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Project **Levies charged for participation in a market on a specified date**

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 to identify the event that gives rise to a liability.
2. The concern relates to when a liability should be recognised and to the definition of a present obligation in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.
3. The Committee decided to add this issue to its agenda in July 2011.

Purpose of the papers

4. The objective of these papers is to provide an analysis of the accounting treatment applicable to levies charged for participation in a market on a specified date.
5. These papers do not address:
 - (a) the accounting for levies that fall within the scope of IAS 12 *Income Taxes* (ie levies that are based on taxable profits);
 - (b) the accounting treatment applicable in the interim financial statements;
 - (c) the measurement of the liability.

This paper has been prepared by the technical staff of the IFRS Foundation for discussion at a public meeting of the IFRS Interpretations Committee.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the IFRS Interpretations Committee or the IASB. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination.

Decisions made by the IFRS Interpretations Committee are reported in *IFRIC Update*.

Interpretations are published only after the IFRS Interpretations Committee and the Board have each completed their full due process, including appropriate public consultation and formal voting procedures. The approval of an Interpretation by the Board is reported in *IASB Update*.

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6. The objective of these papers is not to provide specific answers to each of the situations reported to us. Instead, we aim to provide guidance to help preparers of financial statements to apply IFRSs to a range of facts and circumstances.

Structure of the papers

7. For ease of reference, we have split the analysis as follows:
 - (i) Agenda paper 2A addresses the following issue: when should the liability for the obligation to pay a levy be recognised?
 - (ii) Agenda paper 2B addresses the following issue: is the liability for the obligation to pay a levy associated with an asset or an expense?
 - (iii) Agenda paper 2C provides some illustrations of the application of our accounting analysis to a range of levies charged for participation in a market on a specified date.

Decisions taken at the last meeting in July 2011

8. During the last meeting, the Committee discussed the two following issues:
 - (a) 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
 - (b) whether a liability should be recognised in an interim reporting period in situations where the activity date and the calculation date fall in the same annual financial reporting period.
9. Having assessed the issues against the agenda criteria, the Committee decided to add the first issue onto its agenda with a view to developing guidance, after which the Committee will consider whether such guidance would address the second issue and, if not, whether the second issue should be added to the agenda.
10. To avoid confusion between the date or period in which the entity participates in the market and the date or period that is used to calculate the amount of the levy, the Committee decided to use the following terms:

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- (a) Activity date/period: this is the date or period in which the entity's participation in the event/market/activity occurs (in IFRIC 6 this is called the measurement period);
 - (b) Calculation date/period: this is the date or period of the financial data used to calculate the amount of the levy.
11. The Committee also tentatively concluded that IFRIC 6 is not directly applicable, but because IFRIC 6 is an interpretation of IAS 37, any conclusions drawn on the application of IAS 37 to the levies should be consistent with the conclusions drawn in IFRIC 6.

Characteristics of the levies considered

12. The levies considered in these papers have the following characteristics:
- (a) the participation in the market on a specified date or period triggers the payment of the levy;
 - (b) the levy is an annual recurring tax (it might be payable by instalments);
 - (c) the calculation basis of the levy is based upon financial data for the current or a previous reporting period.
13. We provide below examples of levies considered in these papers (see also Agenda paper 2C Illustrative examples).

Illustrative example 1: calculation period and activity period coincide

14. The legislation imposes an annual levy for each calendar year for entities participating in a specific market. A levy is due if entity A generates revenues in that specific market in 2011. The amount of the levy is determined by reference to revenues generated by entity A in the market in 2011. The levy arising from the activity in the specific market in 2011 is payable in full in April 2012. Entity A generates revenues on the market on 1 January 2011. In this example, the activity period (ie 2011) and the calculation period (ie 2011) are the same.

Illustrative example 2: calculation date is at the end of the activity period

15. The legislation imposes an annual levy for each calendar year for entities participating in a specific market. A levy is due if entity B participates in that specific market in 2011. The amount of the levy is determined by reference to balance sheet data of entity B on 31 December 2011. The levy is payable in April 2012. Entity B participates in the market on 1 January 2011. In this example, calculation date (ie 31 December 2011) is at the end of the activity period (ie 2011).

Illustrative example 3: calculation period precedes activity period

16. The legislation imposes an annual levy for each calendar year for entities participating in a specific market. The levy is due if entity C generates revenues in that specific market in 2011. The amount of the levy is determined by reference to revenues generated by entity C in the market in the preceding year (ie 2010). The levy arising from the activity in the specific market in 2011 is payable in full in April 2012. Entity C participates in the specific market on 1 January 2011. In this example, the calculation period (ie 2010) precedes the activity period (ie 2011).

Rights and obligations associated with the payment of a levy charged for participation in a market

17. We believe that an analysis of the rights and obligations associated with the payment of a levy should be performed in order to propose an appropriate accounting treatment.
18. For the levies considered in these papers, we note that the levy is intended to be an annual tax that, in substance, is charged in return for the entity participating in a market for a specified period (generally a calendar year). The entity cannot participate in the market without paying the levy.
19. In our view, the situation of an entity that participates in a market in exchange for the payment of a levy is equivalent to the situation of an entity that purchases a licence to conduct certain activities in a specific market in exchange for the payment of a consideration.

20. We think that the obligation to pay a levy in the cases described above is associated with an implicit right for the entity to participate in a specific market for a specified period.

Question for the Committee

Does the Committee agree that the obligation to pay a levy in the cases described above is associated with a right for the entity to participate in a specific market for a specified period?

21. In our view, the analysis of the substance of this transaction raises three questions:
- (a) Is the transaction associated with the obligation to pay a levy executory (ie is the levy a cost that needs to be incurred to operate in the specific market in a specified period)?
 - (b) Does the right to participate in the market meet the definition of an asset?
 - (c) When does the entity have a present obligation to pay the levy?
22. We think that the answer to these questions will determine what the accounting treatment will be both in the annual financial statements and in the interim financial statements.