IFRIC Interpretation DI/2015/1
Uncertainty over Income Tax Treatments

Request for views issued by the IASB in October 2015

Comments from ACCA
18 January 2016

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Further information about ACCA's comments on the matters discussed here may be obtained from the following:

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ACCA welcomes the opportunity to provide views in response to the request from the International Accounting Standards Board.

MAIN COMMENTS

ACCA supports the Interpretation Committee's proposed draft Interpretation *Uncertainty over Income Tax Treatments* as it contributes to greater clarity and consistency in accounting approaches in this area.

We would urge the Interpretation Committee to consider further the difficulties of recognising and disclosing the effects of uncertainty over income tax treatments in the period to which the income tax treatments relate, without using hindsight.

We would also encourage the Interpretation Committee to clarify the Interpretation in relation to the following areas:

- Whether adjustments reflecting changes in facts and circumstances should be recognised prospectively or retrospectively,
- The possibility of offsetting tax assets against tax liabilities when considering uncertain tax treatments collectively, and
- The circumstances in which an implicit acceptance from the taxation authority can be assumed.

Finally, we would recommend the Interpretation Committee to consider exploring the potential for alignment between IAS 12 and IAS 37. We note that the concept of probability underlies both standards, and IAS 37 disclosure requirements in respect of contingent liabilities and contingent assets are referred to in IAS 12. We believe that the quality of financial reporting will benefit from greater consistency between the two standards.

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SPECIFIC COMMENTS ON QUESTIONS RAISED

Q1. Scope of the draft interpretation

> The draft Interpretation provides guidance on accounting for current and deferred tax liabilities and assets in circumstances in which there is uncertainty over income tax treatments. Such uncertain tax treatments may affect taxable profit (tax loss), tax bases, tax credits or tax rates that are used to recognise and measure current or deferred tax liabilities or assets in accordance with IAS 12 *Income Taxes*.
>
> Do you agree with the proposed scope of the draft Interpretation? If not, why and what alternative do you propose?

We agree with the proposed scope of the draft Interpretation.

Currently, a diversity in the accounting treatment for uncertain tax positions exists and we believe this draft Interpretation is a step towards establishing consistent accounting treatment.

We also agree with the inclusion of both current and deferred tax within the scope of the draft Interpretation.

Q2. When and how the effect of uncertainty over income tax treatments should be included in determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates

> The draft Interpretation requires an entity to consider whether it is probable that a taxation authority will accept an uncertain tax treatment, or group of uncertain tax treatments, that it used or plans to use in its income tax filings.
>
> If the entity concludes that it is probable that the taxation authority will accept an uncertain tax treatment, the draft Interpretation requires the entity to determine taxable profit (tax loss), tax bases, unused tax losses, unused tax credits or tax rates consistently with the tax treatment included in its income tax filings.
>
> If the entity concludes that it is not probable that the taxation authority will accept an uncertain tax treatment, the draft Interpretation requires the

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entity to use the most likely amount or the expected value in determining taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates. The method used should be the method that the entity concludes will provide the better prediction of the resolution of uncertainty.

Do you agree with the proposal in the draft Interpretation on when and how the effect of uncertainty should be included in the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates? If not, why and what alternative do you propose?

We agree broadly with the approach set out for the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates.

We believe that the timing of the recognition or disclosure of uncertain tax positions require further clarification. We note that in most tax jurisdictions, with the exception of specific advance agreements made with tax authorities (such as Advance Pricing Agreements for transfer pricing purposes), the tax treatments adopted in entities' income tax filings would not have been finalised at the end of the accounting period. It would therefore be extremely difficult for many entities to determine the probability of uncertain tax treatments being accepted or rejected in the reporting period to which the tax treatments relate, without the use of hindsight.

Consequently, to appropriately account for the effect of uncertain tax treatments, it is crucial for entities to consider changes in facts and circumstances that affect its conclusions about the acceptability of tax treatments or its estimates of the effect of uncertainty, in reporting periods subsequent to the reporting period to which the tax treatments relate. This is considered in paragraph 18 of the draft Interpretation, which states that any such change would be reflected in the period of the change. We would encourage the Interpretation Committee to strengthen guidance in this important area by making specific reference to IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. The wording of the draft Interpretation implies the changing effects of uncertain tax positions should be recognised consistently with paragraphs 36 to 40 of IAS 8, as changes in accounting estimates. This would further suggest that prospective recognition would be applied; however, the transitional guidance set out in B2 (b) contradicts this. We would encourage the Interpretation Committee to further

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consider consequences of adopting prospective recognition over retrospective recognition, and clarify the recognition basis in the Interpretation accordingly.

We welcome the use of 'probability' as both a recognition threshold and a measurement model. We also agree with Interpretation Committee's decision to allow for a choice between the single most likely amount and the expected value. This is because the calculation of expected values could prove difficult, as the identification of an unspecified number of individual outcomes and the assignment of an individual probability to each outcome are difficult to achieve in many tax jurisdictions.

Q3. Whether uncertain tax treatments should be considered collectively

The draft Interpretation requires an entity to use judgement to determine whether each uncertain tax treatment should be considered independently, or whether some uncertain tax treatments should be considered together, in order to determine taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates.

Do you agree with the proposal in the draft Interpretation on the determination of whether uncertain tax treatments should be considered collectively?

If not, why and what alternative do you propose?

We agree that entities are permitted to make judgements regarding whether each uncertain tax treatment should be considered separately, or whether some uncertain tax treatments should be considered collectively.

However, there is a risk that dissimilar current or deferred tax assets and liabilities are offset against one another, reducing the clarity of the financial statement disclosure. We would recommend that the draft Interpretation makes specific reference to IAS 12 paragraphs 71 and 74 in respect of the offset of current or deferred tax assets and liabilities.

Q4. Assumptions for taxation authorities' examinations and the effect of changes in facts and circumstances

The draft Interpretation requires an entity to assume that a taxation authority with the right to examine any amounts reported to it will examine those amounts and will have full knowledge of all relevant information when making those examinations.

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The draft Interpretation also requires an entity to reassess its judgements and estimates if facts and circumstances change. For example, if an entity concludes that new information indicates that it is no longer probable that the taxation authority will accept an uncertain tax treatment, the entity should reflect this change in its accounting. The expiry of the period in which the taxation authority may examine the amounts reported to it would also be an example of a change in circumstances.

Do you agree with the proposal in the draft Interpretation on the assumptions for taxation authorities' examinations and on changes in facts and circumstances? If not, why and what alternative do you propose?

We agree with the required assumption that a taxation authority with the right to examine any amounts reported to it will examine those amounts and will have full knowledge of all relevant information when making those examinations.

We also agree with the requirement for entities to reassess its judgements and estimates in subsequent reporting periods if facts and circumstances change. For reasons discussed above in our response to Question 2, we believe this requirement is essential.

Paragraph A6 of the draft Interpretation cites the taxation authority's silence about tax treatments as an implicit acceptance, constituting a new fact for tax treatments within the scope of the examination. However, jurisdictions such as the UK have extended periods for agreeing to claims for tax reliefs, allowing the taxation authority to challenge such claims several years after the reporting period to which they relate. We would suggest that the example in paragraph A6 is reworded to specify that the taxation authority's silence about tax treatments should not be taken as an implicit acceptance until such time that the taxation authority's right to examine the amounts reported has expired.

Q5. Other proposals

Disclosure

The draft Interpretation does not introduce any new disclosure requirements, but highlights the relevance of the existing disclosure requirements in paragraphs 122 and 125–129 of IAS 1 *Presentation of Financial Statements*, paragraph 88 of IAS 12 and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

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Transition

The draft Interpretation requires an entity to apply its requirements by recognising the cumulative effect of initially applying them in retained earnings, or in other appropriate components of equity, at the start of the reporting period in which an entity first applies them, without adjusting comparative information. Full retrospective application is permitted, if an entity can do that without using hindsight.

Do you agree with the proposals in the draft Interpretation on the disclosure and the transition requirements? If not, why and what alternative do you propose?

Disclosure

We do not agree with the Interpretation Committee's decision not to introduce new disclosure requirements, and to refer instead to the existing disclosure requirements set out in IAS 1 *Presentation of Financial Statements*, paragraph 88 of IAS 12 and IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

The current cross-referencing between IAS 1, IAS 12 and IAS 37 is unclear, and liable to give rise to divergence in disclosure. In particular, the reference in paragraph 21 of the draft Interpretation would appear inconsistent with the explicit exclusion of income taxes from the scope of IAS 37 (paragraph 5). The disclosure requirements paragraph 125 of IAS 1 *Presentation of Financial Statements* are too general to be applied to uncertain tax treatments.

We would recommend that the Interpretation sets out specific disclosure requirements in respect of uncertainty over income tax treatments. Nevertheless, we agree that each entity should determine whether disclosure should be made in respect of uncertain tax treatments, having regard to the specific circumstances giving rise to each uncertainty.

Further, we note that income taxes are specifically excluded from the scope of IAS 37, and we observe that the recognition threshold for a tax asset arising from an uncertain tax treatment ('probable') therefore differs from the definition of a contingent asset in accordance with IAS 37 ('virtually certain'). In this context, the reference to paragraph 88 of IAS 12, which makes reference to 'tax related contingent liabilities and contingent assets' may cause confusion. We would recommend the Interpretation Committee to clarify how a tax asset arising from uncertain tax treatments should be distinguished from a tax-related contingent asset.

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As a related point, the reference in paragraph 21 of the draft Interpretation to 'tax-related contingences' may cause confusion. We would recommend that this is reworded to refer to the effects of uncertainty over income tax treatments where the entity concludes that it is probable that the treatment will be accepted by the taxation authority.

Transition

We welcome the choice permitted between making full retrospective application and adjusting the cumulative effect of initially applying the Interpretation in the opening balance of retained earnings, or other appropriate components of equity.

We note that while a choice is permitted, the majority of entities are likely to opt for adjusting the opening balances of retained earnings or other appropriate components of equity. The unlikelihood of retrospective application without the use of hindsight, as described in our response to Question 1, and the accounting burden of applying retrospective adjustments where the uncertainty affects multiple prior reporting periods, will discourage preparers from retrospective application.

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