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International
Accounting Standards
Board

This observer note is provided as a convenience to observers at IFRIC meetings, to assist them in following the IFRIC's discussion. Views expressed in this document are identified by the staff as a basis for the discussion at the IFRIC meeting. This document does not represent an official position of the IFRIC. Decisions of the IFRIC are determined only after extensive deliberation and due process. IFRIC positions are set out in Interpretations.

Note: The observer note is based on the staff paper prepared for the IFRIC. Paragraph numbers correspond to paragraph numbers used in the IFRIC paper. However, because the observer note is less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

IFRIC meeting: **January 2007, London**

Project: **IAS 19: special wages tax (Agenda Paper 14(ii))**

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1. At the last meeting, the IFRIC considered rejection wording for the issue of how to account for a tax on pension costs. The IFRIC did not accept the rejection wording and asked the staff to develop a paper for the Agenda Committee on the nature of the taxes (whether they are income taxes or other taxes on the entity or taxes paid by the entity on behalf of employees) and whether the scope of IAS 19 is employee benefits or the cost of employee benefits.

2. The previous IFRIC paper giving the background to the issue is attached for information. [Previous observer notes attached.]

3. Having consulted the Agenda Committee, the staff recommends the following rejection wording.

The IFRIC was asked to consider whether taxes related to 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 the following:

(a) taxes paid by a defined benefit plan are included in the definition in IAS 19 of the return on plan assets

(b) income taxes paid by the entity are accounted for in accordance with IAS 12

(c) the scope of IAS 19 is not restricted to benefits paid to employees. It includes some costs of employee benefits that are not paid to employees and

(d) a wide variety of taxes on pension costs could exist world-wide, each specific to its own jurisdiction, and it is a matter of judgment whether they are income taxes within the scope of IAS 12, costs of employee benefits within the scope of IAS 19, or other costs within the scope of IAS 37. Given this, guidance beyond the above observations cannot be developed in a reasonable period of time.

The IFRIC therefore [decided] not to take the issue on to its agenda.

Staff analysis

4. As noted in previous papers, the staff does not regard the taxes that are the subject of this sumbission as income taxes. The amount of the tax is determined by reference to some measure of pension expense, either a cash expense (contributions) or calculated in accordance with specified rules. It is not determined by reference to an entity's net income.

5. The staff also understands that the taxes that have been raised with the IFRIC are expressed in the form of a tax on the entity. If the taxes were expressed in the

form of a tax paid by an entity on behalf of employees, the staff thinks the accounting would be clear: the pension cost would be measured and recognised in accordance with IAS 19 regardless of how much was paid to the employees and how much was paid to the taxing authorities.

6. Whether the scope of IAS19 is employee benefits or the cost of employee benefits is difficult to determine, as indeed is the scope of the term 'employee benefits'. The objective refers to the accounting and disclosure for employee benefits. But many paragraphs refer to the cost of various benefits (for example, paragraphs 11, 14, 17 and 63). Further, the definition of employee benefits refers to all forms of consideration given by an entity in exchange for service rendered by employees, without stating that the consideration needs to be given to the employees. Similarly, the definition of the present value of the defined benefit obligation refers to expected future payments required to settle the obligation resulting from employee service in the current and prior periods, again without specifying the recipient of the payments.

7. [Not reproduced in observer notes.]

8. Having considered these points, the Agenda Committee noted that there were similarities between this issue and the issue of which taxes should fall within the scope of IAS 12, which the IFRIC considered in March 2006. In both cases, there could be a wide variety of different taxes, each specific to its own jurisdiction. Although the taxes brought to the attention of the IFRIC are not income taxes, there may be taxes related to employee benefits in other jurisdictions that are. Similarly, although the taxes brought to the attention of the IFRIC are paid by the entity not the plan, there may be other taxes with the same economic or fiscal intent that are paid by the plan.

9. On the IAS 12 issue, the IFRIC concluded that it would not be possible to give guidance on each individual tax. Instead, the IFRIC made some general observations on the context in which a judgement on the matter should be made. The proposed rejection wording above is based on the rejection wording for the IAS 12 issue.

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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.