

KSA IFRS CONVERSION

HYPHEN POINTS TO KNOW (PTK) SERIES

ACTUARIAL VALUATION

WHAT'S THE RATIONALE

End of Service Benefit (ESOB) is already recognized in the books of accounts. Why do we need Actuarial Valuation!

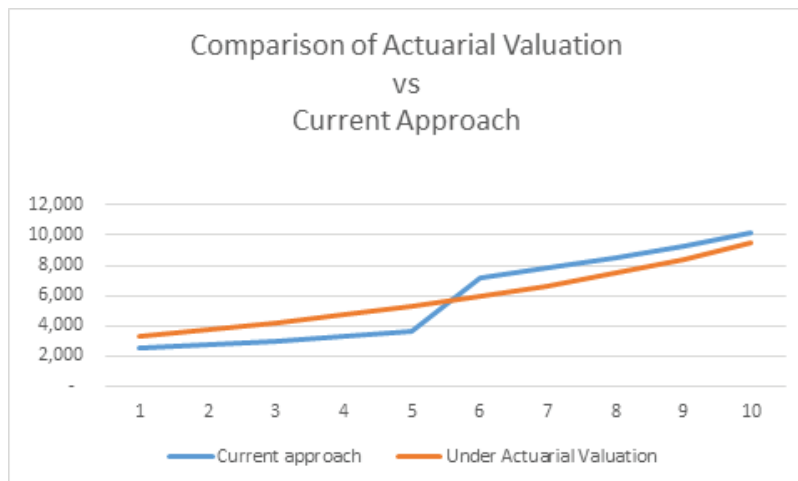
Currently, liability in respect of End of Service Benefits (EOSB) is booked at the reporting date for the number of years employee has worked at that point of time. Under this practice, the impact of future events on current liability is not taken into account as more fully explained below.



WHAT IT ENTAILS

Essentially, actuarial valuation calculates actual amount payable for all the employees in future taking into account the demographic factors (likelihood of termination of employment, retirement, disability, or death at each age) and economic factors (rate of inflation, GDP growth, government regulations etc.). This total amount payable in future is then discounted to reporting date for disclosure in financial statements.

Actuarial valuation effectively results in straight line expense in relation to end of service benefits.



Above graph indicates an employee who joins the entity for the salary of SR 5,000/month (the same to be used for the purposes of calculation of EOSB). Keeping in view the company policies and past history, we expect an employee to continue working for the company for 10 years. Further, the company has a policy of salary increments of @ 5% per annum. The discount rate to be used is 7%.

Graph indicates recognition of higher expense in the first year under actuarial method (same is the case for the entities adopting actuarial valuation for the first time) and then gradual unwinding of the liability. Under "current approach", expense jumps by 97% in the sixth year as the employee's EOSB will now be calculated based on full salary under Saudi Regulations. Whereas, under Actuarial method the expenses is distributed on a straight line basis over a period of 10 years as this effect was already taken into account.



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