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Project **Tentative agenda decision**

Topic **IAS12 Income tax—rebuttable presumption to determine the manner of recovery**

Purpose of this paper

1. This paper discusses a question raised in the submission (see Appendix A) regarding a rebuttable presumption in paragraph 51C of IAS 12 Income Tax.

2. This paper:

   (a) explains the issue;

   (b) provides background information;

   (c) analyses the issue raised within the context of IFRSs; and

   (d) makes a staff recommendation for the Committee agenda decision.

Explanation of the issue

3. The IASB issued amendments to IAS 12 *Deferred Tax: Recovery of Underlying Assets* in December 2010. The amendments added a paragraph 51C which introduced a rebuttable presumption that the investment property's carrying amount is recovered entirely through sale. Paragraph 51C states:

   > If a deferred tax liability or asset arises from investment property that is measured using the fair value model in IAS 40, there is a rebuttable presumption that the carrying amount of the investment property will be recovered through sale. Accordingly, unless the

> presumption is rebutted, the measurement of the deferred tax liability or deferred tax asset shall reflect the tax consequences of recovering the carrying amount of the investment property entirely through sale. <u>This presumption is rebutted if the investment property is depreciable and is held within a business model whose objective is to consume substantially all of the economic benefits embodied in the investment property over time, rather than through sale</u>. If the presumption is rebutted, the requirements of paragraphs 51 and 51A shall be followed. (<u>emphasis</u> added)

4. The submission observed that there could be two possible ways to interpret the rebuttable presumption in IAS12.51C. They are:

    (a) View A—the presumption can be rebutted in circumstances other than those described in paragraph 51C; and

    (b) View B—the presumption can only be rebutted in circumstances described in paragraph 51C.

5. Supporters of View A think that the presumption can be rebutted in other circumstances because paragraph 51C is not worded as 'if and only if' while 'if and only if' is already used in other parts of IAS 12.[1] They think that entities can rebut the presumption by merely demonstrating the entity's expectation to recover the carrying amount of an asset other than through sale. They think that it would be a loss of relevant information if the presumption is not rebutted in situations where the tax rate applied on the sale of the asset is different to that of the use of the asset, and an entity intends to use an investment property for a period of time and then sell it (ie a dual-purpose asset).

6. Supporters of View B think that paragraph BC11 of the Basis for Conclusions makes clear that an entity is to assume recovery entirely through sale even if the entity expects it to be used and then sold. Paragraph BC 11 states:

> BC11 Many respondents to the exposure draft of September 2010 commented that the Board should develop application guidance rather than creating an exception. The Board could have achieved a similar result in many cases by providing application guidance on how to apply the underlying principle to investment

[1] See Appendix C for excerpts of 'if and only if' used in other parts of IAS 12.

> property. However, the Board chose an exception because it is simple, straightforward and can avoid unintended consequences by a strict definition of its scope. In fact, this exception is very similar to application guidance. However, it is technically an exception because, in some cases, the asset's carrying amount is assumed to be recovered entirely through sale even though an entity expects it to be recovered partly through sale and partly through use. (emphasis added)

7. The submitter asked us to clarify this issue by:

   (a) clarifying how the rebuttable presumption in paragraph 51C should be interpreted; and

   (b) explaining how the final sentence of paragraph BC11 should be understood.

Background

8. In December 2010, the IASB issued the amendments to IAS 12 in order to provide a practical solution to an issue that often arose when investment properties were measured at fair value. That issue typically arose when an asset is expected to generate future cash flows more than its carrying amount as a result of both use and sale and its value is not expected to diminish as a result of using it. The issue has relevance in financial reporting when different tax rates applied to income from using the investment property (rental income) and to a gain from sale of the investment property.

9. Before the amendments, entities had to estimate how much of carrying amount of the investment property would be recovered through sale and how much of it would be recovered through use. The Board determined that practice issues arose because of difficulty and subjectivity in determining;

   (a) which part of future cash in-flows represent recovery of the carrying amount that is subject to recognition of a deferred tax liability at the end of the reporting period; and

   (b) which part of future cash in-flows represent additional income that is subject to recognition of a tax liability in the future reporting periods.

10. The amendments removed the difficulty and subjectivity by introducing a presumption that the carrying amount will be recovered entirely through sale. The amendments made clear that the presumption is rebutted when an asset is depreciable and is held within the entity's business model whose objective is to consume substantially all of the asset's economic benefits over time rather than through sale. The reason for describing this particular set of circumstances was to replace the original proposal in the exposure draft of the December 2010 amendment, which proposed that an entity would need to provide clear evidence to rebut the presumption(see paragraph BC23 of IAS 12)

Staff analysis

Can the presumption be rebutted in other circumstances?

11. The term 'rebuttable presumption' is often used in IFRSs[2]. It is not a defined term, so it should be used as a general term in a dictionary. The Oxford English Dictionary defines the word 'presumption' as follows:

> an idea that is taken to be true on the basis of probability: underlying presumptions about human nature
>
> [mass noun] the acceptance of something as true although it is not known for certain: the presumption of innocence
>
> chiefly Law an attitude adopted in law or as a matter of policy towards an action or proposal in the absence of acceptable reasons to the contrary: the planning policy shows a general presumption in favour of development

12. Having considered the above, we think that a rebuttable presumption used in IFRSs is a matter of policy towards the application of principle (or exception) in IFRSs in the absence of acceptable reasons to the contrary. It is therefore rebutted if sufficient evidence is available to overcome the presumption.

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[2] See Appendix C for excerpts of rebuttable presumption used in IFRSs.

13. The presumption under consideration is the presumption that the carrying amount of the investment property will be recovered through sale. This is an exception from the general principle in paragraph 51 that deferred tax is measured to reflect the manner in which the entity expects to recover or settle the carrying amount of its assets and liabilities.

14. Paragraph 51C of IAS 12 provides a case in which the presumption of recovery through sale is rebutted. This is a situation in which recovery entirely through sale generally does not happen. It does not say whether that is the only case (a restrictive interpretation) or it is an example (a permissive interpretation). However, having considered the general meaning of 'presumption', we think that this paragraph should not be read restrictively because there are other cases in which the presumption does not hold (ie we hold View A). For example, the presumption of recovery entirely through sale does not hold if an entity expects a dual-purpose asset to be sold at a future date at a price below its carrying amount after receiving sufficient economic benefits to recover, in a combination of sale proceeds and rental income, the carrying amount at the reporting date.

What is paragraph BC11 trying to say?

15. The words 'some cases' are interpreted differently between View A and View B. They are:
    (a) In View A, 'some cases' mean <u>a subset of</u> cases in which
        (i) the presumption was not rebutted (ie the carrying amount is recovered entirely through sale);
        (ii) even though the cases involve a dual-purpose asset (ie the asset is used and then sold); and
    (b) In View B, some cases mean <u>all</u> cases involving a dual-purpose asset.

16. Supporters of View B think that the last sentence of paragraph BC11 requires the recovery through sale to always be applied to a dual-purpose asset. They think that this sentence indicates that the Board intended to require the entity to apply the recovery through sale in all circumstances involving a dual-purpose asset.

17. However, as we hold View A, we think that the Board's intention that is reflected in the last sentence of paragraph BC11 of the Basis for Conclusions is no more than an intention to introduce an exception to the measurement principle in IAS 12. In the Board's deliberation in 2010 on amending IAS 12, the Board first decided to introduce an exception in order to solve this issue, and then decided to use a rebuttable presumption as the form of the exception. Because an exception in the form of a rebuttable presumption has very similar results to application guidance, we think that paragraph BC11 of the Basis for Conclusions is explaining why it is an exception rather than application guidance. We think that it is not explaining when the exception should be applied. We do not believe that the Basis for Conclusions is adding a requirement to the standard.

18. The submitters who support View A argue that the presumption should always be rebutted when a case involves a dual-purpose asset (ie when an asset is used and then sold). They think that it would be a loss of relevant information if the presumption is not rebutted if the case involves a dual-purpose asset.

19. However, we think that the presumption does not always have to be rebutted when a case involves a dual-purpose asset even under View A. In order to rebut the presumption, it is not sufficient for an entity to demonstrate that it will use the asset. In addition, the entity should demonstrate that it does not expect to sell the property in the future at a price above its carrying amount so that the carrying amount of an asset cannot be recovered entirely through sale. The presumption of recovery through sale should continue to be held when an entity expects to sell the asset in the future at least for a price equal to the asset's carrying amount.

20. Applying this approach, we think that the accounting result is consistent between a property that is accounted for in accordance with IAS 16 *Property, Plant and Equipment* and an identical property that is accounted for in accordance with IAS 40 *Investment Property*. The following example explains this:

> Assume that there is a property of which fair value is CU100 and that entities that acquired that property can claim a tax deduction only up to CU60. Assume that, because of the nature of the property, entities do not expect that the property value diminishes as a result of using it. As a result, entities expect the property to be worth more than CU100 when it will be sold in the future. Also assume that this is a situation in which the

> initial recognition exception in IAS12.15 does not apply to a temporary difference of CU40 (CU100-CU60).
>
> Entity A that owns the property and accounts it for in accordance with revaluation model in IAS 16 does not depreciate the property because it expects that the property value does not diminish. Entity A measures a deferred tax liability for the temporary difference of CU40 based on a recovery entirely through sale in the light of guidance in paragraph 51B of IAS 12 because no part of the carrying amount is depreciated in accordance with IAS 16.
>
> Entity B owns the identical property and accounts it for in accordance with the fair value model in IAS 40. Paragraph 51C of IAS 12 requires Entity B assume a recovery of the carrying amount entirely through sale if it expects to sell the property in the future at least for a price equal to the carrying amount.
>
> As a result, both Entity A and Entity B measures a deferred tax liability for a temporary difference of CU40 based on a recovery of the carrying amount entirely through sale.

21. We think that the presumption of recovery entirely through sale does not result in a loss of relevant information if the presumption is used when an entity expects to sell the property, after use, at least for a price equal to or above the asset's carrying amount. This is because, in such a case, the tax consequences of the recovery entirely through sale represent the tax cash flows that are expected to happen upon the future sale.

What is the nature of the rebuttal in paragraph 51C?

22. Paragraph 51C provides a case in which the presumption is rebutted by looking at the entity's business model. The case is interpreted as follows under View A and View B respectively:

    (a) View A—it is an example of cases in which the presumption can be rebutted; and

    (b) View B—it is the only case in which the presumption can be rebutted.

Consideration of View B

23. We understand that, during the Board's deliberation on the amendments to IAS12 in December 2010, the Board did not contemplate other cases in which the

presumption should be rebutted. Therefore, the supporters of View B think that the Board wanted the rebuttal of the presumption to be restrictive rather than permissive.

24. However, we think that it is not possible to read the paragraph 51C restrictively for the following reasons:

25. Because of the meaning of the term ‘presumption’ noted in paragraph 11, the presumption should be rebutted if it does not hold. There are many circumstances in which the presumption cannot be held. However, the rebuttal in paragraph 51C provides only one of those cases.

26. We think that the Board should have provided an exclusive list of cases in which the presumption does not hold if it wanted the case in paragraph 51C to be restrictive. Alternatively, we also think that the Board could have used a different form other than rebuttable presumption if it wanted to restrict the rebuttal of the presumption to the single case currently described in paragraph 51C. For example, the Board could have used a requirement with a narrowly drawn exception.

27. Because the Board chose to use the form of the rebuttable presumption and did not provide an exclusive list of the rebuttable cases in paragraph 51C, we think that the paragraph 51C cannot be restrictive. As a result, we support View A.

Consideration of View A

28. If the presumption can be rebutted in other cases (ie View A), a question arises as to why paragraph 51C needs to provide a specific case in which the presumption is rebutted. Some supporters of View A think that IAS12.51C provides an example in order to show the degree of comfort or sufficiency of evidence necessary to rebut the presumption. They think that paragraph 51C could be improved through Annual Improvements by adding the words ‘for example’ before the single case of rebuttal.

(Interpretation) Agenda criteria assessment for the Committee

29. The staff's preliminary assessment of the (interpretation) agenda criteria is as follows:

    (a) *The issue is widespread and has practical relevance.*

    No, because the amendments have not been applied widely. Except for early adopters, it will be adopted from 1 January 2012. However, it is potentially widespread and has practical relevance because, once it is adopted, it applies to all business enterprises in jurisdictions in which the tax consequences of selling an asset is different from the tax consequences of using it. In some jurisdictions, the sale of an asset is tax-free while income generated from using the asset is taxable.

    (b) *The issue indicates that there are significantly divergent interpretations (either emerging or already existing in practice). The Committee will not add an item to its agenda if IFRSs are clear, with the result that divergent interpretations are not expected in practice.*

    No, because the amendments have not been applied widely. However, they could potentially create significant divergence because some could read the rebuttal of the presumption in paragraph 51C in a different way.

    (c) *Financial reporting would be improved through elimination of the diverse reporting methods.*

    Yes. If the Committee clarifies this before the amendments will take effect, we do not expect significantly diverse reporting methods to emerge in practice.

    (d) *The issue can be resolved efficiently within the confines of existing IFRSs and the Framework, and the demands of the interpretation process.*

    No. We do not think it is an issue that needs interpreting, rather it is a question of whether the requirements of the standard are clear enough. We think that the issue is clear from the general meaning of the word 'presumption' in a dictionary.

    (e) *It is probable that the Committee will be able to reach a consensus on the issue on a timely basis.*

    Yes, we believe that the issue is clear and that the Committee can reach a consensus on a timely basis.

(f) *If the issue relates to a current or planned IASB project, there is a pressing need to provide guidance sooner than would be expected from the IASB's activities. The Committee will not add an item to its agenda if an IASB project is expected to resolve the issue in a shorter period than the Committee requires to complete its due process.*

Not applicable. The Income Tax project has already completed a limited amendment to deal with the issue arising from fair valuing an investment property and the Board's plans for any future work on Income Taxes will be subject to its consideration of feedback received through its Agenda Consultation. However, we understand that in some jurisdictions, there are pressing needs to clarify this issue before the effective date of the amendments to IAS 12 on 1 January 2012..

Staff recommendation

30. We recommend that the Committee does not take this issue on to its agenda.

31. Firstly, this issue is not an issue that need an interpretation but rather it is an issue that some people request clarification. Therefore, the issue does not meet the interpretation agenda criteria.

32. Secondly, some people think that Annual Improvement is necessary to clarify this issue. They think that some of the Board's intentions are not clear from the existing basis for conclusions of IAS 12 and need to be clarified by adding 'for example' in paragraph 51C.

33. However, having considered the general meaning of 'presumption' noted in paragraph 11 and a fact that paragraph 51C does not provide an exclusive list of cases in which the presumption does not hold, we think that it is clear that the presumption in paragraph 51C can be rebutted in other circumstances. We think that it is clear that 'some cases' in paragraph BC11 does not refer to all circumstances involving a dual-purpose asset. We think that that paragraph merely means that there is a subset of cases in which **both** of the followings happen:

    (a) The entity expects to sell the asset after use, and

(b) The entity assumes the recovery of the carrying amount entirely through sale.

34. As a result, we think that the issue is clear from the existing wording in the standard and that the Annual Improvements to add ‘for example’ in paragraph 51C is not necessary.

Question to the Committee

35. The staff would like to put the following questions to the Committee:

Question 1—staff analysis
Does the Committee agree with the staff assessment that the presumption in paragraph 51C of IAS 12 can be rebutted in circumstances other than the case given in that paragraph?

Question 2—staff recommendation
Does the Committee agree with the staff recommendation not to add this issue on to the interpretation agenda? If yes, does the Committee agree with the proposed wording of the tentative agenda decision in Appendix B? If not, how does the Committee recommend the staff to proceed?

Appendix A—the submission

Re: *Amendments to IAS 12 Deferred Tax: Recovery of Underlying Assets*

On behalf of [the Submitter], I am writing to inform about a critical issue we have with the Amendments to IAS 12 *Deferred Tax: Recovery of Underlying Assets* issued by the IASB in December 2010 ('the Amendments').

In February 2011, [the Submitter] commenced its initial discussions. During our discussions it was not clear how the rebuttable presumption introduced by the amendments should be interpreted.

The purpose of this letter is to bring this issue to your attention, and to urge you to consider addressing it within a reasonable timeframe.

The issue

The Amendments introduce a 'default' single measurement attribute (in the form of a rebuttable presumption) to determine deferred taxes on investment property measured at fair value under IAS 40 *Investment Property*. IAS 12.51C (as amended) describes the rebuttable presumption as follows:

> *If a deferred tax liability or asset arises from investment property that is measured using the fair value model in IAS 40, <u>there is a rebuttable presumption that the carrying amount of the investment property will be recovered through sale</u>. Accordingly, unless the presumption is rebutted, the measurement of the deferred tax liability or deferred tax asset shall reflect the tax consequences of recovering the carrying amount of the investment property entirely through sale. <u>This presumption is rebutted if the investment property is depreciable and is held within a business model whose objective is to consume substantially all of the economic benefits embodied in the investment property over time, rather than through sale.</u> If the presumption is rebutted, the requirements of paragraphs 51 and 51A shall be followed.*

The rebuttable presumption could be interpreted in two different ways:

- View A – the presumption can be rebutted in circumstances other than those described in paragraph 51C (i.e. merely by demonstrating recovery other than through sale); and
- View B – the presumption can *only* be rebutted in the circumstances described in paragraph 51C (i.e. 'if and only if').

Those who hold View A believe that as paragraph 51C states that 'this presumption is rebutted *if*…', the condition that follows is not an exclusive condition because it is not preceded by the phrase '*if and only if*' (see also Appendix 1).

Those who hold View B believe that the final sentence of paragraph BC11 requires an entity to assume recovery entirely through sale even if the entity actually expects it to be recovered partly through sale and partly through use (see also Appendix 1).

Whether View A or View B is the appropriate interpretation is important […] for the reason described below.

Impact

Under View A the interpretation the Amendments would not introduce a significant change in accounting, because entities would be able to rebut the presumption and could continue to apply the measurement principles in IAS 12. However, under View B, there is a loss of relevant information because, some entities that are currently able to apply the principles in IAS 12 using reasonable management assumptions, will be ‘forced’ to produce financial information on a basis that does not reflect actual fact. For these entities, the exemption in paragraph 51C of the Amendments is not needed.

The loss of relevance is likely to occur in situations where the tax rate applied on the sale of the asset is different to that of use of the asset, and an entity intends to use an investment property for a period of time and then sell it. In these cases, the carrying amount of the investment property will be recovered and taxed in two different ways (a dual-purpose asset) and the deferred tax amount should reflect the dual economic reality.

In some cases, the period during which an investment property is being ‘used’ to generate economic benefits will be insignificant relative to the period of its useful life. In those cases, the impact on relevance is unlikely to be significant. However, in other cases the ‘use’ period is not expected to be insignificant and the Amendments are likely to have an adverse effect on relevance.

Addressing the issue

As noted above, it was not clear during our discussions how the rebuttable presumption introduced by the amendments should be interpreted. We would therefore urge you to consider addressing this issue within a reasonable timeframe by

(a) clarifying how the rebuttable presumption should be interpreted; and

(b) explaining how the final sentence in paragraph BC11 should be interpreted.

If you wish to discuss further, please do not hesitate to contact me.

Yours sincerely

[Submitter]

Appendix B—the proposed wording for agenda decision

B1. The tentative agenda decision below is proposed if the Committee thinks that the issue is clear from the existing wording in the standard.

IAS 12 *Income Tax*—Rebuttable presumption to determine the manner of recovery

Paragraph 51C of IAS 12 contains a presumption that the carrying amount of an investment property will be recovered through sale. The Committee received a request to clarify whether that presumption can be rebutted in cases other than the case described in paragraph 51C.

The Committee noted that a presumption is a matter of policy in applying a principle (or an exception) in IFRSs in the absence of acceptable reasons to the contrary and that it can be rebutted when there is sufficient evidence to overcome the presumption. Because paragraph 51C does not provide an exclusive list of cases in which the presumption can be overcome, the presumption in paragraph 51C of IAS 12 can be rebutted in circumstances other than the case given in that paragraph, provided that sufficient evidence is available to support that rebuttal. The Committee also noted that 'some cases' in paragraph BC11 of the Basis for Conclusions do not mean all cases in which an entity intends to use an investment property for a period of time and then sell it (a dual-purpose asset). The Committee noted that some cases mean a subset of cases in which the carrying amount is recovered entirely through sale even though the cases involve a dual-purpose asset.

The Committee thinks that the standard is clear and diversity in practice on the rebuttal of the presumption should not emerge. Consequently, the Committee [decided] not to add this issue to its agenda.

Appendix C—Examples of 'if and only if' used in IAS 12

73 In consolidated financial statements, a current tax asset of one entity in a group is offset against a current tax liability of another entity in the group if, and only if, the entities concerned have a legally enforceable right to make or receive a single net payment and the entities intend to make or receive such a net payment or to recover the asset and settle the liability simultaneously.

74 An entity shall offset deferred tax assets and deferred tax liabilities if, and only if:

(a) the entity has a legally enforceable right to set off current tax assets against current tax liabilities; and

(b) the deferred tax assets and the deferred tax liabilities relate to income taxes levied by the same taxation authority on either:

(i) the same taxable entity; or

(ii) different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

75 To avoid the need for detailed scheduling of the timing of the reversal of each temporary difference, this Standard requires an entity to set off a deferred tax asset against a deferred tax liability of the same taxable entity if, and only if, they relate to income taxes levied by the same taxation authority and the entity has a legally enforceable right to set off current tax assets against current tax liabilities.

Appendix D—Examples of rebuttable presumption in IFRSs

IFRS 2 *Share-based Payment*

IN5 For equity-settled share-based payment transactions, the IFRS requires an entity to measure the goods or services received, and the corresponding increase in equity, directly, at the fair value of the goods or services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the entity is required to measure their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted. Furthermore:

(a) for transactions with employees …

(b) for transactions with parties other than employees (and those providing similar services), there is a rebuttable presumption that the fair value of the goods or services received can be estimated reliably. That fair value is measured at the date the entity obtains the goods or the counterparty renders service. In rare cases, if the presumption is rebutted, the transaction is measured by reference to the fair value of the equity instruments granted, measured at the date the entity obtains the goods or the counterparty renders service.

(c) …

(d) …

(e) …

13 To apply the requirements of paragraph 10 to transactions with parties other than employees, there shall be a rebuttable presumption that the fair value of the goods or services received can be estimated reliably. That fair value shall be measured at the date the entity obtains the goods or the counterparty renders service. In rare cases, if the entity rebuts this presumption because it cannot estimate reliably the fair value of the goods or services received, the entity shall measure the goods or services received, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted, measured at the date the entity obtains the goods or the counterparty renders service.

BC119 In many share-based payment transactions with parties other than employees, it should be possible to measure reliably the fair value of the goods or services received. The Board therefore concluded that the IFRS should require an entity to presume that the fair value of the goods or services received can be measured reliably.[17] However, in rare cases in which the presumption is rebutted, it is necessary to measure the transaction at the fair value of the equity instruments granted.

[17] ED 2 proposed that equity-settled share-based payment transactions should be measured at the fair value of the goods or services received, or by reference to the fair value of the equity instruments granted, whichever fair value is more readily determinable. For transactions with parties other than employees, ED 2 proposed that there should be a rebuttable presumption that the fair value of the goods or services received is the more readily determinable fair value. The Board reconsidered these proposed requirements when finalising the IFRS. It concluded that it would be more consistent with the primary accounting objective (explained in paragraphs BC64–BC66) to require equity-settled share-based payment transactions to be measured at the fair value of the goods or services received, unless that fair value cannot be estimated reliably (eg in transactions with employees). For transactions with parties other than employees, the Board concluded that, in many cases, it should be possible to measure reliably the fair value of the goods or services received, as noted above. Hence, the Board concluded that the IFRS should require an entity to presume that the fair value of the goods or services received can be measured reliably.

BC128D Paragraph 13 of the IFRS stipulates a rebuttable presumption that the value of identifiable goods or services received can be reliably measured. The Board noted that goods or services that are unidentifiable cannot be reliably measured and that this rebuttable presumption is relevant only for identifiable goods or services.

BC237B However, the Board concluded that the entity's failure to meet a non-vesting condition is a cancellation if the entity can choose whether that non-vesting condition is met. Furthermore, the Board noted that no non-arbitrary or unambiguous criteria exist to distinguish between a decision by the counterparty not to meet a non-vesting condition and a cancellation by the entity. The Board considered establishing a rebuttable presumption that a counterparty's failure to meet a non-vesting condition is (or is not) a cancellation, unless it can be demonstrated that the entity had no (or had some) influence over the counterparty's decision. The Board did not believe that the information about the entity's decision-making processes that is publicly available would be sufficient to determine whether the presumption has been rebutted. Therefore, the Board concluded that a failure to meet a non-vesting condition should be treated as a cancellation when either the entity or the counterparty can choose whether that non-vesting condition is met.

IG5 For transactions with parties other than employees (and others providing similar services) that are measured by reference to the fair value of the equity instruments granted, paragraph 13 of IFRS 2 includes a rebuttable presumption that the fair value of the goods or services received can be estimated reliably. In these situations, paragraph 13 of IFRS 2 requires the entity to measure that fair value at the date the entity obtains the goods or the counterparty renders service.

IG5D Paragraph 13A of IFRS 2 specifies how such transactions should be measured. The following example illustrates how the entity should apply the requirements of the IFRS to a transaction in which the entity cannot identify specifically some or all of the goods or services received.

IG Example 1

Share-based payment transaction in which the entity cannot identify specifically some or all of the goods or services received

Background

An entity granted shares with a total fair value of CU100,000[2] to parties other than employees who are from a particular section of the community (historically disadvantaged individuals), as a means of enhancing its image as a good corporate citizen. The economic benefits derived from enhancing its corporate image could take a variety of forms, such as increasing its customer base, attracting or retaining employees, or improving or maintaining its ability to tender successfully for business contracts.

The entity cannot identify the specific consideration received. For example, no cash was received and no service conditions were imposed. Therefore, the identifiable consideration (nil) is less than the fair value of the equity instruments granted (CU100,000).

Application of requirements

Although the entity cannot identify the specific goods or services received, the circumstances indicate that goods or services have been (or will be) received, and therefore IFRS 2 applies.

In this situation, because the entity cannot identify the specific goods or services received, the rebuttable presumption in paragraph 13 of IFRS 2, that the fair value of the goods or services received can be estimated reliably, does not apply. The entity should instead measure the goods or services received by reference to the fair value of the equity instruments granted.

[2] In this example, and in all other examples in this guidance, monetary amounts are denominated in 'currency units (CU)'.

IFRS 3 *Business Combinations*

BC173 In developing IFRS 3, the IASB noted that the fair value of identifiable intangible assets acquired in a business combination is normally measurable with sufficient reliability to be recognised separately from goodwill. The effects of uncertainty because of a range of possible outcomes with different probabilities are reflected in measuring the asset's fair value; the existence of such a range does not demonstrate an inability to measure fair value reliably. IAS 38 (before amendment by the revised IFRS 3) included a rebuttable presumption that the fair value of an intangible asset with a finite useful life acquired in a business combination can be measured reliably. The IASB had concluded that it might not always be possible to measure reliably the fair value of an asset that has an underlying contractual or legal basis. However, IAS 38 provided that the only circumstances in which it might not be possible to measure reliably the fair value of an intangible asset that arises from legal or other contractual rights acquired in a business combination were if it either:

(a) is not separable; or

(b) is separable, but there is no history or evidence of exchange transactions for the same or similar assets, and otherwise estimating fair value would depend on immeasurable variables.

BC291 The 2005 Exposure Draft proposed a rebuttable presumption that the subsequent recognition of acquired tax benefits within one year of the acquisition date should be accounted for by reducing goodwill. The rebuttable presumption could have been overcome if the subsequent recognition of the tax benefits resulted from a discrete event or circumstance occurring after the acquisition date. Recognition of acquired tax benefits after the one-year period would be accounted for in profit or loss (or, if IAS 12 or SFAS 109 so requires, outside profit or loss). Respondents suggested particular modifications to that proposal, including removing the rebuttable presumption about subsequent recognition of acquired tax benefits within one year of the acquisition date and treating increases and decreases in deferred tax assets consistently. (IAS 12 and SFAS 109 provided guidance on accounting for decreases.) The boards agreed with those suggestions and revised the requirements of the revised standards accordingly.

IFRS 4 *Insurance Contracts*

IN8 There is a rebuttable presumption that an insurer's financial statements will become less relevant and reliable if it introduces an accounting policy that reflects future investment margins in the measurement of insurance contracts.

27 An insurer need not change its accounting policies for insurance contracts to eliminate future investment margins. However, there is a rebuttable presumption that an insurer's financial statements will become less relevant and reliable if it introduces an accounting policy that reflects future investment margins in the measurement of insurance contracts, unless those margins affect the contractual payments. Two examples of accounting policies that reflect those margins are:

(a) using a discount rate that reflects the estimated return on the insurer's assets; or

(b) projecting the returns on those assets at an estimated rate of return, discounting those projected returns at a different rate and including the result in the measurement of the liability.

28 An insurer may overcome the rebuttable presumption described in paragraph 27 if, and only if, the other components of a change in accounting policies increase the relevance and reliability of its financial statements sufficiently to outweigh the decrease in relevance and reliability caused by the inclusion of future investment margins. For example, suppose that an insurer's existing accounting policies for insurance contracts involve excessively prudent assumptions set at inception and a discount rate prescribed by a regulator without direct reference to market conditions, and ignore some embedded options and guarantees. The insurer might make its financial statements more relevant and no less reliable by switching to a comprehensive investor-oriented basis of accounting that is widely used and involves:

(a) current estimates and assumptions;

(b) a reasonable (but not excessively prudent) adjustment to reflect risk and uncertainty;

(c) measurements that reflect both the intrinsic value and time value of embedded options and guarantees; and

(d) a current market discount rate, even if that discount rate reflects the estimated return on the insurer's assets.

29 In some measurement approaches, the discount rate is used to determine the present value of a future profit margin. That profit margin is then attributed to different periods using a formula. In those approaches, the discount rate affects the measurement of the liability only indirectly. In particular, the use of a less appropriate discount rate has a limited or no effect on the measurement of the liability at inception. However, in other approaches, the discount rate determines the measurement of the liability directly. In the latter case, because the introduction of an asset-based discount rate has a more significant effect, it is highly unlikely that an insurer could overcome the rebuttable presumption described in paragraph 27.

BC124 The IFRS contains further specific requirements supporting paragraph 22:

(a) paragraph 24 permits an insurer to change its accounting policies for some insurance liabilities that it designates, without satisfying the normal requirement in IAS 8 that an accounting policy should be applied to all similar items (paragraphs BC174–BC177).

(b) paragraph 25 permits the following practices to continue but prohibits their introduction:

(i) measuring insurance liabilities on an undiscounted basis (paragraphs BC126 and BC127).

(ii) measuring contractual rights to future investment management fees at an amount that exceeds their fair value as implied by a comparison with current fees charged by other market participants for similar services (paragraphs BC128–BC130).

(iii) using non-uniform accounting policies for the insurance contracts of subsidiaries (paragraphs BC131 and BC132).

(c) paragraph 26 prohibits the introduction of additional prudence if an insurer already measures insurance liabilities with sufficient prudence (paragraph BC133).

(d) paragraphs 27–29 create a rebuttable presumption against the introduction of future investment margins in the measurement of insurance contracts (paragraphs BC134–BC144).

(e) paragraph 30 addresses 'shadow accounting' (paragraphs BC181–BC184).

(f) paragraph 45 permits an insurer to redesignate financial assets as 'at fair value through profit or loss' when it changes its accounting policies for insurance liabilities (paragraphs BC145 and BC146).

BC136 In the light of these comments, the Board replaced the prohibition proposed in ED 5 with a rebuttable presumption, which could be overcome if the other components of a change in accounting policies increase the relevance and reliability of an insurer's financial statements sufficiently to outweigh the disadvantage of introducing the practice in question (see paragraph 28 of the IFRS for an example).

BC143 It follows from the Board's conclusions on relevance and reliability (paragraphs BC123–BC125), investment management fees (paragraphs BC128–BC130) and future investment margins (paragraphs BC134–BC137) that an insurer can introduce embedded value measurements in its balance sheet only if all the following conditions are met:

(a) the new accounting policy will result in more relevant and reliable financial statements (paragraph 22 of the IFRS). This is not an automatic decision and will depend on a comparison of the insurer's existing accounting with the way in which it intends to apply embedded value.

(b) this increase in relevance and reliability is sufficient to overcome the rebuttable presumption against including future investment margins (paragraph 29 of the IFRS).

(c) the embedded values include contractual rights to future investment management fees at an amount that does not exceed their fair value as implied by a comparison with current fees charged by other market participants for similar services (paragraph 25(b) of the IFRS and paragraphs BC128–BC130).

BC144 In some measurement approaches, the discount rate is used to determine the present value of a future profit margin, which is then attributed to different periods using a formula. However, in other approaches (such as most applications of embedded value), the discount rate determines the measurement of the liability directly. The Board concluded that it is highly unlikely that an insurer could overcome the rebuttable presumption in the latter case (see paragraph 29 of the IFRS).

BC227 The following is a summary of the main changes from ED 5 to the IFRS. The Board:

(a) …

…

(h) changed the prohibition on introducing asset-based discount rates into a rebuttable presumption (paragraphs BC134–BC144).

(i) …

…

(q) …

IAS 1 *Presentation of Financial Statements*

24 For the purpose of paragraphs 19–23, an item of information would conflict with the objective of financial statements when it does not represent faithfully the transactions, other events and conditions that it either purports to represent or could reasonably be expected to represent and, consequently, it would be likely to influence economic decisions made by users of financial statements. When assessing whether complying with a specific requirement in an IFRS would be so misleading that it would conflict with the objective of financial statements set out in the *Framework*, management considers:

(a) why the objective of financial statements is not achieved in the particular circumstances; and

(b) how the entity's circumstances differ from those of other entities that comply with the requirement. If other entities in similar circumstances comply with the requirement, there is a rebuttable presumption that the entity's compliance with the requirement would not be so misleading that it would conflict with the objective of financial statements set out in the *Framework*.

BC30 In view of the strict criteria for departure from a requirement in an IFRS, IAS 1 includes a rebuttable presumption that if other entities in similar circumstances comply with the requirement, the entity's compliance with the requirement would not be so misleading that it would conflict with the objective of financial statements set out in the *Framework*.

IAS 12 *Income Taxes*

51C If a deferred tax liability or asset arises from investment property that is measured using the fair value model in IAS 40, there is a rebuttable presumption that the carrying amount of the investment property will be recovered through sale. Accordingly, unless the presumption is rebutted, the measurement of the deferred tax liability or deferred tax asset shall reflect the tax consequences of recovering the carrying amount of the investment property entirely through sale. This presumption is rebutted if the investment property is depreciable and is held within a business model whose objective is to consume substantially all of the economic benefits embodied in the investment property over time, rather than through sale. If the presumption is rebutted, the requirements of paragraphs 51 and 51A shall be followed.

Example illustrating paragraph 51C

An investment property has a cost of 100 and fair value of 150. It is measured using the fair value model in IAS 40. It comprises land with a cost of 40 and fair value of 60 and a building with a cost of 60 and fair value of 90. The land has an unlimited useful life.

Cumulative depreciation of the building for tax purposes is 30. Unrealised changes in the fair value of the investment property do not affect taxable profit. If the investment property is sold for more than cost, the reversal of the cumulative tax depreciation of 30 will be included in taxable profit and taxed at an ordinary tax rate of 30%. For sales proceeds in excess of cost, tax law specifies tax rates of 25% for assets held for less than two years and 20% for assets held for two years or more.

Because the investment property is measured using the fair value model in IAS 40, there is a rebuttable presumption that the entity will recover the carrying amount of the investment property entirely through sale. If that presumption is not rebutted, the deferred tax reflects the tax consequences of recovering the carrying amount entirely through sale, even if the entity expects to earn rental income from the property before sale.

…

51D The rebuttable presumption in paragraph 51C also applies when a deferred tax liability or a deferred tax asset arises from measuring investment property in a business combination if the entity will use the fair value model when subsequently measuring that investment property.

BC23 After considering the responses to the exposure draft, the Board reworded the rebuttable presumption so that clear evidence would not be required to rebut it. Instead, the presumption is rebutted if an asset is held within a business model whose objective is to consume substantially all of the economic benefits embodied in the investment property over time, rather than through sale. Many respondents were concerned that, because clear evidence is an ambiguous term, the requirement to gather clear evidence would have been onerous for entities that have no problem applying the existing principle in IAS 12, and could have led to abuse by entities that choose whether to gather clear evidence to achieve a favourable result. The Board chose to use the term 'business model' because it is already used in IFRS 9 *Financial Instruments* and would not depend on management's intentions for an individual asset. Many respondents were concerned that the presumption would lead to inappropriate results in some cases because it would not be rebutted if a minor scrap value would be recovered through sale. The Board also reworded the rebuttable presumption in order to respond to those concerns. The Board also made it clear that the presumption of recovery through sale cannot be rebutted if the asset is non-depreciable because that fact implies that no part of the carrying amount of the asset would be consumed through use (see paragraph BC6).

BC31 Many respondents to the exposure draft said that entities would not benefit from the amendments in jurisdictions in which this practice issue did not exist but would suffer from an increased administrative burden as a result of the amendments. Their criticism mainly focused on the rebuttable presumption, as discussed in paragraphs BC22 and BC23. They also said that the disclosure requirement proposed in the exposure draft would be onerous.

BC32 After considering the responses to the exposure draft, the Board narrowed the scope of the exception to apply only to investment property carried at fair value. It reworded the rebuttable presumption so that clear evidence would no longer be required to rebut the presumption. The Board also did not pursue the proposed disclosure requirement regarding the fact of, and reason for, the rebuttal. After those changes, the Board believes that the amendments will not be onerous for entities that have previously been able to establish without difficulty how they expect to recover investment property carried at fair value.

IAS 33 *Earnings per Share*

BC7 The Exposure Draft proposed that an entity should include in the calculation of the number of potential ordinary shares in the diluted earnings per share calculation contracts that may be settled in ordinary shares or cash, at the issuer's option, based on a rebuttable presumption that the contracts will be settled in shares. This proposed presumption could be rebutted if the issuer had acted through an established pattern of past practice, published policies, or by having made a sufficiently specific current statement indicating to other parties the manner in which it expected to settle, and, as a result, the issuer had created a valid expectation on the part of those other parties that it would settle in a manner other than by issuing shares.

BC8 The majority of the respondents on the Exposure Draft agreed with the proposed treatment of contracts that may be settled in ordinary shares or cash at the issuer's option. However, the Board decided to withdraw the notion of a rebuttable presumption and to incorporate into the Standard the requirements of SIC-24 *Earnings Per Share—Financial Instruments and Other Contracts that May Be Settled in Shares*. SIC-24 requires financial instruments or other contracts that may result in the issue of ordinary shares of the entity to be considered potential ordinary shares of the entity.

BC9 Although the proposed treatment would have converged with that required by several liaison standard-setters, for example, in US SFAS 128 *Earnings per Share*, the Board concluded that the notion of a rebuttable presumption is inconsistent with the stated objective of diluted earnings per share. The US Financial Accounting Standards Board has agreed to consider this difference as part of the joint short-term convergence project with the IASB.

IAS 36 *Impairment of Assets*

BC131A The Board concluded that goodwill should not be amortised and instead should be tested for impairment annually, or more frequently if events or changes in circumstances indicate that it might be impaired. IAS 22 *Business Combinations* required acquired goodwill to be amortised on a systematic basis over the best estimate of its useful life. There was a rebuttable presumption that its useful life did not exceed twenty years from initial recognition. If that presumption was rebutted, acquired goodwill was required to be tested for impairment in accordance with the previous version of IAS 36 at least at each financial year-end, even if there was no indication that it was impaired.

IAS 38 *Intangible Assets*

IN9 The previous version of IAS 38 was based on the assumption that the useful life of an intangible asset is always finite, and included a rebuttable presumption that the useful life cannot exceed twenty years from the date the asset is available for use. That rebuttable presumption has been removed. The Standard requires an intangible asset to be regarded as having an indefinite useful life when, based on an analysis of all of the relevant factors, there is no foreseeable limit to the period over which the asset is expected to generate net cash inflows for the entity.

BC19A In developing IFRS 3, the IASB noted that the fair values of identifiable intangible assets acquired in a business combination are normally measurable with sufficient reliability to be recognised separately from goodwill. The effects of uncertainty because of a range of possible outcomes with different probabilities are reflected in measuring the asset's fair value; the existence of such a range does not demonstrate an inability to measure fair value reliably. IAS 38 (as revised in 2004) included a rebuttable presumption that the fair value of an intangible asset with a finite useful life acquired in a business combination can be measured reliably. The Board had concluded that it might not always be possible to measure reliably the fair value of an asset that has an underlying contractual or legal basis. However, IAS 38 (revised 2004) provided that the only circumstances in which it might not be possible to measure reliably the fair value of an intangible asset acquired in a business combination that arises from legal or other contractual rights were if it either:

(a) is not separable; or

(b) is separable, but there is no history or evidence of exchange transactions for the same or similar assets, and otherwise estimating fair value would depend on immeasurable variables.

BC103 The following are the main changes from the Exposure Draft of Proposed Amendments to IAS 38:

(a) …

(b) The Exposure Draft proposed that, except for an assembled workforce, an intangible asset acquired in a business combination should always be recognised separately from goodwill; there was a presumption that sufficient information would always exist to measure reliably its fair value. The Standard states that the fair value of an intangible asset acquired in a business combination can *normally* be measured with sufficient reliability to qualify for recognition separately from goodwill. If an intangible asset acquired in a business combination has a finite useful life, there is a rebuttable presumption that its fair value can be measured reliably (see paragraphs BC16–BC25).

(c) …

IAS 40 *Investment Property*

53 There is a rebuttable presumption that an entity can reliably determine the fair value of an investment property on a continuing basis. However, in exceptional cases, there is clear evidence when an entity first acquires an investment property (or when an existing property first becomes investment property after a change in use) that the fair value of the investment property is not reliably determinable on a continuing basis. This arises when, and only when, comparable market transactions are infrequent and alternative reliable estimates of fair value (for example, based on discounted cash flow projections) are not available. If an entity determines that the fair value of an investment property under construction is not reliably determinable but expects the fair value of the property to be reliably determinable when construction is complete, it shall measure that investment property under construction at cost until either its fair value becomes reliably determinable or construction is completed

(whichever is earlier). If an entity determines that the fair value of an investment property (other than an investment property under construction) is not reliably determinable on a continuing basis, the entity shall measure that investment property using the cost model in IAS 16. The residual value of the investment property shall be assumed to be zero. The entity shall apply IAS 16 until disposal of the investment property.

B57 E64 included a rebuttable presumption that an entity will be able to determine reliably the fair value of property held to earn rentals or for capital appreciation. E64 also proposed a reliability exception: IAS 16 should be applied if evidence indicates clearly, when an entity acquires or constructs a property, that fair value will not be determinable reliably on a continuing basis.

B58 Some commentators opposed various aspects of this proposal, on one or more of the following grounds:

(a) the rebuttable presumption underestimates the difficulties of determining fair value reliably. This will often be impossible, particularly where markets are thin or where there is not a well-established valuation profession;

(b) …

(c) …

(d) …

B59 The Board concluded that the rebuttable presumption and the reliability exception should be retained, but decided to implement them in a different way. In E64, they were implemented by excluding a property from the definition of investment property if the rebuttable presumption was overcome. Some commentators felt that it was confusing to include such a reliability exception in a definition. Accordingly, the Board moved the reliability exception from the definition to the section on subsequent measurement (paragraphs ~~47–49~~ 53–55).