Project **Item for continuing consideration**

IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and IFRIC 6 *Liabilities arising from Participating in a Specific Market—Waste Electrical and Electronic Equipment—*

Topic **Summary paper**

Introduction

1. The IFRS Interpretations Committee (the Committee) received a request to clarify whether, under certain circumstances, IFRIC 6 *Liabilities arising from Participating in a Specific Market—Waste Electrical and Electronic Equipment* should be applied by analogy to other levies charged for participation in a market on a specified date as a method for identifying the event that gives rise to a liability.

2. The Committee first discussed this issue at its meeting in May 2011.

Purpose of the paper

3. The objective of this paper is to:

   (a) provide background information on the issue; and

   (b) provide a summary of feedback received from national standard-setters and other interested parties on the issue.

Structure of agenda papers

4. For ease of reference we have split the analysis of the two critical issues identified from the original submission (see paragraph 5 below) as follows:

   (a) **Agenda paper 5A** discusses whether, in the situations described to us, the obligating event is the participation in an activity on the date specified by the legislation, or whether other factors create an earlier obligation; and

   (b) **Agenda paper 5B** discusses the accounting in interim reporting period in the situations where the activity date/period and the calculation date/period fall in the same annual financial reporting period.

Interpretations Committee's directions from the meeting in May 2011

5. We reproduce below an excerpt from the May 2011 IFRIC Update:

> […]
>
> The Committee observed that the levies presented in the submission are all different. Whether and how the consensus in IFRIC 6 would apply to them could vary depending upon the facts of each levy.
>
> The Committee also noted that the issue raises the two following fundamental challenges:
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> - determining whether the obligating event is the participation in an activity on the date specified by the legislation, or whether other factors create an earlier obligation; and
> - when the obligating event arises in the current annual period, determining the circumstances when an appropriate portion of the charge can be accrued at an interim reporting date.
>
> The Committee directed the staff to review the guidance in IAS 37 on the timing of recognition of a liability and to perform further outreach activities to National Standard Setters to learn about what analysis has already been performed on similar levies that might be helpful to the Committee. The staff will present the results of this further work at the meeting in July 2011.

Result of outreach activities to national standard-setters

Overview of feedback received

6. We carried out outreach activities to national standard-setters asking them to provide details for levies in their jurisdictions:

   (a) for which determining the obligating event, and thus when to recognise the liability, has proved difficult, and

   (b) for which an analysis had already been performed.

7. We received feedback from 15 jurisdictions, of which 7 claim that they face levies with similar issues as those raised in agenda paper 15 presented at the May 2011 Interpretations Committee meeting.

8. In many of the jurisdictions in which concern was raised about the accounting for levies, analysis is still at an early stage because the discussions and the enactment of related legislation are both quite recent. Consequently, in many cases, we obtained a broad description of the levies rather than an analysis of the accounting treatment that would be applied to those levies.

9. One standard-setter brought to our attention an authoritative piece of literature as part of US GAAP, which deals with liabilities to account for fees paid to the Federal Government by pharmaceutical manufacturers. The authoritative literature is in the form of a consensus of the FASB Emerging Issues Task Force (the EITF) that was published in December 2010. The consensus is reproduced in Appendix A to this paper.

10. The fees paid to the Federal Government by pharmaceutical manufacturers in the USA is similar to other levies set out in the original submission, in that the measurement period is different from the time during which the entity is within the scope of the levy. More specifically both happen in different annual financial reporting periods.

11. In addition, we received further information from interested parties on the Hungarian bank levy that was broadly depicted in the original submission.

Feedback received included an analysis of a possible accounting treatment for that levy.

Main features of the levies described in feedback received

12. Given the feedback received, we are of the opinion that the following four relevant situations reflect the diversity that currently exists as to the timing of recognition of the liability:

    (a) the UK bank levy;

    (b) the fees paid to the Federal Government by pharmaceutical manufacturers in the US;

    (c) the bank levy in Hungary; and

    (d) the railway tax in France.

13. Of those situations, two were presented in agenda paper 15 for the Committee meeting in May 2011: the UK bank levy and the railway tax in France.

14. The main features of these levies that are relevant for the purpose of our analysis are listed in the table below:

	UK bank levy	**Fees paid to the Federal Government by pharmaceutical manufacturers in the US**	**Hungarian bank levy**	**Railway tax in France**
Date in the legislation on which the entity falls in the scope of the levy	Last day of reporting period. Payment is quarterly in advance.	No date specified in the legislation as to when the entity falls within the scope of the levy. Only the payment date is specified and is no later than September 30 of the calendar year.	Tax for 2010: financial institutions fall within the scope of the levy when they filed financial statements before 1 July 2010 Tax for 2011: on 1 January 2011.	1 January, each year commencing 1 January 2011.
Measurement features	Levy calculated by reference to the amount of certain liabilities and equities on the last day of the reporting period.	Levy calculated by reference to revenue in the reporting period preceding the reporting period in which the entity falls within the scope of the levy.	Financial data in a specified year: 2009 for the 2010 and 2011 taxes—measurement basis depends on the nature of the entity.	Levy calculated by reference to revenue in the reporting period preceding the reporting period in which the entity falls within the scope of the levy.
Additional information	Charge over a period of account Pro rata when the period of account is shorter than 12 months. Quarterly instalments in the financial period prior to the date on which the entity falls within the scope of the levy.	Intent via a speech: entities that qualify are those on the market during current reporting period.	In case of liquidation or discontinued operations, levy due in full.	5-year certificate necessary to operate (see agenda paper 15 presented in May 2011).

15. The table below sets out examples of levies based on 2012 - for annual financial periods ending 31 December:

	UK bank levy	**US pharma fees**	**Hungarian bank levy**	**French railway tax**
Trigger date, per legislation	31/12/12	Date of first sale of qualifying drugs during 2012	The details of paying extra tax in 2012 will be set out in a separate act.	1/1/12
Payment date	Quarterly payments; April 2012, July 2012, October 2012, January 2013 (true-up)	September 2012		1/01/12
Measurement basis	Value of liabilities and equity at 31/12/12	Revenues during 2011	The details of paying extra tax in 2012 will be set out in a separate act. For the tax payable in 2011, the tax base is either a certain balance sheet amount as at 31 December 2009 or a certain income statement amount for the financial year ended 31 December 2009, depending on the activity of the entity.	Revenues during 2011

Analyses received from national standard-setters and other interested parties

16. We reproduce below a summary of analysis for the accounting treatment in the cases in which it has been provided to us:

	Accounting treatment	**Rationale**
Fees paid to the Federal Government by pharmaceutical manufacturers in the US	Recognition of a liability from the first sale in the year of payment. Simultaneous recognition of an asset, which is amortised to profit or loss over the reporting period.	No liability if the entity does not operate in the year of payment. Annual fee: a right to operate in year of payment. The asset recognised reflects that right. Amortisation of asset on a straight-line basis over the year reflects the pattern of consumption of economic benefits.
Hungarian bank levy	Liability for 2010 recognised in full on the date on which the law was enacted, i.e. 27 September 2010 Levy for 2011: liability recognised in full on 1 January 2011, which is the date when the law was enacted.	The tax meets the definition of a liability on the date the law is enacted. Even in the case of liquidation, the tax is due in full.
Railway tax in France	Recognised in the financial reporting period preceding the one in which the entity falls in the scope of the tax, i.e. recognised in the same financial year as the revenues are earned on which the amount of the tax is calculated.	Going concern principle: virtual certainty that the entity will operate on the date on which the entity falls in the scope of the levy. Similarity to and dependence on an income tax, hence the same recognition principle is retained for both.

The analysis of the UK levy was provided in agenda paper 15 at the May 2011 Committee meeting.

IASB Staff paper
Appendix A

Appendix A—excerpt from FASB EITF 2010-27

Other Expenses—Fees Paid to the Federal Government by Pharmaceutical Manufacturers

Overview and Background

General

720-50-05-1 This Subtopic provides guidance on the annual fee paid by pharmaceutical manufacturers to the U.S. Treasury in accordance with the Patient Protection and Affordable Care Act as amended by the Health Care and Education Reconciliation Act (the Acts).

720-50-05-2 The Acts impose an annual fee on the pharmaceutical manufacturing industry for each calendar year beginning on or after January 1, 2011. An entity's portion of the annual fee is payable no later than September 30 of the applicable calendar year and is not tax deductible. The annual fee ranges from $2.5 billion to $4.1 billion in total, a portion of which will be allocated to individual entities on the basis of the amount of their branded prescription drug sales for the preceding year as a percentage of the industry's branded prescription drug sales for the same period. An entity's portion of the annual fee becomes payable to the U.S. Treasury once a pharmaceutical manufacturing entity has a gross receipt from branded prescription drug sales to any specified government program or in accordance with coverage under any government program for each calendar year beginning on or after January 1, 2011.

Scope and Scope Exceptions

General

720-50-15-1 The guidance in this Subtopic applies to all pharmaceutical manufacturers that are subject to the annual fee imposed by the Acts described in paragraphs 720-50-05-1 through 720-50-05-2. The guidance in this Subtopic is based on the unique facts and circumstances of the fee to be paid by pharmaceutical manufacturers in accordance with the Acts; accordingly, an entity should apply judgment when evaluating the facts and circumstances of other fee arrangements before analogizing to the guidance in this Subtopic.

Recognition

General

720-50-25-1 The liability related to the annual fee described in paragraph 720- 50-05-1 shall be estimated and recorded in full upon the first qualifying sale with a corresponding deferred cost that is amortized to expense using a straight-line method of allocation unless another method better allocates the fee over the calendar year that it is payable.

Other Presentation Matters

General

720-50-45-1 The annual fee described in paragraph 720-50-05-1 shall be presented as an operating expense.

Transition and Open Effective Date Information

> Transition Related to Accounting Standards Update No. 2010-27, Other Expenses (Topic 720): Fees Paid to the Federal Government by Pharmaceutical Manufacturers

720-50-65-1 The following represents the transition and effective date information related to Accounting Standards Update No. 2010-27, *Other Expenses (Topic 720): Fees Paid to the Federal Government by Pharmaceutical Manufacturers:*

a. The pending content that links to this paragraph shall be effective for calendar years beginning after December 31, 2010.

b. The pending content that links to this paragraph does not require an entity to reevaluate its existing policies related to similar fees assessed by governmental authorities.