IFRS

STAFF PAPER

September 2018

IFRS® Interpretations Committee meeting

Project	Payments relating to taxes other than income tax	
Paper topic	Item for continuing consideration	

CONTACT(S) Jan Carlo Pereras cpereras@ifrs.org +44 (0) 20 7246 0571

Objective

1. This paper discusses the consultation the staff had with the International Accounting Standards Board (Board) on when and how preparers of financial statements refer to the *Conceptual Framework for Financial Reporting* (*Conceptual Framework*) in accounting for particular payments of taxes that are outside the scope of IAS 12 *Income Taxes.*

2. The paper then asks the IFRS Interpretations Committee (Committee) whether it agrees with our recommendation not to add the matter to its standard-setting agenda.

Introduction

3. The Committee received a submission about how to account for a tax deposit. In the fact pattern described in the submission, an entity and a tax authority dispute whether the entity is required to pay a particular tax. The tax is not an income tax, so it is not within the scope of IAS 12. Any liability or contingent liability to pay the tax is instead within the scope of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. Taking account of all available evidence, the preparer of the entity's financial statements judges it probable that the entity will not be required to pay the tax—it is more likely than not that the dispute will be resolved

in the entity's favour. Applying IAS 37, the entity discloses a contingent liability and does not recognise a liability. To avoid possible penalties, the entity has deposited the disputed amount with the tax authority. Upon resolution of the dispute, the tax authority will either refund the deposit to the entity (if the dispute is resolved in the entity's favour) or use the deposit to settle the entity's liability (if the dispute is resolved in the tax authority's favour).

Submission received and discussion to date

4. The Committee considered and discussed the submission at its March and May 2018 meetings. The Committee considered whether the tax deposit gives rise to an asset, a contingent asset or neither. A contingent asset is a possible asset whose existence will be confirmed only by uncertain future events not wholly within the control of the entity (paragraph 10 of IAS 37).

5. The Committee observed that if the tax deposit gives rise to a contingent asset, that contingent asset would be within the scope of IAS 37. However, if the tax deposit instead gives rise to an asset, that asset would not clearly be captured within the scope of any IFRS Standard.

6. The Committee noted that, in the absence of an IFRS Standard that specifically applies to a transaction, an entity applies paragraphs 10–12 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Paragraph 10 of IAS 8 requires management of an entity to use its judgement in developing and applying an accounting policy that results in relevant and reliable information. Paragraphs 11–12 of IAS 8 set out a hierarchy of authoritative guidance that management considers in making that judgement (IAS 8 hierarchy):

   (a) paragraph 11 of IAS 8 requires an entity to refer to, and consider the applicability of, in descending order:

      (i) the requirements in IFRS Standards dealing with similar and related issues; and

(ii) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the *Conceptual Framework*.

(b) paragraph 12 of IAS 8 states that management may also consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework to develop accounting standards, other accounting literature and accepted industry practices, to the extent that these sources do not conflict with the sources in paragraph 11 of IAS 8.

7. In March 2018, the Board issued a revised *Conceptual Framework* (the 2018 *Conceptual Framework*). At the same time, it updated most of the references to earlier versions of the *Conceptual Framework* in IFRS Standards—including the reference in IAS 8—so that they now refer to the 2018 *Conceptual Framework*. Entities are required to apply the amended references for annual periods beginning on or after 1 January 2020. However, earlier application is permitted if an entity applies all the amendments at the same time.[1] Consequently, if an entity is applying a reference to the *Conceptual Framework* during the transition period, it could be applying a reference to either the 2018 *Conceptual Framework* or an earlier version.

8. In considering whether the tax deposit gives rise to an asset, the Committee applied the IAS 8 hierarchy and referred to the asset definition and supporting concepts in both the 2018 *Conceptual Framework* and the previous *Conceptual Framework* issued in 2010 (2010 *Conceptual Framework*). The staff paper for the Committee's May 2018 meeting explained the reason for referring to those asset definitions and concepts instead of the asset definition and requirements in IAS 38 *Intangible Assets*. The reason was that IAS 38 does not deal with issues similar or related to those arising for the tax deposit.

9. The Committee reached the same conclusions applying the asset definitions in both the 2010 *Conceptual Framework* and the 2018 *Conceptual Framework*. It concluded that, in the fact pattern described in the submission, the payment gives

[1] *Amendments to References to the Conceptual Framework in IFRS Standards*, March 2018.

rise to an asset. It gives the entity a right that will produce economic benefits. The form of the economic benefits will depend on the outcome of the dispute—if the outcome is favourable to the entity, the economic benefits will be a cash refund; if the outcome is unfavourable, the economic benefits will be the use of the payment to settle the entity's tax liability. The payment does not give rise to a contingent (possible) asset because, although there is uncertainty about the form of the economic benefits, there is no uncertainty that the entity has a right to economic benefits in one form or another. Therefore, there is no uncertainty about whether an asset exists. The Committee also observed that the entity has not recognised a liability for the disputed amount. Accordingly, if it becomes probable that an outflow of future economic benefits will be required for the disputed amount, the entity would recognise a provision in the period in which the change in probability occurs. At that time, the entity would consider any implications of the payment already made to the tax authority in accounting for the asset and liability.

10. However, the Committee noted that the submission had raised questions about when and how preparers of financial statements refer to the *Conceptual Framework* for assistance in developing accounting policies. The Committee decided to consult the Board on these questions.

Developments since the last Committee discussion

July 2018 Board meeting

11. In response to the Committee's decision, the staff prepared a paper for the Board to consider—for ease of reference, that Board paper is included as agenda paper 7A for this meeting. In that paper, the staff analysed how requirements in IAS 1 *Presentation of Financial Statements* and IAS 8 determine the process for developing an accounting policy. The staff observed that:

    (a) if an IFRS Standard specifically applies to a transaction, other event or condition, an entity applies the requirements of that Standard, even if those requirements conflict with concepts in the *Conceptual Framework*;

(b) for most transactions, other events or conditions—especially those that give rise to liabilities—there is an IFRS Standard that specifically applies;

(c) if no IFRS Standard specifically applies to a transaction, other event or condition, the entity's management refers first to requirements in IFRS Standards dealing with similar and related issues, if there are any such Standards;

(d) the entity's management refers to the definitions, recognition criteria or measurement concepts in the *Conceptual Framework* for assistance in developing accounting policies if both:

  (i) no IFRS Standard specifically applies to a transaction, other event or condition; and

  (ii) no IFRS Standards deal with similar or related issues;

(e) for some transactions, other events or conditions, there could be several issues to consider in developing an accounting policy. For some of those issues there might be an IFRS Standard dealing with similar or related issues, whereas for others there might be no such Standard. In such situations, an entity's management might refer to requirements in an IFRS Standard for some issues and to concepts in the *Conceptual Framework* for other issues; and

(f) even if no IFRS Standard specifically applies, general disclosure requirements apply.

12. The staff applied these conclusions to consider how an entity develops an accounting policy for various transactions, including tax deposits of the type discussed by the Committee (example 4 in agenda paper 7A). The staff noted that, in developing an accounting policy for such tax deposit the entity has to decide:

(a) whether the tax deposit gives rise to an asset, a contingent asset, or neither; and

(b) if the tax deposit gives rise to an asset, whether the entity recognises that asset and, if so, how it measures and presents the asset and what information it discloses about it.

13. The staff concluded that:

(a) an entity's management may refer to the *Conceptual Framework* to reach a view that the tax deposit gives rise to an asset. This is because there may be no IFRS Standard that either:

(i) specifically applies to that asset; or

(ii) deals with issues similar or related to the issue that arises in assessing whether the rights arising from paying the tax deposit meet the definition of an asset (ie whether use of the tax deposit to settle a liability is an 'economic benefit').

(b) having decided that the tax deposit gives rise to an asset, the entity's management may refer to IFRS Standards for assistance in developing policies for recognising, measuring and presenting that asset and disclosing information about it. This is because the issues that need to be addressed in developing those policies may be similar to those that arise in relation to recognition, measurement, presentation and disclosure of other monetary assets, such as financial assets within the scope of IFRS 9 *Financial Instruments* or income tax assets within the scope of IAS 12.

14. The Board discussed the staff paper at its meeting in July 2018. The Board was not asked to approve the staff analysis. However, Board members commented that the analysis was useful and suggested only a few refinements to it. The main suggestion was that the analysis should emphasise more strongly the overall objective that the IAS 8 hierarchy seeks to meet, which is to develop policies that result in relevant and reliable information.

Other development since the last Committee discussion

15. In June 2018, the Committee received correspondence from the ASCG included as Appendix B to this paper. The ASCG disagreed with the conclusions reached by the Committee at its March and May 2018 meetings. The ASCG is:

 (a) not convinced that the tax payment creates a resource that is controlled by the entity and results in potential future economic benefits. The ASCG thinks there is uncertainty about the existence of potential future economic benefits: it thinks settlement of a tax liability may not be an economic benefit because no tax liability has yet been recognised; and

 (b) not convinced that the conclusion would be the same regardless of whether the payment is voluntary or required.

16. We do not agree with the ASCG's views:

 (a) We think extinguishment or settlement of a liability would be an economic benefit irrespective of when the liability is recognised. The right exists regardless of the timing of recognition of the liability.

 (b) Whether the payment is voluntary or required, it gives the entity exactly the same right to receive future economic benefits and therefore does not affect the observation that the entity has an asset.

Staff Conclusion

17. The staff conclusion remains unchanged—the tax deposit gives rise to an asset. In making that assessment, an entity's management applies the IAS 8 hierarchy and in doing so may refer to the *Conceptual Framework*. This is because there may be no IFRS Standard that either specifically applies to that asset or deals with issues similar or related to the issue that arises in assessing whether the rights arising from paying the tax deposit meet the definition of an asset.

18. The staff conclusion is also unchanged with regards to recognition and measurement—the entity would apply the IAS 8 hierarchy in developing policies for recognising, measuring and presenting that asset and disclosing information about it. In doing so it may refer to IFRS Standards for assistance. This is because the issues that need to be addressed in developing those policies may be

similar to those that arise in relation to recognition, measurement, presentation and disclosure of other monetary assets.

19. In the fact pattern described in the submission, the entity's management has judged it probable that the entity will not be required to pay the tax so the entity has not recognised a liability for the disputed amount. If it becomes probable that an outflow of future economic benefits will be required for the disputed amount, the entity would recognise a provision in the period in which the change in probability occurs. At that time, the entity would consider any implications of the payment already made to the tax authority in accounting for the asset and liability.

Question 1 for the Committee
1. Does the Committee agree with our analysis of the requirements in IFRS Standards and the *Conceptual Framework* that, in the fact pattern described in the submission, the entity (a) has an asset when it makes the payment to the tax authority, and (b) applies IAS 8 in developing policies for recognising, measuring and presenting the asset and disclosing information about it?

Should the Committee add this matter to its standard setting agenda?

Is it necessary to add to or change IFRS Standards to improve financial reporting?[2]

20. Based on our analysis in this paper (and previous agenda papers discussed in March and May 2018), we think that the requirements in existing IFRS Standards and the *Conceptual Framework* provide an adequate basis for the entity to account for payments relating to taxes other than income tax.

[2] Paragraph 5.16(b) of the *Due Process Handbook*.

Staff recommendation

21. Based on our assessment of the Committee's agenda criteria in paragraphs 5.16–5.17 of the *Due Process Handbook* (discussed in paragraph 20 above), we recommend that the Committee does not add this matter to its standard-setting agenda. Instead, we recommend publishing an agenda decision that outlines how an entity applies the requirements in IFRS Standards and the *Conceptual Framework* to payments relating to taxes other than income tax.

22. Appendix A to this paper sets out the proposed wording of the tentative agenda decision. The tentative agenda decision refers to payments made by an entity, and not specifically to voluntary payments made. Although the request asked only about voluntary payments, we think the voluntary nature of a payment, in isolation, would not change our analysis. Accordingly, we have clarified in the tentative agenda decision that the payment need not be voluntary.

23. We have also reinforced in the fact pattern in the tentative agenda decision that in not recognising a liability, the entity has appropriately applied IAS 37. This has been done by referring to some of the requirements from the applicable paragraph (paragraph 16) of IAS 37.

Questions 2 and 3 for the Committee
2. Does the Committee agree with our recommendation not to add this matter to its standard-setting agenda? 3. Does the Committee have any comments on the proposed wording of the tentative agenda decision set out in Appendix A to this paper?

Appendix A—Proposed wording of the tentative agenda decision

IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*—Payments relating to taxes other than income tax

The Committee received a request about how to account for particular payments of taxes that are outside the scope of IAS 12 *Income Taxes* (ie payments for taxes other than income tax). In the fact pattern described in the request, an entity and a tax authority dispute whether the entity is required to pay a particular tax. The tax is not an income tax, so it is not within the scope of IAS 12. Any liability or contingent liability to pay the tax is instead within the scope of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. Taking account of all available evidence, the preparer of the entity's financial statements judge it probable that the entity will not be required to pay the tax—it is more likely than not that the dispute will be resolved in the entity's favour. Applying IAS 37, the entity discloses a contingent liability and does not recognise a liability. To avoid possible penalties, the entity has deposited the disputed amount with the tax authority. Upon resolution of the dispute, the tax authority will either refund the deposit to the entity (if the dispute is resolved in the entity's favour) or use the deposit to settle the entity's liability (if the dispute is resolved in the tax authority's favour).

The Committee considered whether the tax deposit gives rise to an asset, a contingent asset or neither.

The Committee concluded that there is no IFRS Standard that deals with issues similar or related to the issue that arises in assessing whether the rights arising from particular payments of taxes meet the definition of an asset. Accordingly, the Committee referred to the two definitions of an asset now in IFRS literature—the new definition in the *Conceptual Framework for Financial Reporting* issued in March 2018 and the definition in the previous *Conceptual Framework* that was in place when many existing IFRS Standards were developed. The Committee concluded that the payment made by the entity meets either of those definitions. The payment gives the entity a right to obtain future economic benefits, either by receiving a cash refund or by using the payment to settle the tax liability. The nature of the payment—whether voluntary or required—does not affect this right and therefore does not affect the conclusion that there is an asset. The payment is not a contingent asset as defined by IAS 37 because it is an asset, and not a possible asset, of the entity.

Consequently, the Committee concluded that in the fact pattern described in the request the entity has an asset when it makes the payment to the tax authority.

The Committee also observed that the asset may not be clearly within the scope of any IFRS Standard. In the absence of a Standard that specifically applies to a transaction, an entity applies paragraphs 10–11 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* in developing and applying an accounting policy for the asset. The entity's management uses its judgement in developing and applying a policy that results in information that is (i) relevant to the economic decision-making needs of users of financial statements and (ii) reliable. The Committee noted that the entity's management may refer to IFRS Standards for assistance in developing the policies for recognising, measuring and presenting the asset and disclosing information about it. This is because the issues that need to be addressed in developing those policies may be similar to those that arise in relation to recognition, measurement, presentation and disclosure of other monetary assets.

The Committee concluded that the requirements in IFRS Standards and the *Conceptual Framework for Financial Reporting* provide an adequate basis for an entity to account for payments relating to taxes other than income tax. Consequently, the Committee [decided] not to add this matter to its standard-setting agenda.

Appendix B—Correspondence from the Accounting Standards Committee of Germany

Deutsches Rechnungslegungs Standards Committee e.V.

Accounting Standards Committee of Germany

DRSC

ASCG • Zimmerstr. 30 • 10969 Berlin

Sue Lloyd
Chair of the IFRS Interpretations Committee
30 Cannon Street
London EC4M 6XH

United Kingdom

IFRS Technical Committee
Phone: +49 (0)30 206412-12
E-Mail: info@drsc.de

Berlin, 26 June 2018

Dear Sue,

Re: Flagging concerns regarding the most recent IFRS IC's discussion on "Voluntary payments" in the March & May 2018 meetings

On behalf of the Accounting Standards Committee of Germany (ASCG), I am writing to comment on the issue "Payments relating to taxes other than income taxes" as discussed by the IFRS Interpretations Committee (IFRS IC) in its meetings in March and May 2018 and on the findings as published in the respective *IFRIC Updates*.

We consider the IFRS IC's tentative conclusions in respect of this issue neither precise nor sufficient.

Acknowledging that the findings aim at (only) addressing the fact pattern in the request, we do not fully agree with two specific findings. Firstly, we are not convinced that the payment indeed creates a resource that is controlled by the entity and results in potential future economic benefits. In this regard, it is particularly the second part that seems debatable. Some of us argue that the voluntary payment may not be used to settle the tax liability, since no tax liability has been recognised yet. Thus, there is still uncertainty about the *existence of* future economic benefits, not only about *the form of* those benefits. In other words, there is a contingency. Secondly, the findings do not contribute to clarity since they address payments that an entity pays "either voluntary or because it is required to do so". If phrased this way, it remains unclear and debatable why the answer does not differ when considering "voluntary" and "required" payments. We would have expected that voluntariness is a crucial point in this fact pattern.

Deutsches Rechnungslegungs Standards Committee e.V.

Accounting Standards Committee of Germany

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Further, we deem the issue under discussion being part of a broader question, which is how to account for any kind of payments before they become due or payments that are "voluntary" in character (eg. prepayments, overpayments, deposits, etc.) and which we believe deserves deliberation. The IFRS IC's findings do not allow for being carried over to other, similar or comparable, voluntary payments. Moreover, the IFRS IC's rationale – the issue (i.e. asset) is not captured by any IFRS, hence, IAS 8.10 et seq. apply – leaves, or even opens, much room for interpretation.

In summary, we feel that the broader issue of accounting for any kind of "voluntary payments" remains unanswered – and possibly becomes even more unclear with these recent findings.

If you would like to discuss our views further, please do not hesitate to contact Jan-Velten Große (grosse@drsc.de) or me.

Yours sincerely,

Andreas Barckow

President