



EMPLOYEE BENEFIT VALUATIONS OF  
COMPANIES OUTSIDE INDIA  
CARRIED OUT BY INDIAN ACTUARIES

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CHALLENGES, CONSIDERATIONS AND  
EXPERIENCES

Presenter

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# AGENDA

## 1. Decision to take up the assignment

- \* Source of assignment
- \* Information available
- \* Background checks

## 2. Understanding benefits to be valued

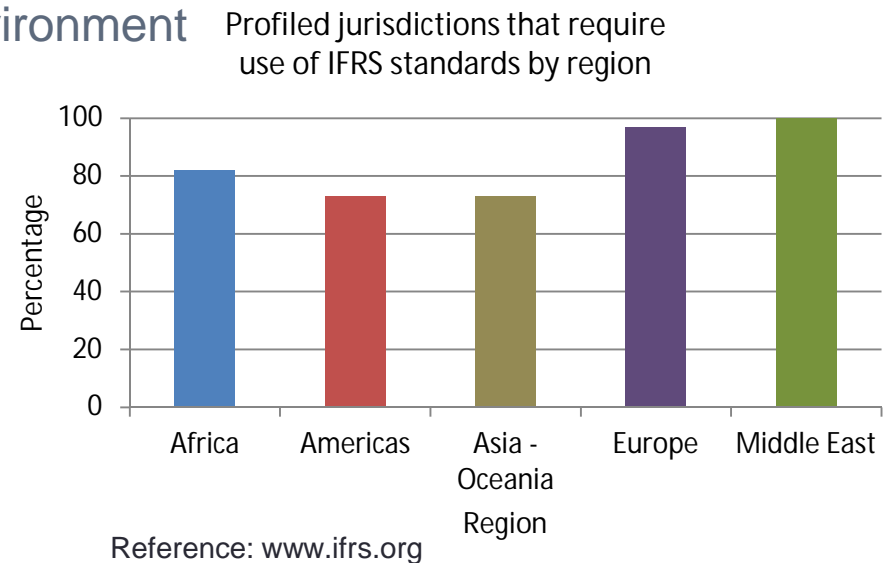
- \* Need of valuation
- \* Common type of plan
- \* Variation in benefits
- \* Nature of termination benefits

## 3. Preparation of results

- \* Data collection
- \* Assumption selection
- \* Other considerations

# WHY VALUATIONS OF COMPANIES OUTSIDE INDIA FAVORABLE FACTORS

- A. Globalization
- B. Widespread adoption of IFRS accounting standard
- C. Ever increasing pressure on public & private sector arrangements:
  - As population across geographies age
  - Low growth\low interest economic environment
  - Multiple favorable pension reforms
- D. Similar benefits in many locations
- E. Limited practitioners at many locations





# 1. Decision to take up Assignment

## DECISIONS TO TAKE UP ASSIGNMENT

### SOURCE OF ASSIGNMENT

India MNC foreign  
subsidiary or JV –  
for India books

Foreign MNC  
subsidiary or JV –  
for local books

Merger &  
Acquisition (M&A) –  
due diligence

- Whether assignment is from our existing client or new client?

Challenges include:

- Understanding overall benefits - e.g. all type of regulatory benefits and practices by local company.
- Availability of necessary plan documents to understand benefits.
- Limited communication channel\window with the local entity.

## **DECISIONS TO TAKE UP ASSIGNMENT INFORMATION AVAILABLE**

- A. Restrictions of advice by regulation, local actuarial society?
- B. Purpose of valuation – Accounting\Funding\Other?
- C. Accounting Standard for reporting?
- D. Is there any language barrier?
- E. Are the benefits actuarially valued by someone else? Will reports of prior actuarial valuation available for this assignment?
- F. Does the company has an internal well laid out rules\terms for there employee benefits?
- G. Timelines sufficient for proper assessment?

## **DECISIONS TO TAKE UP ASSIGNMENT BACKGROUND CHECKS**

- One may want to do a background check on:
  - Company – business activities, serious litigations
  - Country – sanctions, data security laws, outsourcing laws
  - Local laws for remittance and taxes – competitive disadvantage
- Do not want to associate name with entities involved in dubious activities, countries with sanctions etc.
- Why this assignment is discussed with Indian Actuary?



## 2. Understanding benefits to be valued



## UNDERSTANDING BENEFITS TO BE VALUED COMMON TYPE OF PLANS

- Severance Pay
  - Usually payable on exit of employee on conditions other than retirement, death and disability.
  - Commonly employer pays in form of lumpsum to extinguish liability
  - Indemnities only in case of in-voluntary terminations, redundancy exercises may not be require Accounting valuation for long term benefit obligations
- Retirement Indemnity
  - Sometimes refer to DC type retirement savings plan.
  - Plans may offer same benefit as in case other forms of exit like termination.
  - May be less material with countries of young population & high attrition.

# UNDERSTANDING BENEFITS TO BE VALUED

## COMMON TYPE OF PLANS

- Leaves
  - Whether leaves are encashable (service\exit) or can only be availed as holiday
  - How long accrued leaves can be carried forward from current year?
  - Flexible benefits offered to employees in lieu of accumulated leaves
- Pension & PRM
  - DB or DC arrangement
  - Cost sharing arrangement b\w employer\employee
- Long service award
  - Non-Monetary benefits like Appreciation, Plaque, Seniority etc.
- Associated education assistance program

## UNDERSTANDING BENEFITS TO BE VALUED NEED OF AN ACTUARIAL VALUATION

- Sometimes benefit payable may have:
  - Very low probability of occurrence
  - Low cost for employer
- E.g. company practices to give cash award to employees with 25 years of service on retirement. Company operates in an high salary & high attrition environment.
- Although paying benefit is a practice of company and is long term in nature but its obligation may not be material in company financials.
- Materiality discussion should happen with company, auditors to help them decide.

Likelihood of payment

May be	Yes
No	May be

Value of benefit

Decision matrix to decide valuation of a benefit.

## **UNDERSTANDING BENEFITS TO BE VALUED**

### **NATURE OF TERMINATION BENEFIT**

- Regulations of many countries offer different kind of benefits on exit of an employee from company.
- Benefits could vary on an employee reason for termination from company:
  - Voluntary Resignation
  - Involuntary Resignation
- Many regulations cover these benefits with different names:
  - Severance pay
  - Termination indemnity
  - Redundancy package

## **UNDERSTANDING BENEFITS TO BE VALUED**

### **NATURE OF TERMINATION BENEFIT**

- E.g. an employer shall pay severance allowance where an employee has completed 6 months of service and where following conditions apply:
  - ✓ on employee contract termination by company
  - ✓ on employee contract termination due to employer insolvency
  - ✓ on employer inability to pay wages
  - ✓ if employee dies or met physical incapacity in service
- Benefits payable for reasons other than termination on employer discretion (e.g. retirement, death, disability and resignation) will need to be recorded in long term obligation.

## UNDERSTANDING BENEFITS TO BE VALUED

### VARIATION IN BENEFITS

- Variation in benefit on employee nature of exit from company:
  - *Thai companies offer generous benefits on employee retirement compared to resignation. Employees are also offered long service award in form of GOLD!*
- Flexible benefits:
  - *Israel law require companies to offer both DB & DC benefits. Employees who opts for DC benefit see accumulation of DB benefit at lower rate.*
- Variation in salary definition for benefit amount:
  - *US tax laws mandate employers to limit maximum wages to be considered for pension benefits for schemes eligible for tax-rebates. Companies can offer separate schemes allowing unlimited wages (for executives).*
  - *Similarly there are cap(s) on maximum benefit payable to an employees.*
- Any non-discriminatory regulations needs to be considered in valuation.



## 3. Preparation of Results

## PREPARATION OF RESULTS

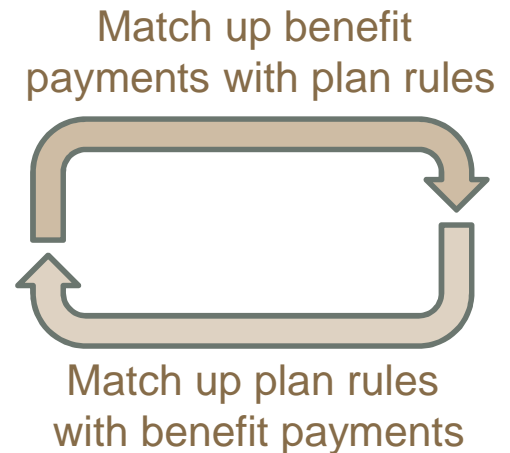
### DATA COLLECTION PROCESS

- Actuary could face challenges in collecting correct information for valuation.
    - Indirect communication
    - Language
    - Understanding gap on benefit practice
  - Pitfalls
    - Salary – CTC\Gross vs. Salary for benefit
    - Scheme Membership date vs hire date
    - Participating members – deferred, retirees etc.
    - Treatment of Partial payments\*
    - Denomination Currency
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- South Korea severance payment laws allow an individual withdraw accrued benefit partially in service.



## PREPARATION OF RESULTS DATA COLLECTION PROCESS

- Quality of data
  - Is the purpose of valuation beyond financial reporting
    - Benefit statements to members
    - Member details to regulator
- Strategy
  - Engage client in active discussions.
  - Discuss & disclose any assumptions made on data.
  - Validate individual benefit payments made in fiscal year against your calculation.

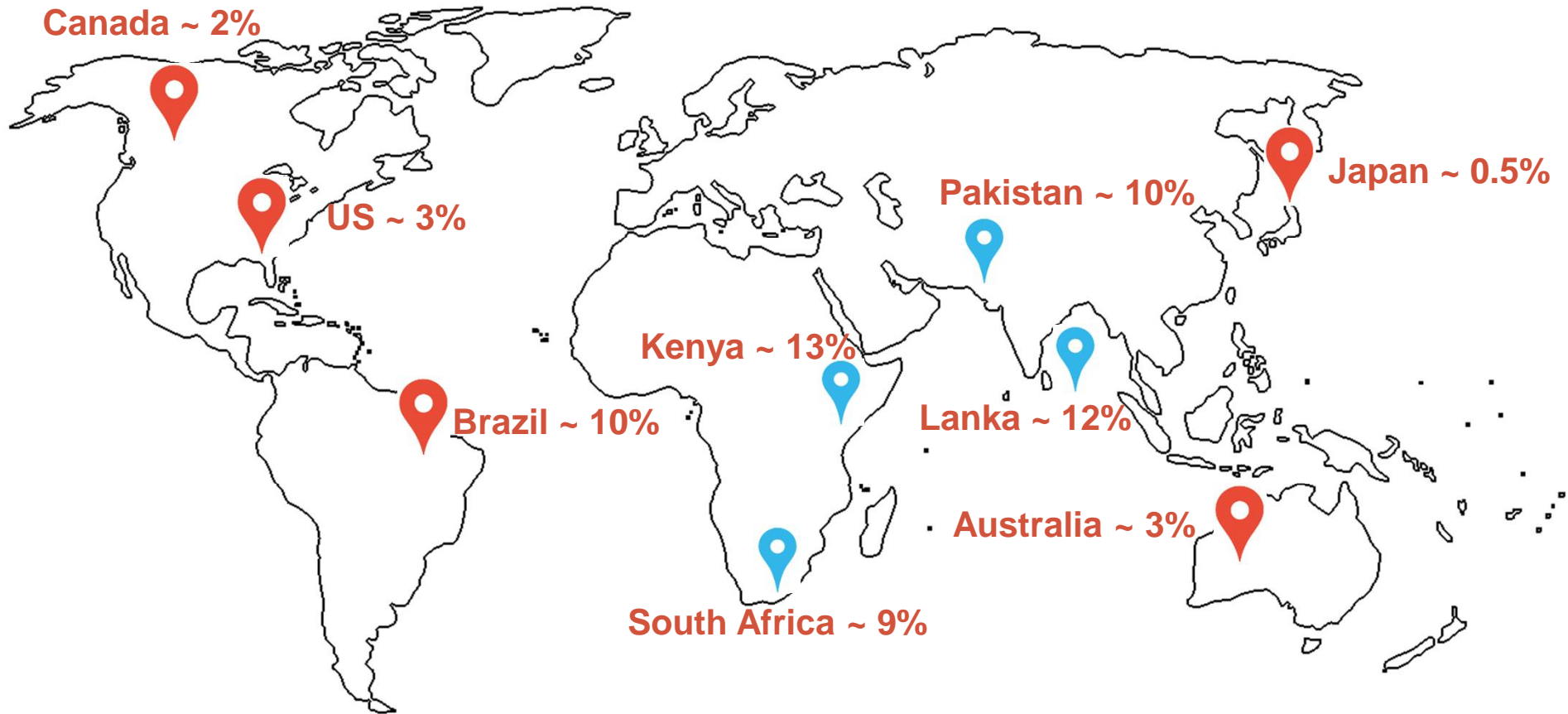


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- Columbia pension plan reporting requires submission of details of members to pension regulator

# PREPARATION OF RESULTS

## DISCOUNT RATE SELECTION

Government bond yields around the world



 - Countries with deep bond market

 - Countries w/o deep bond market

## PREPARATION OF RESULTS

### DISCOUNT RATE SELECTION

- IFRS recommend discount rate selection on high quality Corporate bonds denominated in local currency.
- Not many countries have active & deep Corporate bond market
  - Rely on Government bond yields
- Some countries even do not have active Government bond market
- Discount rate selection may be derived from:
  - Yields of latest issue of Government bonds
  - Yields predicted in World Bank\IMF reports for country
  - Inflation (risk free rate) plus risk premium

## PREPARATION OF RESULTS

### MORTALITY\ MORBIDITY RATE SELECTION

- Selection of Mortality \ Morbidity rates should be in line with local country regulatory &\or professional practice.
- Many developing\ under developed nations do not have sufficient studies on non-annuitant, annuitant mortality and morbidity rates.
- Challenges could be appropriate selection for:
  - Improvement in future mortality.
  - Cohort effect
  - Non-Annuitant mortality vs. overall population statistics
- Assumes more significance in cases like long term annuity payments, low attrition rate environment.

## PREPARATION OF RESULTS

### MORTALITY\ MORBIDITY RATE SELECTION

- Research on appropriate table selection becomes important.
  - Reference from local or other Actuarial society  
<http://mort.soa.org/>
  - Reference from local country listed companies published accounts on employee benefits
  - Guidance and recommendation from local Actuarial society.
  - Use of appropriate, prudent, justifiable adjustments to tables from other related countries.

## PREPARATION OF RESULTS

### REASONABILITY OF ASSUMPTIONS

- Many accounting standards require Actuary to comment on reasonability of assumptions.
- Actuary should be comfortable with assumptions selected by company and should evaluate them on:
  - Inflation\interest rates
  - Local market trends
- Useful source of information:
  - World Bank reports
  - IMF reports
  - Local Government reports

## **PREPARATION OF RESULTS**

### **ACCOUNTING METHOD**

- Most accounting standards permit use of Project Unit Credit method for valuation.
- Some standards require additional information;
  - USGAAP require reporting of Accumulated benefit obligation.
- Treatment of benefit cap, future inflationary increases in benefit may have guiding principles from local Accounting standard or Actuarial body.
- Important to keep consistency if the assignment require reporting under International standard.

## PREPARATION OF RESULTS

### OTHER CONSIDERATIONS

- Asset ceiling
  - Concept of asset ceiling more prominent in geographies with mandated asset backed liabilities.
  - Regulated may limited access of surplus or mandate minimum contributions towards schemes.
- Reimbursement rights
  - Insured Benefits by employer may lead to reimbursement rights
- Reporting to
  - Regulator – certifying scheme financial health
  - Members, auditors – statement quality data
  - Buyer\Seller



## **PREPARATION OF RESULTS**

### **OTHER CONSIDERATIONS**

- Benefits of beneficiaries in scheme – Spouse, Children, dependents.
  - Difficult to collect data and make assumptions
  - May unearth significant portion of liability for employer
- Good practice to disclose
  - Detailed description of benefit understanding
  - Approach used in discount rate selection
  - Caveats on scheme membership data used
- Pricing the project
  - Research required for information
  - Risks associated with project – professional, reputational
  - Level of interaction involved with stakeholders

## SUMMARY

- Valuation of employee benefits of other geographies is a promising opportunity to explore.
- Actuary should consider to fully understand the Accounting, Regulatory, Local practice requirements in this work.
- Active communication with client, auditors would be important to understand benefits\practices, discuss significance of benefits, assumptions etc.
- Additional checks on employee data, reasonability of assumptions and method used for valuation will be required by the Actuary.
- Practicing Actuaries should look to add detailed commentary on understanding, observations and caveats in reports.



Thank You!