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International Accounting Standards Board

INFORMATION FOR OBSERVERS

IFRIC meeting: **3 November 2006, London**

Project: **IAS 19: special wages tax (Agenda Paper 12(iii))**

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1. The issue has been raised of how to account for a tax on pension costs. The tax in question is described as being payable when an entity makes a provision for pension costs. The staff is also aware of taxes in other jurisdictions that are payable when an entity makes a contribution to a pension plan. Both types of tax raise similar issues.

2. The question raised is whether the tax can be recognised directly in equity when actuarial gains and losses are recognised directly in equity in accordance with paragraph 93A of IAS 19 *Employee Benefits*. For taxes that are payable when an entity makes a contribution to a pension plan, an additional question would be whether the deferred recognition options that apply to some components of the pension cost can also apply to the tax. In other words, should a liability be recognised for the tax related to the full deficit in the plan or only for the tax related to the recognised deficit?

3. The staff has identified 4 possible methods for accounting for the tax:

   a. as income tax in accordance with IAS 12 *Income Taxes*. However, the staff notes that the tax is not an income tax and therefore does not fall within the scope of IAS 12. This option is not discussed any further

   b. as part of the defined benefit obligation in accordance with IAS 19

   c. in the same way as administrative costs of the plan in accordance with IAS 19 and

   d. as a provision in accordance with IAS 37.

Treatment as part of the defined benefit obligation

4. The definition of the present value of a defined benefit obligation is the present value, without deducting any plan assets, of expected future payments required to settle the obligation resulting from employee service in the current and prior periods.

5. If the tax fell within the definition of the defined benefit obligation in IAS 19, it would form part of the calculation of the components of pension cost, eg current and past service cost, interest cost and actuarial gains and losses. These components would all include the impact of the tax, and so the actuarial gains and losses recognised directly in equity would include the appropriate amount of the tax. Similarly any tax included in the calculation of the actuarial gains and losses would be deferred in accordance with the entity's accounting policy for actuarial gains and losses.

Treatment as an administrative cost of the plan

6. The tax could be argued to be the same as an administrative cost of the plan. Such costs, other than those included in the actuarial assumption used to measure the obligation, are deducted from the expected and actual return on plan assets (IAS 19 paragraph 107). Given that the tax is related to the pension cost rather than the return on plan assets, it would seem appropriate to include it in the

actuarial assumptions used to measure the obligation, giving the same answer as above.

Treatment as a provision under IAS 37

7. If the tax does not fall under the scope of IAS 12 or IAS 19, it would by default fall under IAS 37. IAS 37 does not permit any part of a provision to be recognised directly in equity nor does it allow for any deferred recognition.

Staff analysis

8. The constituent raising the question gives two views. One is that the tax is not a post-employment benefit and therefore cannot be treated as an actuarial gain or loss. The other is that the tax should be regarded as part of the pension cost, ie should be regarded as part of the defined benefit obligation.

9. [Paragraph omitted from observer notes.]

10. [Paragraph omitted from observer notes.]

11. [Paragraph omitted from observer notes.]

12. The IFRIC Agenda Committee does not recommend that IFRIC take up the issue because it is a relatively narrow issue that does not merit a full Interpretation. The IFRIC Agenda Committee recommends that IFRIC rejects the issue using the following wording[1].

> The IFRIC was asked to consider whether taxes payable by the employer on defined benefits, for example taxes payable on contributions to a defined benefit plan or taxes payable on some other measure of the defined benefit, should be treated as part of the defined benefit obligation in accordance with IAS 19 *Employee Benefits*. The IFRIC noted that paragraphs 4 and 8 of IAS 19 include social security costs as examples of short-term employee benefits and that paragraph 107 refers to the administrative costs of a defined benefit plan: both of

[1] One member of the Agenda Committee, on considering the rejection wording after the Agenda Committee meeting, suggested instead that a minor amendment be made to IAS 19.

which are considered to be part of the costs of providing employee benefits. The IFRIC noted that taxes payable by an employer on defined benefits were similarly part of the cost of providing the employee benefit.

The IFRIC decided that diversity in practice would be unlikely after attention is drawn to the paragraphs of IAS 19 noted above. The IFRIC therefore decided not to take the issue on to its Agenda.