



EFRAG
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Dear Sirs

Improving the financial reporting of income taxes

ACCA (Association of Chartered Certified Accountants) welcomes the opportunity to comment on the above discussion paper (DP). This was considered by ACCA's Corporate Reporting Global Forum and I am writing to give you their views.

ACCA is a professional accountancy body which is based in the UK but which operates on a global basis. We currently have 154,000 qualified members and 432,000 students training for the ACCA qualification. Over 200,000 of our members and students are based in EU countries. Our members work across the range of business sectors, including business, finance, audit and the public sector.

We set out below some overall comments and then our responses to the specific questions raised for comment in the DP.

Overall comments

We agree that the subject of the accounting for income taxes should be considered for inclusion on the agenda of the IASB. Ultimately the IASB needs to decide whether to make any changes to IAS12, improve the standard or work towards a replacement. In our view EFRAG and the ASB have helpfully identified the key potential improvements and the main possible models for accounting for taxes for any more fundamental reconsideration of deferred tax

accounting. The DP's findings and the responses to it should now be passed to IASB and they will no doubt be helpful to them in making their decisions.

ACCA's responses to the questions raised

Part 1 Possible amendments to IAS12

Q0.1 Are there deficiencies in IAS12? Limited amendments to IAS12 or a new standard on different principles?

Though it seems that the temporary difference method of IAS12 is working and understood by preparers and auditors, we have reservations about

- how well it is in practice complied with
- the complexities introduced via the inconsistencies and exceptions in the standard (for example those set out in Part 2 paragraphs 2.13 to 2.44) which also call into question the model on which it is based.
- deferred tax credit balances often represent amounts that will never be paid and potentially confuse rather than explain the difference between cash paid and the accounting tax charge
- whether the current model is consistent with the conceptual framework, especially deferred tax liabilities and the definition of liabilities
- the consistency of IAS12 liabilities and others in respect of discounting
- most significantly perhaps, whether the deferred tax model is either understood or required by users of financial statements. We note that the user needs (see 1.7) surveyed in Chapter 1 do not point to the need for any deferred tax accounting as such, but to an interest in estimating future effective tax rates.

We have noted to the IASB that starting a new project to replace or substantially alter an accounting standard needs to be justified. In assessing that case for IAS12, it appears there is no significant gap in IFRS, nor a fundamental problem in practice with the existing standard. However there is a possibility for there to be significant gains in terms of a reduction in complexity compared to the existing IAS12.

On those grounds we favour a consideration of a new standard for income taxes. However any fundamental change will ultimately need to be justified by its cost/benefits. Any reconsideration of IAS12 should not be limited to the accounting model but should include the disclosure and other improvements to existing IAS12 as well.

Q1.1 A reconciliation of taxes paid to current tax expense?

We are conscious of the general ‘cutting clutter’ agenda and on the whole new disclosure requirements should be matched by disclosure requirements deleted. The difference between taxes paid and the current tax portion of the total tax charge reflects the normal effects of accrual accounting and such a reconciliation is not commonly done for other items.

However it would generally be straightforward to produce. It could be done either by producing the reconciliation or by analysing the balance sheet amounts between prior years, current and prepaid. The reconciliation might more helpfully be between taxes paid and the overall tax charge including deferred tax.

Q1.2 Details of deferred tax assets especially unused losses and tax credits

Some explanation is already required by IAS12.82, and the issue in our view is more about improving the quality of implementation of existing requirements than adding new requirements. As with Q1.1 the imposition of new disclosures needs to be justified in the ‘cutting clutter’ context.

Q1.3 Identifying user needs

We agree with the needs identified. We note that the main thrust of users’ needs is towards understanding current tax and estimating likely future effective tax rates. A key part of being able to do this will be some tax allocation to the segmental information that the users are provided with pre-tax. Greater disclosures of tax paid do seem to be a trend – for instance the new requirements for extractive companies being proposed in the EU directive. See also Q1.6

Q1.4 Disclosing tax strategies in the management commentary not the financial statements

While potentially interesting to users estimating future effective tax rates, a requirement for companies to discuss their tax strategies is unlikely to be very helpful. Companies will probably be unwilling to be very transparent in this area, knowing that the tax authorities may be taking a close interest. Boiler

plate statements of the most general sort look very likely. If it were to be asked for then the management commentary seems a better place than the financial statements, given that it concerns future rates of tax rather than an analysis of the current position.

Q1.5 Suggestions for standardising the tax rate reconciliation

We agree with the proposals for a standard structure to the tax reconciliation and an encouragement for “other items” not to become too large without further analysis and explanation. However this latter is a matter of materiality and we have not on the whole favoured “bright lines” (such as the DP’s proposed 5%) in the standards. Hopefully IASB will be taking up a project on disclosures in general and materiality considerations are bound to be a significant element of that. There could also be a standardisation on the rate of tax to be used – either the rate applying in the domicile of the holding company, country of principal operation or a basket of rates of the various states where the group operates.

Q1.6 Limited information about future tax cash flows

As noted above in answer to Q1.3 this seems to be the main objective of the users’ requests for information in 1.7. Given that, it might make more sense for the company simply to give some estimates of future effective tax rates and the main assumptions in making them.

Q1.7 Should discounting deferred tax amounts be required?

We agree in principle to discounting deferred tax balances for consistency with other sorts of liability in IFRS financial statements. Amounts to be paid at some distant time are going to be very much overstated otherwise in comparison to more immediate liabilities. Some of the problems with IAS12 would diminish with discounting simply because the balances would be significantly reduced.

However we acknowledge the significant complexities of the calculation including the estimation of when the liabilities will crystallise, the discount rate to be used and the treatment of differences on items that themselves already represent discounted future cash flows.

Q1.8 Accounting for uncertain tax positions

In our view the accounting and disclosures for uncertain tax positions should be carried out under IAS37, making them comparable to all other sorts of provision. This would mean that uncertain tax positions would be disclosed in the financial statements either as actual provisions or as contingencies depending on the likelihood of a pay-out. Where there are a number of uncertain issues some probability weighting seems to make sense. In cases where there may be a single issue the most likely outcome may be the most appropriate. In assessing the likelihood of a pay-out, the likelihood of whether there will be a review by the tax authorities in the first place needs to be included.

We see no reason why the disclosure restrictions in cases where there might be serious prejudice (IAS37.92) should not apply to these uncertain tax positions.

Q1.9 Other issues with IAS12?

See our answer to Q0.1 above.

Q1.10 Views on the exemptions currently in IAS12

The exceptions have proved workable, but they also challenge the validity of the temporary difference model on which it is based. They do produce different outcomes in cases that look to be broadly comparable. See also our answer to Q0.1 above.

Part 2 Alternative approaches to accounting for income tax

Q2.1 Which of the different models have most merit to be further developed?

All of the 5 models (including the temporary difference approach of IAS12) considered seem to have some merits and some problems. The pro's and con's of each of these seem fairly considered in each of the chapters. However one of the tests that should be applied is consistency with the Framework and especially the definition of liabilities and assets. In the DP this has only really been done for the Accruals approach.

We have noted the apparent lack of interest by users in any deferred tax and that the principal justification of any new standard would have to be in terms of a reduction in complexity. These would point towards the flow through method. However we note the move away from accruals accounting and other disadvantages that the use of this method would entail. At this point we are not clearly in favour of one rather another of the methods outlined.

So any future discussion paper should at least assess the advantages and difficulties of each of the models, including the compliance with the conceptual framework (as noted above). It would help to have some of the common items (such as accelerated depreciation, interest received, revaluations, acquisitions etc.) worked through each of the models to see the effects of applying each of them. Also pilot studies of the application of the different models to different sorts of company, would be instructive in assessing both difficulties and advantages in the models and practical issues of application.

Q2.2 Specific practical difficulties

See our response to Q2.1 above.

Q2.3 Other approaches?

We do not think there are other relevant models to consider.

Q2.4 A combination of approaches?

We would not expect that to be helpful.

If there are any matters arising from the above please be in touch with me.

Yours sincerely



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