STAFF PAPER

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IASB meeting

Project	**IFRS Interpretations Committee issues**
Paper topic	IAS 37 *Provisions, contingent liabilities and contingent assets*—Levies charged for participation in a specific market—date of recognition of a liability

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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 identify the event that gives rise to a liability for other levies charged for participation in a specific market. The concern relates to when a liability within the scope of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* should be recognised and to the definition of a present obligation in IAS 37.
2. At the July 2011 meeting, the Committee decided to add this issue to its agenda with the aim of developing guidance for levies within the scope of IAS 37. At the November 2011 meeting, the Committee tentatively decided to set out the following principles regarding the accounting for a liability to pay a levy charged for participation in a specific market within the scope of IAS 37:

   (a) An entity does not have a constructive obligation to pay a levy that arises from operating in a future period as a result of being economically compelled to continue operating in that future period.

   (b) The preparation of financial statements on the going concern principle does not create a present obligation in accordance with IAS 37 and therefore does not lead to the recognition of a liability at a reporting date for levies that arise from operating in the future.

(c) The obligating event in accordance with IAS 37 for a levy charged by a public authority is the last of the necessary events that is sufficient to create the present obligation when more than one event is required to create an obligation. Consequently, for example, the obligating event for a levy that is charged if the entity undertakes discrete activities both in the current and in the previous period is the activity in the latter period as identified by the legislation.

(d) The obligating event arises progressively if the activity that creates the present obligation occurs over a period of time. For example, a liability is recognised progressively if the obligating event as identified by the legislation is the generation of revenues over a period of time.

(e) The liability for the obligation to pay a levy gives rise to an expense, unless the levy is an exchange transaction in which the entity that pays the levy receives assets or the right to future services in consideration for the payment of the levy.

(f) In accordance with IAS 34 *Interim Financial Reporting*, the same recognition principles should be applied in the interim financial statements as are applied in the annual financial statements

3. At the January 2012 meeting, the Committee reviewed and agreed with some examples that illustrate the application of the principles identified above. These examples are shown in Appendix A. The Committee tentatively decided to develop an interpretation on the accounting for levies charged by public authorities on entities that participate in a specific market. The consensus would be based on the principles identified above and would include illustrative examples.

4. However, with respect to levies that are due only if a minimum threshold is achieved, the Committee could not reach a consensus as to whether:

(a) the threshold is an obligating event (ie is a recognition criterion) and the liability should be recognised at a point in time only after the threshold is met; or

(b) the threshold is a measurement criterion and the liability should be recognised progressively as the entity makes progress to the relevant threshold if the threshold is expected to be met.

5. The Committee noted that IAS 34 provides some guidance on the accounting for tax liabilities within the scope of IAS 12 and contingent lease payments within the scope of IAS 17 *Leases*. The Committee decided to ask the Board whether the Board thinks that the rationale developed in this guidance:

   (a) only applies to interim financial statements or also applies to annual financial statements; and

   (b) is consistent with the core principle of IAS 34 that the same recognition principles should be applied in both the annual and the interim financial statements.

6. At the March 2012 meeting, the Committee will consider the Board's feedback and discuss again the issue of levies that are due only if a threshold is passed.

7. The Committee also asked the staff to consult the Board on whether they think that the characteristics of the levies that would be within the scope of the interpretation are such that they would warrant special treatment. So far, the Committee considers that it is appropriate to treat them under IAS 37.

8. The objective of this paper is to propose different alternatives by which the Board could address the questions raised by the Committee.

Structure of the paper

11. This agenda paper includes:

   (a) background information on the accounting for levies;

   (b) background information on the guidance provided in IAS 34;

(c) a presentation of the different alternatives by which the Board could address the questions raised by the Committee ;

(d) Appendix A: Illustrative examples on the accounting for levies charged for participation in a specific market; and

(e) Appendix B: staff analysis presented to the Committee at the January 2012 meeting on the accounting for levies that are due only if a minimum threshold is achieved.

Background information on the accounting for levies

12. The objective of the interpretation would be to clarify the accounting treatment applicable to levies charged by public authorities on entities that participate in a specific market that are within the scope of IAS 37.

13. Levies charged for participation in a specific market are a subset of taxes. Levies are established to provide revenue to a public authority. Levies might take various forms but they share the following characteristics:

(a) They are resources transferred to public authorities in accordance with laws and/or regulations;

(b) They are non-exchange transactions because the tax payer transfers resources to the public authority, without receiving approximately equal value directly in exchange;

(c) The participation/activity of the entity in a specific market on a specified date or period triggers the payment of the levy to the public authority as stated in the laws and/or regulations;

(d) They are recurring taxes (they might be payable by instalments);

(e) The calculation basis of the levy is based upon financial data for the current or a previous reporting period such as gross amount of sales/revenues or balance sheet data.

14. The interpretation would not address the accounting for levies that fall within the scope of IAS 12 (ie levies that are income taxes). Income taxes within the scope

of IAS 12 are also a subset of taxes. They are defined in IAS 12 as taxes that are based on taxable profit. The IFRIC noted in March 2006 that the term ‘taxable profit’ implies a notion of a net rather than a gross amount. The IFRIC also noted that any taxes that are not within the scope of IAS 12 are within the scope of IAS 37.

15. Some of the Committee members noted that levies within the scope of IAS 37 share similar characteristics with income taxes within the scope of IAS 12. They are generally assessed annually and/or are based on a measure that reflects the activity of the entity. As a result, although these levies are clearly not within the definition of income taxes, some might consider that their nature is very similar to income taxes. These Committee members also noted that the accounting for a levy within the scope of IAS 37 might be different from the accounting for a levy within the scope of IAS 12. They question whether the calculation formula of the levy should dictate the basis of accounting. One could argue that it should only affect the measurement of the liability and that all taxes should be accounted for similarly.

16. For example, levies based on revenues generated in the current period within the scope of IAS 37 (see Example 1 in Appendix A) are recognised progressively, as for income taxes. But for other levies within the scope of IAS 37, the accounting is quite different from the accounting for incomes taxes. In Examples 2 and 3 of Appendix A, some might consider that the outcome in the interim financial statements is misleading for users and is not representative of the economics of the transaction. Indeed, the full expense is accounted for in one interim reporting period, resulting in fluctuations from period to period that might be difficult to explain to users. Others might consider that the outcome is representative of the economics of the transaction and that the smoothing of interim expenses does not give a fair representation of the entity’s liabilities at the interim reporting date. Lastly, depending on the Committee’s decisions, the accounting could also be quite different for levies that are due only if a threshold is met (see section below).

17. Consequently, the Committee decided to consult the Board on whether they think that the characteristics of the levies that would be within the scope of the interpretation are such that they would warrant special treatment. So far, the Committee considers that it is appropriate to treat them under IAS 37.

Background information on the guidance provided in IAS 34

18. When the legislation specifies that the levy is due only if a minimum threshold is achieved, the question that arises is whether the existence of the threshold should affect the date of recognition of the liability or whether it should only affect the measurement of the liability. At the January 2012 meeting, the Committee considered the following example.

> Example 4: Entity D is a calendar year-end entity. An annual levy is due if Entity D generates revenues over CU50 million in a specific market in 20X1 and the amount of the levy is determined by reference to the revenues over CU50 million generated by Entity D in the market in 20X1.

19. IAS 37 or IAS 34 does not provide any guidance on the impact of thresholds on the accounting for a liability in the scope of IAS 37. But IAS 34 provides some guidance on the impact of thresholds on the accounting for liabilities in the scope of IAS 12 and IAS 17.

<u>Guidance on income taxes in IAS 34</u>

According to IAS 34 (paragraph B12), interim period income tax expense is accrued over the year using a weighted average annual tax rate expected for the full financial year applied to the income generated in the period. The weighted average annual tax rate reflects the progressive tax rate structure, ie income taxes are assessed on an annual basis. IAS 34 explicitly states that the accrual of income taxes is consistent with the requirements in IAS 12 and that the same principles would apply in both the annual and the interim financial statements.

> B12 Interim period income tax expense is accrued using the tax rate that would be applicable to expected total annual earnings, that is, the estimated average annual effective income tax rate applied to the pre-tax income of the interim period.
>
> B13 This is consistent with the basic concept set out in paragraph 28 that the same accounting recognition and measurement principles shall be applied in an interim

> financial report as are applied in annual financial statements. Income taxes are assessed on an annual basis. Interim period income tax expense is calculated by applying to an interim period's pre-tax income the tax rate that would be applicable to expected total annual earnings, that is, the estimated average annual effective income tax rate. That estimated average annual rate would reflect a blend of the progressive tax rate structure expected to be applicable to the full year's earnings…

20. In our understanding, for example, if an entity expects to earn CU20,000[1] pre-tax income in the first half-year, expects annual earnings of CU60,000 and operates in a jurisdiction with a tax rate of 0% on the first CU30,000 of annual earnings and 20% of all additional earnings, then a liability of CU2,000[2] should be recognised at the half year reporting date. Consequently, an income tax liability (in the scope of IAS 12) would be recognised before the threshold is met.

Guidance on contingent lease payments in IAS 34

21. According to IAS 34 (paragraph B7), if a lease provides for contingent payments based on the lessee achieving a certain level of annual sales, contingent rental expense are recognised in an interim reporting period before the required annual level of sales has been achieved if the achievement of the target that triggers the contingent rental expense is probable. Contingent rents are lease payments that are in the scope of IAS 17. Consequently, according to paragraph B7, a liability (in the scope of IAS 17) would be recognised before the threshold is met.

> Paragraph B7: Contingent lease payments can be an example of a legal or constructive obligation that is recognised as a liability. If a lease provides for contingent

[1] In this paper, monetary amounts are denominated in 'currency units (CU)'.

[2] CU2,000 = weighted average annual tax rate applied to first half-year income = 10% X CU20,000. Weighted average annual tax rate = ((60,000 – 30,000) X 20%) / 60,000 = 10%

> payments based on the lessee achieving a certain level of annual sales, an obligation can arise in the interim periods of the financial year before the required annual level of sales has been achieved, if that required level of sales is expected to be achieved and the entity, therefore, has no realistic alternative but to make the future lease payment.

22. Paragraph B7 does not specify whether the amount of the liability should be estimated:

    (a) on the basis of revenues generated to date in comparison with the total revenues generated over the year; or

    (b) on the basis of a straight-line allocation over the year.

23. IAS 34 does not contain any Basis for Conclusions that could explain the rationale that underlies the example on contingent lease payments. We note that IAS 17 (paragraph 25) states that contingent rents shall be charged as expenses in the periods in which they are incurred. We think that the word 'incurred' in paragraph 25 means that the expense is charged when the liability is recognised. Thus, IAS 17 does not directly address when to recognise the liability for a contingent rent payment when there is a threshold. Only IAS 34 specifically addresses this matter.

Accounting for levies when the legislation specifies that the levy is due only if a minimum threshold is achieved

24. At the January 2012 meeting, the staff presented two different views for the accounting of the liability to pay a levy in Example 4 described above:

    (a) View A: the liability is recognised progressively over 20X1 as the entity generates revenues if the entity expects to meet the annual threshold in 20X1.

    (b) View B: the liability is recognised only after the threshold is met.

25. The staff analysis presented to the Committee on this matter is shown in Appendix B of this paper. It should be noted that view A or view B would be

applied in the interim financial statements, but also in the annual financial statements (if, for example, the threshold is based on a 2 year period). In other words, the same principles would apply in the annual and in the interim financial statements.

26. The Committee could not reach a consensus on this issue. A slim majority of Committee members think that the activity performed before the threshold for a levy is met is necessary, but not sufficient, to create a present obligation as defined in IAS 37. They think that the last of the necessary events that is sufficient to create the present obligation is the activity performed only after the threshold is met, because the legislation identifies this specific threshold as the event that triggers the payment of the levy. In other words, they think that the threshold is a recognition criterion.

27. Other Committee members think that the last event necessary to create the present obligation is a continuous event that occurs over an extended period as the entity makes progress to the relevant threshold. They think that a common characteristic of the examples in IAS 34 on income taxes and contingent lease payments is that the achievement of a sales or income threshold is a continuous event (and not a succession of discrete events). Similarly, in order to reach the revenue threshold in Example 4 above, the entity has to generate the first CU50 million of revenues over the year. So each sale in a period is a contribution/part achievement to meeting the revenue threshold for that period. Although each sale might be independent from the next, they are all sales in the same lease period or income tax period or levy period (the period being the year if the threshold is assessed on an annual basis as in the examples above). They think that this situation is different from the situation in which multiple discrete events are necessary to create a present obligation and that this rationale is consistent with the fourth principle identified by the Committee and summarised in paragraph 3 (d) of this paper.

Presentation of the different alternatives by which the Board could answer the questions raised by the Committee

28. We think that there are three alternatives by which the Board could address the Committee's questions:

    (a) Alternative A: the Board could conclude that the rationale developed in the example of IAS 34 contingent lease payment applies in both the interim and annual financial statements;

    (b) Alternative B: the Board could conclude that the rationale developed in the example of IAS 34 on contingent lease payment only applies to interim financial statements;

    (c) Alternative C: the Board could decide to exclude levies from the scope of IAS 37 and to develop a specific treatment.

<u>Alternative A: the Board could conclude that the rationale developed in the example of IAS 34 contingent lease payment applies in both the interim and annual financial statements</u>

29. In other words, the Board could conclude that the example in IAS 34 on contingent lease payments is consistent with the core principle of IAS 34 that the same recognition principles are applied in an interim financial report as are applied in annual financial statements.

30. In our view, the main consequence is that, when considering the Board's feedback and discuss again the issue of levies, the Committee might conclude that the rationale developed in this example should be applied by analogy to levies with revenue thresholds that are within the scope of IAS 37. Thus, if a levy is due only if a revenue threshold is met, the liability would be recognised progressively as the entity generates revenue (if the threshold is expected to be met).

31. Indeed, although contingent lease payments are not within the scope of IAS 37, the example on contingent lease payments is based on the notions developed in IAS 37. Paragraph B7 refers to the notion of 'legal or constructive obligation', which is a notion that exists only in IAS 37. As a result, it might be considered that the obligating event in the example of IAS 34 on contingent lease payments is

the generation of sales because the liability is recognised progressively as the entity makes progress to the revenue threshold.

32. If the Board does not think that the example of IAS 34 on contingent lease payments should be applied by analogy to levies in the scope of IAS 37, we think that the Board should amend the example in paragraph B7 so that it does not refer to notions used in IAS 37.

Alternative B: the Board could conclude that the rationale developed in the example of IAS 34 on contingent lease payment only applies to interim financial statements

33. In other words, the Board could conclude that the example in IAS 34 on contingent lease payment is an exception to the core principle in IAS 34 and only applies to interim financial statements, not to annual financial statements.

34. In our view, the main consequence is that, when considering the Board's feedback and discuss again the issue of levies, the Committee might conclude that the rationale in this example should not be applied by analogy to levies that are within the scope of IAS 37 in the annual financial statements, nor in the interim financial statements (because an exception to a principle in a standard should not be applied by analogy to transactions that are not explicitly within the scope of the exception). In other words, the Committee might conclude that the liability should be recognised only after the threshold is met.

35. We think that there will be undesirable consequences and inconsistencies from acknowledging that different principles apply in interim and annual financial statements for contingent lease payments (see section below on additional consideration). Thus, if the Board was to consider that the example on contingent lease payments is inconsistent with the core principle of IAS 34, we would recommend that the Board should amend or delete this example.

Alternative C: the Board could decide to exclude levies from the scope of IAS 37 and to develop a specific treatment

36. The basis for this alternative is that some might consider that levies within the scope of IAS 37 are very similar in nature to income taxes within the scope of IAS

12 (other than the calculation formula) and yet the accounting might be quite different (see section above). However, we do not think that excluding levies from the scope of IAS 37 is appropriate. So far, the Committee also considers that it is appropriate to treat them under IAS 37.

37. We note that the problem that the Committee has faced with levies charged for participation in a specific market is the additional condition that the entities that pay those levies must still be participating in the market on a particular date or they avoid paying the levy.

Additional consideration before the Board addresses the questions raised by the Committee

38. We think that there will be undesirable consequences and inconsistencies from acknowledging that different principles apply in interim and annual financial statements. It should be noted that the question as to whether the same principles should apply in both the annual and the interim financial statements also arise:

(a) for a group's annual consolidated financial statements if some of the subsidiaries have financial year ends that are not co-terminus with the parent;

(b) when the threshold period is not co-terminus with an entity's financial year;

(c) when two distinct entities that pay the same levy have different financial year-end closing.

39. In this last case, the tension is illustrated in the following example. For example, a contingent lease payment (or a levy) is due if a minimum revenue threshold is achieved. The threshold is assessed annually based on the sales generated in a calendar year. Through the year, Entity A expects to meet the revenue threshold, which it does on 30 September 20X1. If Entity A's year-end closing is 31 December 20X1, Entity A would recognise a liability in the half-year financial statements at 30 June 20X1 (because at that date the threshold is expected to be met) and would also recognise a liability at year end (because the threshold has been met and assuming that the liability has not been settled at that date).

However, if different principles applied in interim and annual financial statements, and assuming that Entity A's year-end closing is 30 June 20X1, Entity A would not recognise a liability for the year ended at 30 June 20X1 (because the threshold has not been met at that date). As a result, in that case, the accounting is driven by the entity's closing date and not by the terms of the transaction. Users are unable to compare the financial statements of two entities that have different year-end closing.

40. These observations do not change the analysis in the preceding sections, but highlight that the issue is not simply one of interim versus annual reporting.

Questions to the Board

1. Does the Board think that the rationale developed in the example of IAS 34 on contingent lease payments applies in both the interim and annual financial statements or only applies to interim financial statements?

2. Does the Board think that the example of IAS 34 on contingent lease payments should be amended or deleted?

3. Does the Board have any views on the accounting for levies within the scope of IAS 37 that are due only if a threshold is met?

4. Does the Board think that the characteristics of the levies that would be within the scope of the future interpretation are such that they would warrant special treatment and be excluded from the scope of IAS 37?

Appendix A: Illustrated examples

A1. We provide below three examples in order to illustrate the application of the principles set out by the Committee and described above.

Example 1:

> Entity A is a calendar year-end entity. An annual levy is due if Entity A generates revenues in a specific market in 20X1 and the amount of the levy is determined by reference to revenues generated by Entity A in the market in 20X1.
>
> In this example, the liability is recognised progressively over 20X1 because the obligating event as identified by the legislation is the generation of revenues progressively over 20X1. Entity A has a present obligation to pay a levy to the extent of revenues generated to date. At any point in time in 20X1, it has a present obligation to pay a larger levy only if it generates additional revenues. The obligation to pay a levy for the revenues generated to date is independent of future revenues being generated. Entity A does not have any present obligation for revenues that will be generated in the future. In other words, the last of the necessary events that is sufficient to create the present obligation is the generation of revenues progressively over 20X1.
>
> In the half-year financial statements (at 30 June 20X1), Entity A has an obligation to pay the levy to the extent of the revenues generated from 1 January 20X1 to 30 June 20X1. In other words, an expense is recognised both in the first and second half-year reporting periods based on revenues generated in each period.

Example 2:

> Entity B is a calendar year-end entity. An annual levy is due as soon as Entity B generates revenues in a specific market in 20X1 and the amount of the levy is determined by reference to revenues generated by Entity B in the market in 20X0. Entity B starts to generate revenues in the market on 3 January 20X1.
>
> In this example, the liability is recognised at a point in time on 3 January 20X1 because the obligating event as identified by the legislation is the generation of revenues at a point in time in 20X1. The generation of revenues in 20X0 is a necessary event but is not sufficient to create a present obligation to pay a

levy. Before 3 January 2011, Entity B has no obligation. In other words, the last of the necessary events that is sufficient to create the present obligation is the generation of revenues at a point in time in 20X1. A full liability is recognised on 3 January 20X1 because at that date the amount of the levy is independent of future revenues being generated and is based on revenues generated in 20X0.

Because the liability is recognised in full on 3 January 20X1, the expense is recognised in full in the first half-year reporting period, ie there is no expense accounted for in the second half-year reporting period.

Example 3:

Entity C is a calendar year-end entity. An annual levy is due if Entity C is a bank at the end of the annual period of account. The amount of the levy is determined by reference to data in the balance sheet of Entity C at the end of the annual period of account. If the period of account is less or more than 12 months, the amount of the levy is adjusted in order to reflect the length of the period that it reflects. Entity C reports its annual financial statements on 31 December 20X1.

In this example, the liability is recognised at a point in time on 31 December 20X1 because the obligating event as identified by the legislation is to be a bank at the end of the annual period of account. Before the end of the annual period of account, Entity C does not have a present obligation to pay a levy, even if it is economically compelled to continue operating in the future and to be a bank at the end of the annual period of account. In other words, the last of the necessary events that is sufficient to create the present obligation is to be a bank at the end of the annual period of account, which does not occur until 31 December 20X1.

Because the liability is recognised in full on 31 December 20X1, the expense is recognised in full in the second half-year reporting period, ie there is no expense accounted for in the first half-year reporting period.

Appendix B: Staff analysis presented to the Committee at the January 2012 meeting on the accounting for levies that are due only if a minimum threshold is achieved

Example 4: Entity D is a calendar year-end entity. An annual levy is due if Entity D generates revenues over CU50 million in a specific market in 20X1 and the amount of the levy is determined by reference to the revenues over CU50 million generated by Entity D in the market in 20X1.

View A: the liability is recognised progressively over 20X1 as the entity generates revenues

A2. As mentioned in the first section, the Committee tentatively decided that a liability is recognised progressively if the activity that creates the present obligation occurs over a period of time. Proponents of view A think that the obligating event in Example 4 is the generation of revenues over 20X1. They think that the existence of a threshold only impacts the measurement of the liability, but not the date of recognition of the liability. They note that IAS 34 provides for examples on income taxes and contingent lease payments that are consistent with this rationale (see above).

A3. Paragraph B7 in IAS 34 describes a situation in which a lessee will pay an additional rent at the end of the year if sales for the year exceed a certain level. At an interim reporting date, if the cumulative sales threshold has not been reached, but there is a reasonable expectation that the threshold will be met by the end of the year, then a liability for the contingent rent expense is recognised progressively in the interim financial statements over the year. Although contingent lease payments are not within the scope of IAS 37, proponents of view A note that this example is based on the notions developed in IAS 37. Paragraph B7 refers to the notion of ‘legal or constructive obligation’, which is a notion that exists only in IAS 37 (and that does not exist in IAS 17). Proponents of view A think that the rationale in B7 is that the obligating event is the generation of sales over a period of time. The existence of a threshold does not impact this analysis, because it only impacts the measurement of the liability.

A4. Furthermore, proponents of view A think that levies based on revenues in the scope of IAS 37 are very similar to income taxes in the scope of IAS 12. They note that income tax liabilities are recognised progressively, as for levies based on revenues generated in the current period (see Example 1 above). They note that if the principles for the accounting for liabilities in the scope of IAS 37 were to be applied to income taxes, the obligating event of an income tax liability would be the generation of income over the year. They also observe that, in the interim financial statements, the existence of thresholds does not impact the date of recognition of a liability in the scope of IAS 12, but impacts the measurement of the liability. Proponents of view A think that the principles developed in IAS 12 and IAS 34 on income taxes should be applied by analogy to the accounting for levies in the scope of IAS 37. In Example 4, one could argue that the levy rate is 0% below the threshold and x% above the threshold. In that case, a liability would be recognised progressively using an estimated average annual levy rate.

A5. Lastly, proponents of view A think that a common characteristic of the examples in IAS 34 on income taxes and contingent lease payments is that the achievement of a sales or income threshold is a continuous event (and not a succession of discrete events). Similarly, in order to reach the revenue threshold in Example 4, the entity has to generate the first CU50 million of revenues over the year. The revenue threshold is met because sales are followed by other sales. Although each sale might be independent from the next, they are all sales in the same lease period or income tax period or levy period (the period being the year if the threshold is assessed on an annual basis as in the examples above). In other words, proponents of view A think that the last event necessary to create the present obligation is the achievement of the threshold, but that achieving the threshold in Example 4 is a continuous event that occurs over an extended period. Proponents of view A think that this situation is different from the situation where multiple discrete events are necessary to create a present obligation. In that case, they acknowledge that the last discrete event that is sufficient to create the obligation is the obligating event as defined in IAS 37.

View B: the liability is recognised only after the threshold is met

A6. Proponents of view B think that the obligating event is the generation of revenues only after the threshold is reached. Proponents of view B do not think that the entity has a present obligation before that date, because the entity could decide to stop business and not pay the levy. In other words, if the threshold has not been met at the interim reporting date, the obligation is still dependent on the entity's future conduct of its business, and IAS 37 (paragraph 19) states that no provision is recognised in that case.

A7. Proponents of view B also note that in the oilfield example in IAS 37 (Illustrative example 3), the liability for the obligation to repair the damage caused to the seabed, recognised progressively, corresponds:

(a) to a present obligation to date that is not conditional upon the future activity and

(b) to costs that the entity is obliged to incur in order to repair the damages caused to date.

This is different from a levy that is paid only if the threshold is met. In fact, before the threshold is met, the entity is not obliged to pay any levy.

A8. Furthermore, with regard to the principles set out in the first section of this paper, proponents of view B think that:

(a) The activity performed before the threshold is met is necessary but not sufficient to create the present obligation. They think that the last of the necessary events that is sufficient to create the present obligation is the activity performed only after the threshold is met, because the legislation identifies this specific threshold as the event that triggers the payment of the levy. In other words, the generation of revenues before the threshold is met does not create any present obligation in accordance with IAS 37.

(b) The entity does not have a constructive obligation to pay a levy that arises from operating in a future period, as a result of being economically compelled to continue operating in that future period.

A9. Finally, proponents of view B note that contingent lease payments are lease payments that are within the scope of IAS 17 and that income taxes are in the scope of IAS 12. Proponents of view B think that this guidance is not consistent with the principles in IAS 37 and should not be applied by analogy to levies which are in the scope of IAS 37.

Conclusion

A10. As a result, the two views in Example 4 would be the following:

> Example 4: Entity D is a calendar year-end entity. An annual levy is due if Entity D generates revenues over CU50 millions in a specific market in 20X1 and the amount of the levy is determined by reference to revenues over CU50 millions generated by Entity D in the market in 20X1.
>
> View A: the liability is recognised progressively over the year 20X1 if the required level of revenues is expected to be met, because the obligating event as identified by the legislation is the generation of revenues over the year 20X1.
>
> View B: the liability is recognised at a point in time only after the threshold is met because the obligating event as identified by the legislation is the generation of revenues only after the threshold is met.

Questions for the Committee

In Example 4 above, does the Committee think that the liability for the obligation to pay the levy should be recognised progressively over 20X1 if the threshold is expected to be met?

If not, does the Committee think that the liability should be recognised at a point in time only after the threshold is met?