

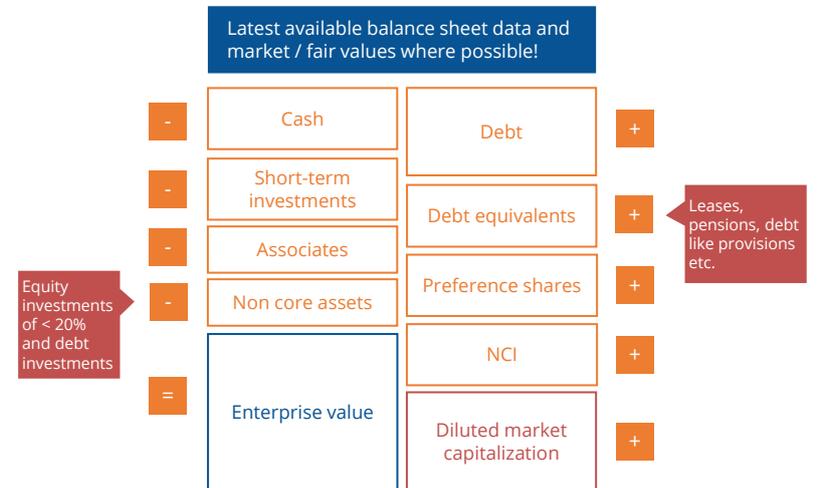


## Contents

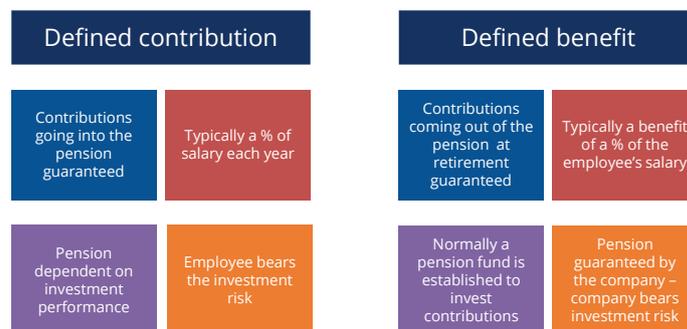
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- Types of pension scheme
- Pension accounting mechanics
- Pensions in valuation
- Cash and credit implications

## Value – Equity to Enterprise Value Bridge

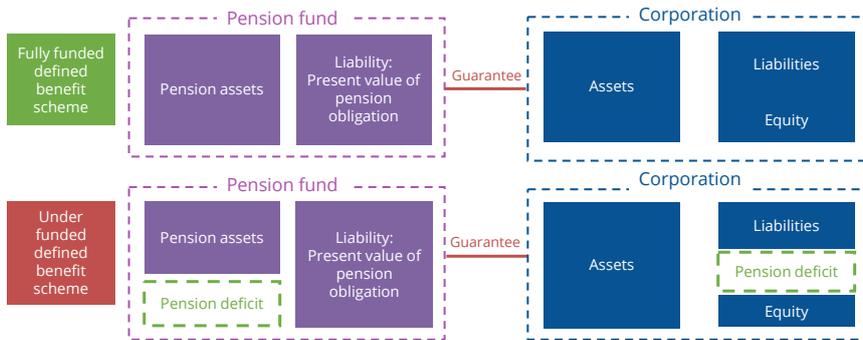


## Defined Contribution vs Benefit Plans



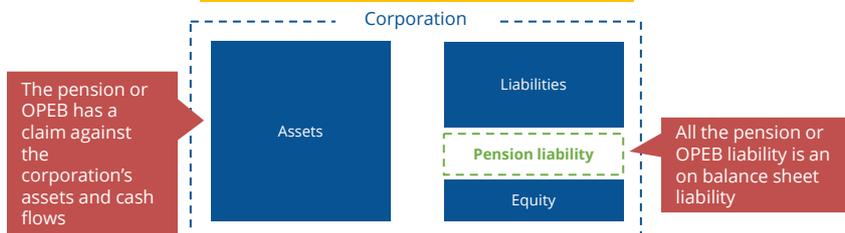
## Funded and Underfunded Plans

Most countries require defined benefit plans to have a pension fund



## Unfunded Schemes

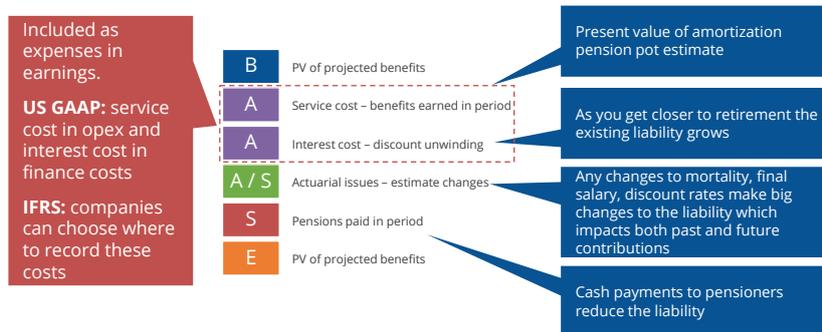
Other Post Employment Benefits (OPEBs) often unfunded as are pension schemes in Germany



## Mechanics of the Accounting – Service Cost

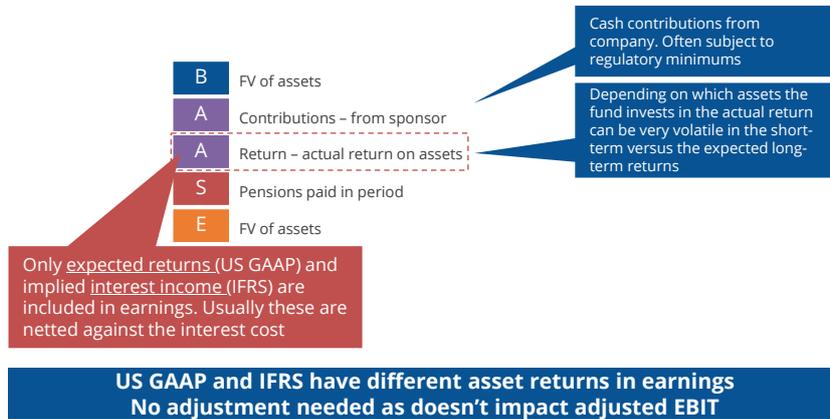
Pension payment based on 60% of final salary  Pension pot required at retirement  Simple straight-line amortization of the pension pot  Each year amortization discounted by the number of years remaining	Retirement age	65.0	Service cost calculation			
	Mortality	80.0	Pension	PV of	Discount	
	Discount rate	4.0%	amort.	amort.	Year	
	Final salary estimate	100.0		133.4	114.0	4.0
	% final salary	60.0%		133.4	118.6	3.0
	Pension payment each year at retirement	60.0		133.4	123.3	2.0
	PV of annuity at retirement	667.0		133.4	128.3	1.0
	Age now (for simplicity calc. only for 5 years)	60.0		133.4	133.4	0.0

## Mechanics of the Accounting – Projected Benefit Obligation

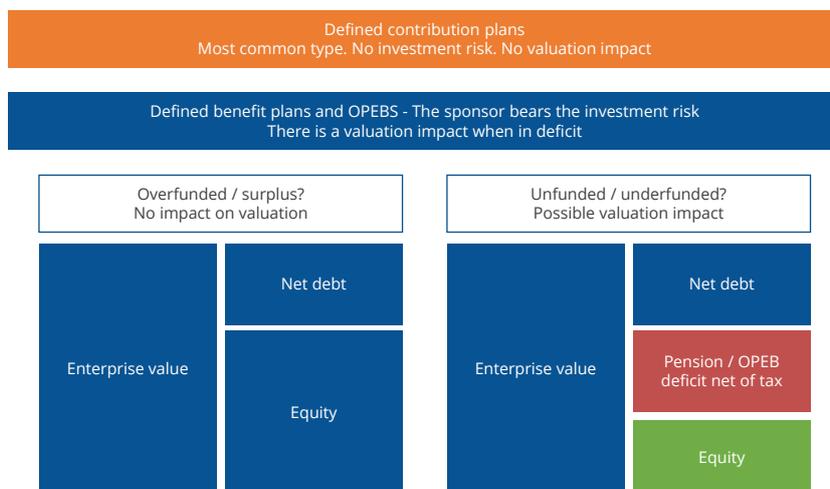


**Only the service cost is a 'real' operating cost**  
**We need to check whether to adjust EBIT for IFRS companies**

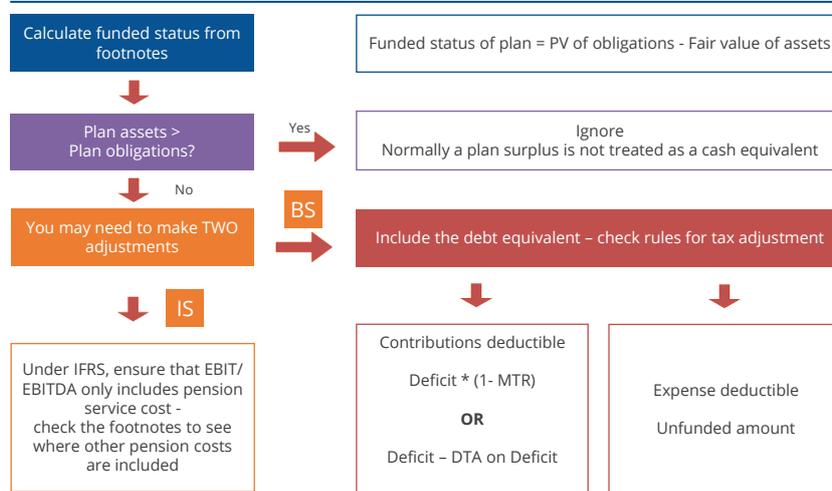
## Mechanics of the Accounting – Plan Assets



## Pensions and OPEBs – Valuation Adjustments



## Pensions and OPEBs – Valuation Adjustments



## Pensions and OPEBs – BS Information

**Funded status = Projected benefit obligations - Value of plan assets**

Funded Status				
End of year	\$ (5,892)	\$ (6,772)	\$ (22,463)	\$ (24,662)

All pension and other post employment benefits numbers are embedded in several balance sheet line items and detailed in the footnotes

At December 31,	Pension		Health Care and Life	
	2015	2014	2015	2014
<b>Amounts recognized on the balance sheet</b>				
Noncurrent assets	\$ 349	\$ 337	\$ -	\$ -
Current liabilities	(93)	(122)	(695)	(528)
Noncurrent liabilities	(6,148)	(6,987)	(21,768)	(24,134)
<b>Total</b>	<b>\$ (5,892)</b>	<b>\$ (6,772)</b>	<b>\$ (22,463)</b>	<b>\$ (24,662)</b>
Long-term debt			103,705	110,536
Employee benefit obligations			29,957	33,280
Deferred income taxes			45,484	41,563
Non-current liabilities related to assets held for sale			959	-
Other liabilities			11,641	5,574

**The balance sheet is often confusing: 22,463 + 5,892 ≠ 29,957**  
**The footnotes are normally much easier to use**

# US GAAP Valuation Adjustment

Calculate debt equivalent value using footnotes

Year Ended December 31, 2019			
	Pension Benefits		Global OPEB Plans
	U.S.	Non-U.S.	
Ending benefit obligation	64,684	21,398	6,304
Ending fair value of plan assets	59,239	14,961	
Ending funded status	\$ (5,445)	\$ (6,437)	\$ (6,304)

Deferred tax assets		December 31, 2019
Postretirement benefits other than pensions		1,695
Pension and other employee benefit plans		2,968

Pension and OPEB Valuation Adjustment				
	Pensions (US)	Pensions (non-US)	OPEBs	Total
Obligation	64,684.0	21,398.0	6,304.0	92,386.0
Plan assets	59,239.0	14,961.0	0.0	74,200.0
Deficit	(5,445.0)	(6,437.0)	(6,304.0)	(18,186.0)
Tax adjustment (1,695 + 2,968)				4,663.0
Debt equivalent				(13,523.0)

# IFRS Valuation Adjustments

Calculate debt equivalent value using footnotes and check whether EBIT needs adjusting

2020			
At 31 March	Assets	Liabilities	Deficit <sup>a</sup>
	Em	Em	Em
BTPS	52,240	(53,010)	(770)
EEPS	820	(879)	(59)
Other plans <sup>b</sup>	411	(722)	(311)
<b>Retirement Benefit Obligations (gross of tax)</b>	<b>53,471</b>	<b>(64,611)</b>	<b>(11,140)</b>
Deferred tax asset			175
<b>Retirement Benefit Obligations (net of tax)</b>			<b>(965)</b>

Pension and OPEB Valuation Adjustment				
	BTPS	EEPS	Other Plans	Total
Obligation	53,010.0	879.0	722.0	54,611.0
Plan assets	52,240.0	820.0	411.0	53,471.0
Deficit	(770.0)	(59.0)	(311.0)	(1,140.0)
Tax adjustment				175.0
Debt equivalent				(965.0)

Year ended 31 March		2020
		Em
Operating loss		328
Net finance expense		
Interest expense on retirement benefit obligation		145
Interest on spectrum annual license fee refund		(5)
		140
Year ended 31 March		2020
		Em
Recognised in the income statement before specific items		
- Service cost (including administration expenses and PPF levy)		86
- Defined benefit plans		540
- Defined contribution plans		-
- First service credit <sup>c</sup>		-
Subtotal		626
Recognised in the income statement as specific items (note 9)		
- Costs to close BT Pension Scheme and provide transition payments <sup>d</sup> for affected employees		22
- Cost to equalise benefits between men and women <sup>e</sup>		-
- Net interest expense on pensions deficit included in specific items		145
Subtotal		167
<b>Total recognised in the income statement</b>		<b>793</b>

## OPEBs Versus Pensions Ranking

Pensions		Other Post Employment Benefits	
Pension for retirement	Typically a senior liability – and often need regulatory approvals in acquisitions / restructuring	Typically healthcare benefits at retirement	Usually a subordinated liability – treat as a general creditor in debt restructuring, as debt for valuation
In most countries must be funded (some exceptions e.g. Germany)	Usually, a minimum cash payment must be made to the fund each year	Many companies don't fund OPEBs. More common in US where healthcare costs are significant	No minimum payments, but the liability is senior to shareholders so must be deducted from EV