

Policies and Procedures

Policy: 2013-01 | Title: Accounting for Employee Termination Costs



Financial

1.0 PURPOSE

The purpose of this policy is to ensure that all actions to terminate employees are preapproved by BCO Senior Management and that the accounting for these actions is in accordance with U.S. GAAP.

2.0 SUMMARY

2.1 Policy Cross-reference

Material transactions that fall under this policy must also comply with the *Communication of Material Transactions* policy.

2.2 Senior Management Approval

Severance and restructuring plans in which aggregate payments are expected to be in excess of \$100,000 are required to be documented on the "Severance/Restructuring Action Approval Form" attached as an exhibit to this policy. Completed forms must be submitted to the BCO Chief Financial Officer and Chief Human Resources Officer for review and approval.

2.3 Accounting

The cost to terminate an employee (or a group of employees) may include severance payments, related payroll taxes, other social charges, job placement services, and other types of costs.

The timing of the recognition of these costs depends on the type of termination benefit arrangement that is involved. A single termination action may involve more than one type of arrangement, which means some of the costs may be recognized in different accounting periods for a single action.

The facts of the benefit plans, laws, or contracts in place, as well as the terms of the contemplated severance actions, will need to be analyzed to determine the appropriate accounting treatment. For example:

1. Are there vesting benefits? If so, then those benefits should likely be accrued during the employee's service period.

Example of a single action that involves more than one arrangement. A terminated employee is

1. legally owed continued employment for a period of time after they have been notified of being terminated, PLUS
2. owed severance payments based on formulas known to the employee (i.e., under a union contract, employee contract, a local law or a local custom), PLUS
3. owed an 'extra' amount that exceeds the legal or contractual amounts owed based on individual negotiations, company plan, or union contract.

The benefits may be accrued in different periods.

Policies and Procedures

Policy: 2013-01 | Title: Accounting for Employee Termination Costs



Financial

2. For benefits that do not vest, are they owed under an existing plan or contract? If so, then those benefits should be accrued when probable of being paid and estimable.
3. Under the proposed action plan, will employees volunteer for termination to receive benefits? If so, then the accrual should be recorded when the employees volunteer for termination.
4. Are there special benefits (i.e., a sweetener to the normal plan) to be paid in addition to the normal benefits to be paid? The special benefits should only be recorded when the employee has been notified (note that the normal benefits may need to be accrued sooner).

3.0 ACCOUNTING METHOD FOR EACH TYPE OF EMPLOYEE TERMINATION BENEFIT ARRANGEMENT

Types of arrangements. The types of employee termination benefit arrangements are:

1. Vesting benefits (employee receives benefits at termination even if they quit)
2. Non-vesting (employee does not receive benefits if they quit)
 1. Ongoing termination benefit arrangement
 2. Contractual termination benefit
 3. Special termination benefit
 4. One-time termination benefit arrangement

3.1 Vesting Benefits

Certain countries have laws that provide employees with termination benefits that vest. Benefits that are "vested" means that the employee is guaranteed to receive the benefits when they leave the company, even if they quit. The laws / contracts generally require that the employee work for the company for a minimum period before the benefits vest. Collective bargaining agreements may extend the amount of benefits beyond the levels required by law. Some countries require that these benefits be funded by employers.

Accounting. These plans are accounted for under post-employment or pension benefit accounting rules. Actuaries may be required to perform calculations. Please consult Corporate Accounting if you have an employee termination benefit arrangement that vests.

Example of Vesting Termination Benefit. The law in a country requires that a minimum severance of one month's salary per year of service is owed to an employee when they leave the company, as long as they have completed one year of service. An actuary would be required to estimate the amount of obligation to be accrued under postemployment or pension US GAAP rules.

Policies and Procedures

Policy: 2013-01 | Title: Accounting for Employee Termination Costs



Financial

3.2 Non-Vesting Benefits

3.2.1 Ongoing Termination Benefit Arrangement

Ongoing termination benefit arrangements are the most common severance plan category. Ongoing termination benefit arrangements include those severance costs owed to terminated employees pursuant to:

1. Existing laws and regulations within a country or jurisdiction,
2. Existing terms of a collectively bargained contractual agreement where the union is not required to accept or approve the plan prior to implementation,
3. A written human resources plan,
4. An unwritten human resources plan where the entity has a past history of providing similar termination benefits.

Unwritten plans. If an entity has a history of providing similar benefits to employees who were involuntarily terminated, the benefits are presumed to be part of an ongoing benefit arrangement unless there is evidence to the contrary. For example, if a company has historically paid 1 week per year of service to terminated employees, this likely is an ongoing benefit arrangement even though there is no written plan.

Accounting. For termination benefits related to an ongoing arrangement, the liability should be recognized when the loss is probable and the amount can be reasonably estimated. For planned headcount reductions triggering termination benefits under an ongoing arrangement, the termination is deemed probable and estimable if the plan for terminations meets the following criteria:

1. Management, having the authority to approve the action, commits to a plan of termination.
2. The plan identifies the number of employees to be terminated, their job classifications or functions and their locations, and the expected completion date.

Q. Are severance actions contemplated in the development of next year's annual operating plan sufficiently 'probable and estimable' at the point the operating plan is approved by Regional and Corporate management?

A. Usually not. In most cases the status of the severance action is too preliminary to be considered probable and estimable and thus an accrual for the costs should not be recorded in the general ledger at the point the operating plan is approved. Please consult with corporate accounting if you believe you have met the criteria.

Policies and Procedures

Policy: 2013-01 | Title: Accounting for Employee Termination Costs



Financial

3. The plan establishes the terms of the benefit arrangement, including the benefits that employees will receive upon termination (including but not limited to cash payments) in sufficient detail to enable employees to determine the type and amount of benefits they will receive if they are involuntarily terminated.
4. Actions required to complete the plan indicate it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

Direct communication of the terms of the plan to employees is not required for recognition of a liability related to an ongoing termination benefit arrangement.

3.2.2 Contractual Termination Benefit

A contractual termination benefit is a benefit that is payable under an employee contract.

Accounting. Severance expense should be accrued when the termination benefit is probable of occurring and the amount of the benefit can be estimated.

3.2.3 Special Termination Benefits

Special termination benefits are benefits offered to employees for a short period of time in exchange for the voluntary termination of service.

Accounting. For special termination benefits such as those described above, the company shall only recognize the expense and related liability when the affected employee accepts the offer. It is not appropriate to estimate the number of employees who will accept the special termination benefits and record an estimated liability prior to actual acceptance of the offer. Some or all of the benefits may need to be accounted for as a pension benefit.

Example: Contractual Termination Benefit. An employee has an employment contract which provides a specific termination benefit if terminated. Management determines to terminate employee.

The termination benefit shall be recognized as an expense and liability in the period in which the employee's termination becomes probable and the amount of the benefit can be reasonably estimated. The accrual may need to be recognized prior to the employee being informed of the action.

Example: Special Termination Benefit. A company offers an early-retirement package to employees that have 10 years of service and are 50 years or older. The package offered includes a lump-sum payment or monthly payments over a period of time. The employees are not required to accept the offer and may continue working for the company. The special benefits are in addition to benefits to be paid under the company's ongoing termination benefit arrangements.



Please contact Corporate Accounting if you have or intend to offer special termination benefits.

3.2.4 One-time Termination Benefit Arrangement

A one-time termination benefit generally applies only for a specified termination event or for a specified future period and is not, in substance, part of an ongoing termination benefit arrangement.

Accounting. One-time termination benefits should be accrued when the obligation is probable and estimable and the employee has been notified. For a one-time termination benefit, communication to the affected employees is also required in order to meet the threshold for recognition of the liability.

A liability should be recognized for one-time benefit arrangements if the plan meets the following criteria:

1. Management, having the authority to approve the action, commits to a plan of termination.
2. The plan identifies the number of employees to be terminated, their job classifications or functions and their locations, and the expected completion date.
3. The plan establishes the terms of the benefit arrangement, including the benefits that employees will receive upon termination (including but not limited to cash payments) in sufficient detail to enable employees to determine the type and amount of benefits they will receive if they are involuntarily terminated.
4. Actions required to complete the plan indicate it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.
5. The planned terminations and benefits have been communicated to the affected employees.

Example: One-time Termination Benefit Arrangement. *A company has an existing ongoing arrangement that pays termination benefits equal to one week of salary per year of service. The company closes a specific branch and offers two weeks of salary per year of service for each employee involuntarily terminated due to the branch closing. If the company intends to return to its written plan (i.e., one week's salary per service year) for all future termination events, the incremental one week of salary per service year for this specific branch closing would qualify as a one-time termination benefit arrangement. See Example 2 at Exhibit B*

Policies and Procedures

Policy: 2013-01 | Title: Accounting for Employee Termination Costs



Financial

It is noted that the first four criteria for meeting the probable and estimable threshold for one-time termination benefits are the same four criteria for ongoing termination benefit arrangements.

It is expected that one-time termination benefits will be **infrequent** given that termination benefits under a substantive plan (as required by law or historical severance payments) would qualify as an ongoing benefit arrangement.

4.0 ACCRUALS FOR TERMINATIONS PROJECTED BEYOND SIX MONTHS IN THE FUTURE NEED BCO CONTROLLER APPROVAL

The accounting for termination benefits that do not vest requires that the cost be probable and estimable. History has shown that severance actions projected in the longer term are less likely to occur as a result of either plans changing and / or the company finding alternative positions to place employees previously expected to be terminated. As a result, no accrual should be made for terminations that are not expected to begin within the next six months, without approval from the BCO Controller.

5.0 RECORDING TERMINATION BENEFITS IN HFM

For termination benefits related to ongoing termination benefit arrangements, contractual termination benefits, special termination benefits and one-time termination benefit arrangements, the ledger accounts that should be used to accrue severance and other related costs in Hyperion Financial Management (HFM) are:

- **6000_135-Severance** should be debited to record expenses related to direct labor and branch personnel severance costs.
- **7000_135-Severance** should be debited to record expenses related to General and Administrative personnel severance costs.
- **2040_170-Accrued Labor Termination/Severance** should be credited to record a current liability for severance.

For termination benefits that are accounted for as a post-employment or pension plan, please consult with Corporate Accounting for method of selecting actuarial assumptions, which HFM accounts to use, periodic remeasurement entries (usually at fiscal year-end) as well as providing monthly accounting entries to record service cost, interest cost and amortization of actuarial gains/losses.

Policies and Procedures

Policy: 2013-01 | Title: Accounting for Employee Termination Costs



Financial

6.0 EFFECTIVE DATE

This guidance is effective for all severance or restructuring plans entered into on or after September 30, 2013.

EXHIBIT A – Severance/Restructuring Action Approval Form



Severance
Restructuring Actions

EXHIBIT B – ACCOUNTING EXAMPLES

Example 1. Ongoing termination benefit arrangement

The company plans a reduction in force. The laws of the country provide that upon an involuntary termination of employment (for any reason other than cause), each terminated employee will receive one week of severance pay for every year of service. The employees have been identified and the expected completion date is the minimum notification period required by law of 90 days. The plan has been approved by the local General Manager and by BCO Senior Management as of June 30, no further approvals are required, and the plan is not expected to change.

In this example the legal benefit is an ongoing termination benefit arrangement that should be accrued when the plan is approved, since the amount is probable and reasonably estimable at that time. No communication to affected employees is required since this is an ongoing plan in which benefit levels are known by the employees. The estimated termination benefit at June 30 was \$500,000.

Entry at June 30:

Dr 6000_135 Severance	\$500,000	
		Cr 2040_170-Accrued Labor Termination/Severance
		\$500,000

To accrue termination benefit required by law as of plan approval

Note: It is not appropriate to delay the formal approval of severance actions with the intention of delaying the recognition of expense. Actions that are formally

Policies and Procedures

Policy: 2013-01 | Title: Accounting for Employee Termination Costs



Financial

approved shortly after balance sheet dates should be scrutinized to ensure valid pending considerations prevented the approval from occurring prior to balance sheet date. A memo should document the status at the balance sheet date if terminations are approved after a quarterly balance sheet date but before the issuance of BCO consolidated financial statements.

Example 2. Combined ongoing and one-time termination benefit arrangement

Assume the same facts as Example 1, except that, due to negotiations with the union in that country, the Company has decided to pay two weeks of severance pay for every year of service. The additional week of payment was not approved by both parties until July 15, and communication to the employees occurred within one day of the agreement. The Company does not expect that this level of benefit will be provided to employees in the future and is isolated to this specific negotiation with the union. In this case, the entry in Example 1 above would be recorded at June 30 as this is the portion of the benefit that is considered part of an ongoing termination benefit arrangement and no communication is required for accrual. The amount related to the additional week provided would be considered a one-time termination benefit arrangement. Therefore, the accrual would be made once communication to the employees has occurred.

Entry at June 30:

Dr 6000_135 Severance	\$500,000	
		Cr 2040_170-Accrued Labor Termination/Severance
		\$500,000

To accrue ongoing termination benefit required by law as of plan approval

Entry at July 31:

Dr 6000_135 Severance	\$500,000	
		Cr 2040_170-Accrued Labor Termination/Severance
		\$500,000

To accrue one-time termination benefit after communication to the employees has occurred

Example 3. Contractual termination benefits

A company has individual employment contracts with its four top officers. These employment contracts provide for termination benefits in the event of involuntary or voluntary termination after a change in control (i.e., the company is sold to a new majority owner). The termination benefits include salary continuation, acceleration of

Policies and Procedures

Policy: 2013-01 | Title: Accounting for Employee Termination Costs



Financial

long-term incentive compensation, and job placement benefits. The total value of the termination benefits for all four officers combined equals \$2,000,000.

On June 1, the company's Board of Directors meets to discuss a third party offer to acquire a controlling interest in the company. On that date, the Board agrees in principle with the terms for the sale of the company including a proposed closing date for the sale transaction of August 1. Only perfunctory conditions are required to be met for the deal to be signed and completed on August 1 and, at June 30, the sale of the company is deemed probable of occurring and it is known that each of the top four officers will be terminated after the change in control.

Because the event giving rise to the contractual termination benefit, the termination of the officers upon a sale of the company, is probable of occurring as of June 30, an accrual should be recognized at that date.

Entry at June 30:

Dr 7000_135 Severance	\$2,000,000	
		Cr 2040_170-Accrued Labor Termination/Severance
		\$2,000,000

To accrue contractual termination benefit for probable change in control

Example 4. Special termination benefits

On November 30, a company offers special voluntary termination benefits to a group of 50 employees. The special voluntary termination benefits equal one month's pay for each year of service whereas the company's written policy is to offer two week's pay for each year of service. The employees have until January 31 of the next year to decide whether to accept the offer. As of the company's fiscal year-end at December 31, only 10 of the employees have accepted the offer. The total of the special termination benefit payments due to these 10 employees is \$500,000.

As of year-end, the company's management has decided to involuntarily terminate any of the employees who do not accept the special voluntary termination benefit. The total of the severance payments that would be due to these 40 employees if they are involuntarily terminated equals \$1,000,000.

Because the 10 employees accepted the special termination benefit prior to December 31, a liability for \$500,000 should be recognized at the year-end balance sheet date. No additional special termination benefit liability should be recognized for the estimated number of additional employees who will accept the offer before it expires on January 31.

Policies and Procedures

Policy: 2013-01 | Title: Accounting for Employee Termination Costs



Financial

Entry at December 31:

Dr 6000/7000_135 Severance	\$500,000	
		Cr 2040_170-Accrued Labor Termination/Severance
		\$500,000

To accrue special termination benefit for 10 employees who accepted offer before December 31

Because management has decided by December 31 that any employee who does not accept the special offer will be involuntarily terminated, an additional accrual of \$1,000,000 should be recognized at December 31. This is because termination benefits to be paid under an ongoing termination benefit arrangement are probable and estimable at December 31.

Entry at December 31:

Dr 6000/7000_135 Severance	\$1,000,000	
		Cr 2040_170-Accrued Labor Termination/Severance
		\$1,000,000

To accrue ongoing termination benefit for 40 employees who will be involuntarily terminated if they do not accept special termination offer

NOTE: An additional accrual would be required in January for any employees who accept the special offer in January.