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Dear Sirs

EFRAG Discussion Paper: Improving the Financial Reporting of Income Tax

We appreciate the opportunity to comment on the EFRAG Discussion Paper, Improving the Financial Reporting of Income Tax (DP). As an international network, KPMG has a global process in place to respond to international standard setters and similar organisations on behalf of its member firms worldwide. The views expressed in this letter are those of the KPMG member firms in the European Union. Below we summarize our main comments. More detailed responses to the specific questions raised in the DP are set out in the appendix to this letter.

Overall, we support EFRAG's initiative to take a step back and reconsider fundamental recognition and measurement principles as well as disclosure issues. However, we believe that the current guidance on recognition and measurement in IAS 12 is sufficient and widely understood. Therefore, in our view, neither a rethink nor major repairs of the Standard are required.

While we agree with EFRAG's efforts that the Standard should be improved to better address user needs by focusing on information regarding future tax cash flows, it is not clear in the DP what specific information users are demanding to achieve this goal.

We believe that agenda items should be added to the IASB's agenda only when there is strong evidence of a major problem with, or deficiency in, current standards. This evidence is not yet available with respect to IAS 12. We suggest therefore – before making any changes to the current income tax standard – that more specific research is done on exactly what kind of information users would find most beneficial. Furthermore, it should be clearer what information is really relevant in terms of tax reporting, especially if information for future tax cash flows is provided only by a proxy of actual tax cash flows and other information. Therefore, it should be analysed what information would be the best proxy of future tax cash flows and as a consequence meets users' needs best. Only after a comprehensive understanding of the type of information and depth of the user needs is established, we will be in a better position to answer the key question of the DP whether a fundamental rethink of IAS 12 – including the introduction of a new accounting approach for income taxes – is needed or changes made through amendments to IAS 12 would suffice.

However, such a research project should only be conducted after consultation with the IASB.

At this time we would not support the IASB putting reporting of income tax back on its agenda, due to other high priorities.

Any new disclosure requirements with respect to taxes should not simply be additive and increase the reporting burden. Such an approach would add to the complexity of communicating tax information, which the DP seeks to avoid. Instead, the focus should be to enhance current disclosures and remove non-value disclosures to better suit user needs. Various stakeholders in the financial reporting community have expressed concerns about disclosure overload and meaningless specific disclosures. We share these concerns and welcome the fact that EFRAG is working in another pro-active project on the development of a disclosure framework.

None of the approaches discussed in the second part of the DP (A review of approaches to accounting for income taxes) seems to be able to remedy all issues of concern raised in the DP. Due to this fact, we believe that a broader and more detailed research is necessary to thoroughly analyse the alternative approaches, the pros and cons of discounting as well as the usefulness of current and additional disclosures.

Although we believe that at this point in time changes to the Standard, if any, should have a low priority, we have commented in Appendix A on the specific issues EFRAG proposed to be addressed (see our response to question Q0.1).

We hope that our comments will be useful. Should you have any question please contact Mark Vaessen +44 (20) 7694 8589 or Winfried Melcher +49 (30) 2068 4671 directly.

Yours faithfully

KPMG LLP

KPMG LLP

Appendix A

Question to constituents – General

Q0.1 Do you consider that there are deficiencies in IAS 12 that should be addressed? If so, should they be addressed through limited amendments to the standard or by developing a new standard based on different principles?

Key Comments:

a) In whole, we support EFRAG's initiative to take a step back and reconsider fundamental recognition and measurement principles as well as disclosure issues, although we think that this project should only have a low priority for the IASB given other unresolved issues on its agenda.

b) We believe that the current guidance on recognition and measurement in IAS 12 is sufficient and widely understood, and major repairs of the Standard are not required.

c) Before answering the question, whether the disclosure issues set out in paragraph 1.7 of the DP are a sign of an overall deficient current approach in IAS 12 or are only singular problems that can be remediated via an amendment of the current standard, more information of the users' needs in respect of income tax reporting is necessary.

d) We suggest – before making any changes and after consulting with the IASB – carrying out a wider, more specific study on exactly what kind of (decision-useful) information users would find most beneficial in terms of income tax reporting, especially if information for future tax cash flows is provided only by proxies of actual tax cash flows and other information. Therefore, it should be analysed what information would be the best proxies of future tax cash flows and as a consequence meets users' needs best.

e) Only after a comprehensive understanding of the type of information and depth of the users' needs is established, we will be in a better position to answer the key question of the DP whether a fundamental rethink of IAS 12 – including the introduction of a new accounting approach for income taxes – is really needed or changes made through amendments to IAS 12 would suffice.

f) Furthermore, no additional disclosure requirements should be implemented without reassessing the real need of currently existing disclosures. Any new disclosure requirements should not simply be additive and increase the reporting burden. Such an approach would add to the complexity of communicating tax information, which the DP seeks to avoid. Instead, the focus should be to enhance current disclosures and remove non-value disclosures to better suit user needs ("Cutting the Clutter" as in EFRAG's pro-active disclosure framework project). We also note that some of the regulators and enforcers are questioning the amount of disclosures, thus obscuring the really relevant information.

Questions to constituents – Part 1: Possible amendments to IAS 12

Q1.1 Under current IAS 12 a difference between the tax paid and the current tax expense reported in the income statement leads to misunderstandings of these relationships. Do you agree that additional disclosure that would provide a reconciliation of the taxes paid and current tax expense will help in understanding this relationship? (Paragraphs 1.15 to 1.18)

Key Comments:

a) Due to the accrual method of accounting there is a difference between tax paid and the current tax expense reported in the income statement as is the case in nearly every other caption (e.g. sales cash flows in and sales recognized, accruals set up and cash flows out for the usage of accruals).

b) It is not clear, if a reconciliation of income taxes paid and current income tax expense would really help to meet users' demands. Therefore, more research is required to find out what users' needs really are. Only if a valid reason exists, should a reconciliation of income tax expense and income tax paid be required, keeping in mind that such a reconciliation is not required for other material captions in the financial statements (e.g. sales or accruals).

Q1.2 Do you agree that additional more detailed disclosures regarding deferred tax assets, especially unused tax losses and unused tax credits are necessary and useful? (Paragraphs 1.23 to 1.24)

Key Comments:

a) Disclosure requirements according to IAS 12.81(e) are more of a general nature. This allows preparers to tailor the disclosures to better fit the company's specific facts and circumstances. However, it is unclear what users really are looking for and which additional information would better serve their needs.

b) Any new disclosure requirements with respect to taxes should not simply be additive and increase the reporting burden. Such an approach would add to the complexity of communicating tax information, which the DP seeks to avoid. Instead, the focus should be to enhance current disclosures and remove non-value disclosures to better suit user needs. Various stakeholders in the financial reporting community have expressed concerns about disclosure overload and meaningless specific disclosures. We share these concerns and welcome the fact that EFRAG is working in another pro-active project on the development of a disclosure framework. This will help to focus on cutting non decision-useful clutter before considering adding more items to the existing disclosure list.

Q1.3 Do you agree with the identified users' information needs in Chapter 1 of Part 1? Do you have any suggestion for additional information requirements regarding reporting of income taxes? (Paragraphs 1.8 to 1.24)

Key Comments:

a) We strongly believe that the analysis in the current DP is not detailed enough and needs to focus more on the question what users' needs really are and if information on actual income tax cash flows as a substitute for future income tax cash flows increases the overall decision-usefulness of the financial statements or not.

b) There should be no additional disclosure requirements without previously reassessing the informational value of present disclosures (cutting the clutter – see also our comments to Q1.2).

Q1.4 Do you agree that tax strategies to accommodate user information needs should be disclosed in the management commentary and not in the financial statements? Why or why not? (Paragraphs 1.8 to 1.9)

Key Comments:

a) We believe that a careful analysis of the usefulness of such a disclosure is required and question that detailed information on tax strategies would help users in general, as this is not an indication for future tax cash flows. Also, we see a risk that such a disclosure would rather be boiler plate and would provide only limited insight, as companies might not have a specified tax strategy (rather than avoiding tax if legally possible) or use a very complicated tax strategy that is too complex to be stated in the notes and understood by the large majority of users.

b) If a thorough analysis leads to the conclusion that indeed a disclosure on tax strategies is helpful, we believe that the information should be disclosed in the management commentary rather than in the notes.

Q1.5 The reconciliation of the actual tax charge to the charge on profit at the statutory tax rate (tax rate reconciliation) is quite complicated and leads to some misunderstandings. Do you agree that the suggestions made in the paper are helpful by clarifying the explanation why the current tax charge is not equivalent to the standard rate of tax

applied to the accounting profit? Why or why not? (Paragraphs 1.19 to 1.20 and 2.21 to 2.34)

Key Comments:

a) We agree that the tax rate reconciliation should be as transparent as possible. However, based on the information provided by the DP we cannot conclude, whether standardising the captions of the reconciling items actually would create more transparency. Also, in different tax jurisdictions there might be different views on how to make the reconciliation most transparent.

b) In general, we agree that the descriptions of the reconciling items should be straightforward without technical complexity.

c) We strongly suggest, to do further research work on what exact information regarding the tax rate reconciliation would really help users determining future income tax cash flows.

Q1.6 The amounts currently disclosed provide limited information about future tax cash flows. How would you suggest the disclosures in IAS 12 be improved to provide better information about future tax cash flows? (Paragraphs 1.13 to 1.14 and 2.35 to 2.40)

Key Comments:

a) Any improvement of the current Standard should be based on more research on what users really need.

b) Generally, we believe that full projections and detailed schedules on the expected reversals of temporary differences (this could include a time period of sometimes over twenty years) do not meet the cost/benefit test. Maybe an alternative, that would be easier to accomplish, could be to split the amounts of actual and deferred taxes disclosed only into two categories: current and non-current. That would give at least an indication of income tax payments or repayments for the coming twelve months.

Q1.7 The possibility of discounting deferred tax balances is discussed in paragraphs 2.44 to 2.50. In your view, should discounting deferred tax amounts be required? Please explain.

Key Comments:

a) There are some arguments that support the idea of discounting future tax payments as set out in the DP in paragraphs 2.44 to 2.50.

b) There are also valid counter-arguments that support the idea of non-discounting:

- Non discounted tax assets and tax liabilities are much closer to actual cash flows than discounted values. Therefore, there is no need for discounting if the users request information on future income tax cash flows.
- Discounting requires an intensive, in-depth analysis of maturities and reversal dates of each temporary difference, which would require detailed and complex maturity scheduling.
- As a matter of fact, in some cases deferred taxes reported under IAS 12 are effectively discounted, e.g. when a temporary difference results from the difference between a discounted carrying amount and a tax base of nil.
- Due to the inherent level of uncertainties and judgment this complex accounting area would be prone to manipulation.

c) Assessing the arguments stated under a) and b) from a cost-benefit-point of view, we believe that the costs of discounting by far outweigh the benefits.

d) For these reasons, IFRS have a long and established history of not discounting future income tax cash flows.

Q1.8 Currently IAS 12 neither provides explicit guidance for accounting for uncertain tax positions nor contains any specific disclosure requirements regarding the tax risk position.

(a) Do you agree required information regarding uncertain tax positions should be disclosed? If so, which of the following do you prefer?

Altern. 1: Disclosure requirements should be included in management commentary.

Altern. 2: Disclosure requirements should be split in two parts.
Part 1 would include disclosure of all positions for which the tax payer must establish a tax provision under IFRS and will be disclosed in notes to the - financial statements.
Part 2 would include all other uncertainties regarding income taxes for which no provision is recognized [the DP is unclear whether Part 2 should be included in the notes or in the management commentary]. (Paragraphs 1.10 to 1.12)

(b) Do you agree that IAS 12 should address the recognition and measurement of uncertain tax position? Why or why not?

If you agree, should the measurement be based on the most likely outcome or a probability weighted method? Should measurement include the likelihood the tax position will be reviewed by the tax authorities or should that review be assumed? (Paragraph 2.51 to 2.59)

Key Comments:

a) We are not so sure whether information on uncertain tax positions really helps users to better understand future income tax cash flows. We support EFRAG's suggestion to do more research in that aspect, but only after consultation with the IASB.

b) As set out in our comment letter to the IASB on ED 2009/2 Income Tax, in many cases information on income taxes is subject to uncertainty in varying degrees. We would consider a clarification on the recognition and measurement of uncertain tax position based on the definition in the framework, under which the recognition of a liability is – among other criteria – based on the probable outflow of economic benefits, to be helpful.

Q1.9 Are there any issues with IAS 12, which are not addressed in Part 1 that would significantly improve the standard? What amendments would address these issues?

Key Comments:

Although we believe that the Standard needs no major repairs, we would like to address the following issues for consideration, if the IASB decides to amend the existing Standard or to develop a new Standard on Income Tax:

a) Tax goodwill and other specific tax issues related to business combinations
b) Principles for the accounting of deferred taxes on temporary differences that will not reverse for a long time (e.g. tax deductible goodwill)
c) Principles for derecognition of tax assets and tax liabilities
d) Deferred taxes on common control transactions
e) Recognition and measurement of tax uncertainties

Q1.10 What is your view on the exemptions that currently exist in IAS 12?

Key Comments:

The existing exemptions are pragmatic solutions within the current standard and therefore should not be changed as long as the whole concept of IAS 12 is not being revised.

Questions to constituents - Part 2: Alternative approaches to accounting for income tax

Q2.1 If the development of a new standard for income tax, based on different principles from those used in IAS 12 is to be considered, which of the approaches discussed in Part 2 seem to have most merit and should be considered as a basis for further development?

Key Comments:

a) There was not enough detailed information to make a thorough review of the different approaches. Based on the facts in the DP, none of the approaches seems to offer a solution for all problems discussed.

b) We believe that – after consulting with the IASB – more research has to be performed to clearly describe the main principles of the approaches, including their pros and cons. Before commencing this research the users' needs must be clearly identified. Only after this it would be possible for us to decide, which approach had the most merits and should be further developed.

Q2.2 Do you think that there are any special practical difficulties with implementing the approach(es) that you favor in practice? If so, how can those difficulties be addressed?

Key Comments:

See comment to Q2.1.

Q2.3 Are there any approaches that are not discussed in Part 2 that should be considered?

Key Comments:

See comment to Q2.1.

Q2.4 In your view should a combination of approaches be considered? If so, which approach should be used in what circumstances?

Key Comments:

See comment to Q2.1. More information would be needed on the approaches to come to the conclusion whether a combination of approaches should be considered.

Q2.5 Do you have any further comments on the discussion of the various approaches in Part 2?

Key Comments:

We have no further comments at this stage of the discussion.