**

(i) not requiring Tier 3 NFP private entities to measure the probability that payment will be required to be paid; and

(ii) allowing Tier 3 NFP private entities to apply the same probability that payment will be required to be paid irrespective of years of service.

12 In suggesting these approaches, staff had regard to the Board's approach to simplification as agreed at its August 2021 meeting. Approach 1 and Approach 2 demonstrate simplification in areas of:

(a) recognition and measurement (criteria are less subject to judgement and/or easier to apply);

(b) interpretation (requirements are easier to interpret, as less subject to management discretion); and

(c) understandability (requirements result in reporting outcomes that can be easily understood or explained to users).

13 The Board has previously decided at its 8-9 September 2021 Board meeting to propose that entities in the scope of Tier 3 should apply the requirements of a higher tier of Australian Accounting Standards in full for transactions not covered by the Tier 3 reporting requirements. Refer to minutes of 183rd meeting of the AASB.

(b) **Simplification to the PV calculation**:

(i) calculating the amount of other long-term employee benefits at their nominal value (i.e. not discounted for the time value of money); and

(ii) using long-term government bonds (e.g. 10-year Australian government bonds rate) at the reporting date when calculating the PV.

34 The following tables analyse the options to short-term paid absences (Table 1) and long-term paid leave (Table 2) mooted above. The staff analysis takes into consideration current practice in Australia and international jurisdictions, feedback received from stakeholders, and the findings summarised in paragraphs 21 to 30 above.[14]

14 Staff observe other possible simplification alternatives that the Board could consider. Possible options include simplifying the language of requirements in AASB 119 for Tier 3 entities to improve the clarity and understandability of the Standard; or developing application guidance to assist Tier 3 NFP private sector entities in applying AASB 119 (e.g. a summary table, similar to NZ PBE SFR – A (NFP), that lists when and how to recognise and measure the common types of employee benefits-related expenses and provisions for Tier 3 NFP entities). As this paper focuses on the possible simplification for R&M requirements, staff have not adequately explored these options yet. Pending the Board's further deliberation of the broader NFP financial reporting framework project, staff will further analyse other possible simplification alternatives at a future meeting.

Table 1*: Summary of possible options and analysis for Tier 3 – short-term paid absences*

Possible option for Tier 3 – Recognition criteria	**Support for the Option**	**Arguments against the Option**
Option 1: Treat all short-term paid absences as 'non-accumulating', recognising expenses when absences occur, supplemented by disclosure of information about the entity's employee leave entitlements	• Significantly simplified requirements compared to the existing AASB 119. • Reduces the preparation cost and complexity for preparers as feedback suggest recognising leave obligations, particularly during the COVID-19 pandemic, is challenging for some Tier 3 NFP private sector entities.	• Information reported by entities may lack transparency and fail to provide a complete picture of the entity's underlying financial position (e.g. liabilities are not reflected accurately in the financial statements). • Non-recognition of the leave liability on the balance sheet may represent a loss of important information for users (may need disclosure to offset this). • May lead to unintended legal consequences if some entities misinterpret short-term leave as "non-accumulating" for purposes beyond accounting/reporting. • Will impact the comparability of financial statements against entities in other reporting tiers and possibly create consolidation issues, as this requirement would apply only to entities applying Tier 3 reporting requirements. • No other jurisdiction adopts this approach explicitly, with Singapore CAS and HK SME-FRF & SME-FRS being silent on the R&M for employment benefits.
Option 2: Maintain the current recognition requirement for short-term paid leave, with simplified measurement for treating all short-term paid absences obligations as 'current', measuring all short-term paid absence obligations at their nominal value (not discounted for the time value of money).	• Ensures consistency with the existing recognition requirements under AASB 119 and improves comparability with Tier 1 and Tier 2 entities. • Provides greater transparency and comparability around NFP entities' financial position (in comparison to Option 1) • Annual leave appears to be a common and material obligation for NFP entities, and, therefore, users benefit from more information on them to inform their decision making. • Recognises the challenges in calculating the probability of short-term paid absences to be claimed beyond twelve months and PV for smaller NFP private sector entities. • Removes the complexity in applying AASB 119 as entities do not need to assess the probability and discount rate. • The same approach adopted by the UK Charities SORP	• May reduce information for entities with material short-term paid absences to be claimed beyond twelve months, particularly if the effect of discounting is material.

Table 2 ***Summary of possible options and analysis for Tier 3 – Other long-term employee benefits***

Possible option for Tier 3 – Measurement criteria	Support for the Option	Arguments against the Option
Option 1: Treat other long-term employee benefits as an omitted topic for Tier 3 reporting requirements.[15]	• Reduces the complexity of Tier 3 reporting requirements. Entities with no long-term employee benefits would not need to go through the potentially lengthy requirements. • The same approach adopted by New Zealand's PBE SFR – A (NFP)	• It may be misinterpreted by some entities that there is no need to calculate other long-term employee benefits and lead to unintended legal consequences. • Entities for whom other long-term employee benefit obligations are material have to search for additional guidance or opt up to Tier 1/Tier 2 requirements.
Option 2: Retain the current recognition requirements for other long-term employee benefits but with simplification for measurement	• Ensures consistency with the existing recognition requirements under AASB 119 and improves comparability with Tier 1 and Tier 2 entities. • Reduces the cost of preparation and complexity for preparers to determine the probability or PV of the related obligation (discussed further below for options 2(a) to 2(b)).	• Information reported by entities may lack relevance as estimated future cash flow may not be reflected appropriately if the probability or PV is not calculated (discussed further below for options 2(a) to 2(b)).
As noted in paragraph 33 above, staff think that under Option 2, there is an opportunity for simplification for the measurement for other long-term employee benefits. Rows below analyse the options considered by staff.		
Option 2(a): Simplification to the probability measurement:		
(i) not requiring Tier 3 NFP private entities to measure the probability that payment will be required to be paid	• Simple to apply with no interpretation ambiguity. Removes the apparent complexity in the accounting requirement and reduces the cost of preparing the financial statements (as entities don't need to apply different probability rates by years of service).	• It would not faithfully represent of the entity's long-term employee benefits provisions in its entirety as it ignores the effect of probability completely
(ii) allowing Tier 3 NFP private entities to apply the same probability that payment will be required to be paid irrespective of years of service. No simplification to the calculation of PV.	• Same as the cell above, and • Arguably provides users with relevant information, as it still reflects, at least, an average probability of the provision to be paid. While not as faithfully representative of the entity's long-term employee benefits provision in its entirety, this information may be sufficient for users of Tier 3 financial statements.	• It may compromise the faithful representation of the entity's long-term employee benefits provisions as it ignores the differences in probability over time

15 See footnote 13 on page 8.

Possible option for Tier 3 – Measurement criteria	Support for the Option	Arguments against the Option
Option 2(b): Simplification to the PV calculation:		
(i) calculating the amount of other long-term employee benefits at their nominal value (i.e. not discounted for the time value of money).	• Simple to apply with no interpretation ambiguity. Removes the apparent complexity in the accounting requirement. • Reduces the cost of preparation of the financial statements.	• Information reported by entities would be relevant as estimated future cash flow may not be reflected appropriately if the PV is not calculated, considering the impact of discounting on long-term liabilities can be material. • Not consistent with the measurement requirement for non-current provisions other than employee benefits.
(ii) using long-term government bonds rate (e.g. 10-year Australian government bonds rate) at the reporting date when calculating the PV.	• Same as the cell above, and • Provides users with relevant information, as it still reflects the time value of money using a reasonable discounting rate. • Arguably maintains a reasonable level of consistency with other reporting tiers and R&M requirements for non-current provisions other than employee benefits.	• It may compromise information relevance if corporate bond rate is considered to be more appropriate for some entities.

Evaluation of options against the Tier 3 principles

35 With reference to the flowchart in Agenda Paper 11.1 (Appendix A) for this meeting, in addition to the analysis in the tables above, staff also analysed each of the proposed options against the tentative Tier 3 principles previously agreed to by Board members. Staff consider that the proposed options are broadly equally aligned with the Tier 3 principles, except for those listed below:

Principle	**Discussion**
The development of Tier 3 reporting requirements is subject to the AASB Not-for-profit Standard-Setting Framework Tier 3 financial statements are general purpose financial statements. As such, Tier 3 financial statements provide useful information to users of financial statements.	• Option 1 for short-term paid leave, derecognising annual leave liability on the balance sheet, would represent a loss of important information for users to assess the entity's performance, particularly liquidity risk. • Option 2 (and options 2(a) to 2(b)) for other long-term employee benefits may lack relevance as estimated future cash flow may not be reflected appropriately if the probabilities or PV is not calculated. Consequently, the usefulness and relevance of the information provided in the financial statements would suffer.
Consistency with the accounting principles specified in Tier 2: Australian Accounting Standards – Simplified Disclosures is desirable but might not always be warranted since Tier 3 requirements are being developed as a proportionate response	All of the options discussed above would be unique to Tier 3, which will compromise comparability across different reporting tiers to varying degrees by the level of simplification provided. However, staff think departure may be justified regarding less well-resourced Tier 3 entities that may have difficulties in calculating the probability of short-term paid absences to be claimed beyond twelve months and calculating PV.

Staff recommendations

36 On balance, staff support:

- **Option 2 for short-term paid absences.** That is maintaining the current recognition requirement for short-term paid absences, with simplified measurement of treating all short-term paid absences obligations as 'current' and measuring all short-term paid absence obligations at their nominal value.

  Staff consider that this option is appropriate proportionate responses in recognition of the size of Tier 3 entities that may have resource constraints in assessing the probability of short-term paid absences to be claimed beyond twelve months and calculating the PV of future cash flow.

- **A combination of option 2(a)(ii) and 2(b)(ii) for other long-term employee benefits.** That is retaining the current recognition requirements for other long-term employee benefits but with simplification for measurement to allow Tier 3 NFP private entities to apply the same probability that payment will be required to be paid and to long-term government bonds at the reporting date for PV calculation.

Staff consider that this option is an appropriate proportionate response in recognition of the size of Tier 3 entities that may have resource constraints in assessing the probability of other long-term employee benefits. It avoids interpretation ambiguity, reduces the preparation cost, removes the apparent complexity in accounting requirements while not sacrificing the relevance and usefulness of the financial statements to users. It also maintains a reasonable level of consistency with other reporting tiers and the R&M requirements for non-current provisions other than employee benefits.

Questions for Board members

Question 1: Do Board members support, for the discussion paper, the staff recommendation that Tier 3 reporting requirements maintain the current recognition requirement for short-term paid absences, with simplified measurement of treating all short-term paid absence obligations as 'current' and measuring all obligations (e.g. annual leave) at their nominal value (i.e. not discounted for the time value of money) (Option 2)?

If not, what approach do Board members support?

Question 2: Do Board members support, for the discussion paper, the staff recommendation that Tier 3 reporting requirements for other long-term employee benefits, retain the current recognition requirements but with simplification for measurement (Option 2)?

If not, what approach do Board members support?

Question 3: If Board members agree with the staff recommendation in Q2, do Board members support, for the discussion paper, the staff recommendation that simplifies the measurement requirement for Tier 3 reporting requirements for other long-term employee benefits by allowing Tier 3 NFP private entities:

a) to apply the same probability that payment will be required to be paid irrespective of years of service (Option 2(a)(ii)); and

b) to use long-term government bonds at the reporting date for PV calculation (Option 2(b)(ii)).

If not, what approach do Board members support?