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Draft IFRIC Interpretation DI/2015/1

Uncertainty over Income Tax Treatments

Comments to be received by 19 January 2016

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[Draft] IFRIC INTERPRETATION

Uncertainty over Income Tax Treatments

Comments to be received by 19 January 2016

Draft IFRIC Interpretation DI/2015/1 *Uncertainty over Income Tax Treatments* is published by the International Accounting Standards Board (IASB) for comment only. The proposals may be modified in the light of the comments received before being issued in final form. Comments need to be received by **19 January, 2016** and should be submitted in writing to the address below, by email to commentletters@ifrs.org or electronically using our 'Comment on a proposal' page.

All comments will be on the public record and posted on our website unless the respondent requests confidentiality. Such requests will not normally be granted unless supported by good reason, for example, commercial confidence. Please see our website for details on this and how we use your personal data.

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Introduction

The International Accounting Standards Board's IFRS Interpretations Committee ('the Interpretations Committee') has published the draft Interpretation *Uncertainty over Income Tax Treatments* ('the draft Interpretation').

The Interpretations Committee was asked when the recognition of a current tax asset is appropriate if tax laws require an entity to make an immediate payment in respect of a disputed amount. In the situation in the question, a tax examination results in an additional charge but the entity intends to appeal against the additional charge.

The Interpretations Committee noted that IAS 12 *Income Taxes* provides guidance on recognition in such a situation. However, the Interpretations Committee observed diversity in practice for various issues on the recognition and measurement of a tax liability or asset in circumstances in which there is uncertainty in the application of the tax law.

Consequently, the Interpretations Committee proposed the draft Interpretation.

Invitation to comment

The Interpretations Committee invites comments on the proposals in the draft Interpretation, particularly on the questions set out below. Comments are most helpful if they:

(a) comment on the questions as stated;

(b) indicate the specific paragraph or group of paragraphs to which they relate;

(c) contain a clear rationale; and

(d) include any alternative that the Interpretations Committee should consider, if applicable.

The Interpretations Committee is not requesting comments on matters that are not addressed in the draft Interpretation.

Comments should be submitted in writing so as to be received no later than **19 January 2016**.

Questions for respondents

Question 1—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?

Question 2—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 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?

Question 3—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?

Question 4—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. 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?

Question 5—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*. *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?

How to comment

Comments should be submitted using one of the following methods.

Electronically (our preferred method)	Visit the 'Comment on a proposal' page, which can be found at: go.ifrs.org/comment
Email	Email comments can be sent to: commentletters@ifrs.org
Postal	IFRS Foundation 30 Cannon Street London EC4M 6XH United Kingdom

All comments will be on the public record and posted on our website unless confidentiality is requested. Such requests will not normally be granted unless supported by good reason, for example, commercial confidence. Please see our website for details on this and how we use your personal data.

[Draft] IFRIC Interpretation X *Uncertainty over Income Tax Treatments* (IFRIC X) is set out in paragraphs 1–21 and Appendices A and B. [Draft] IFRIC X is accompanied by Illustrative Examples and a Basis for Conclusions. The scope and authority of Interpretations are set out in paragraphs 2 and 7–14 of the *Preface of International Financial Reporting Standards*.

[Draft] IFRIC Interpretation X
Uncertainty over Income Tax Treatments

References

- *Conceptual Framework for Financial Reporting*
- IAS 1 *Presentation of Financial Statements*
- IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*
- IAS 12 *Income Taxes*
- IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*

Background

1 Paragraph 5 of IAS 12 *Income Taxes* states that:

(a) current tax is the amount of income taxes payable (recoverable) in respect of the taxable profit (tax loss) for a period;

(b) deferred tax liabilities are the amounts of income taxes payable in future periods in respect of taxable temporary differences; and

(c) deferred tax assets are the amounts of income taxes recoverable in future periods in respect of deductible temporary differences, the carryforward of unused tax losses and the carryforward of unused tax credits.

2 Paragraph 5 of IAS 12 also states that taxable profit (tax loss) is the profit (loss) for a period, determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable (recoverable).

3 Taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates form the basis for the recognition and measurement of a current or deferred tax liability or asset. The determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates is dependent on the application of tax law.

4 It may be unclear how a specific requirement of the tax law applies to a particular transaction or circumstance. The acceptability of a particular tax treatment under the tax law might depend on the decisions taken by the relevant taxation authority or a court in future. Consequently, the outcome of examinations of a particular tax treatment by the relevant taxation authority or the outcome of a dispute may affect the entity's accounting for a current or deferred tax liability or asset. For example, the taxable profit (tax loss) for the particular period may be affected by the results of a tax examination or dispute, the results of which are uncertain at the end of the entity's reporting period.

5 In this [draft] Interpretation, the term 'tax treatments' refers to the treatments used or planned to be used in an entity's income tax filings. In this [draft] Interpretation, the term 'taxation authority' refers to the body or bodies that make a decision about whether tax treatments are acceptable under the tax law. This might include a court.

6 When there is uncertainty over whether the taxation authority will accept a specific tax treatment under the tax law, that tax treatment is an uncertain tax treatment. An entity's decision not to submit any tax filing in one tax jurisdiction or not to include specific income in taxable profits would also be an uncertain tax treatment, if the acceptability is unclear under the tax law.

7 The Interpretations Committee observed diversity in practice in the accounting for income tax in circumstances in which there is uncertainty in the application of the tax law. IAS 12 provides requirements on the recognition and measurement of a current or deferred tax liability or asset. However, the Interpretations Committee noted that IAS 12 does not provide specific guidance for how uncertainty should be reflected in the accounting for income tax. Consequently, this [draft] Interpretation was developed to provide that guidance.

Scope

8 This [draft] Interpretation applies to the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates, in circumstances in which there is uncertainty over income tax treatments that affects the application of IAS 12.

9 This [draft] Interpretation does not change any existing requirements in IAS 12. An entity shall recognise and measure a current or deferred tax asset or liability by applying the requirements of IAS 12. However, this shall be based on taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates that are determined in accordance with this [draft] Interpretation if there is uncertainty over income tax treatments.

Issues

10 To provide guidance in accounting for uncertainty over income tax treatments, this [draft] Interpretation addresses:

(a) whether an entity should consider uncertain tax treatments collectively;

(b) the assumptions an entity should make about the examination of tax treatments by taxation authorities;

(c) how an entity should determine taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates; and

(d) how an entity should consider changes in facts and circumstances.

Consensus

Whether an entity should consider uncertain tax treatments collectively

11 An entity shall determine whether each uncertain tax treatment should be considered separately, or whether some uncertain tax treatments should be considered together as a group, based on which approach provides better predictions of the resolution of the uncertainty.

12 For example, an entity would consider uncertain tax treatments together as a group when doing so better reflects the manner in which the entity prepares and supports tax treatments or when collective assessment is consistent with the approach that the entity expects the taxation authority to take during an examination, or both.

Examination by taxation authorities

13 In assessing whether and how an uncertain tax treatment affects the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates, an entity shall assume that a taxation authority with the right to examine amounts reported to it will examine those amounts and have full knowledge of all relevant information when making those examinations (see paragraphs A1–A6).

Determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates

14 An entity considers whether or not it is probable that a taxation authority will accept an uncertain tax treatment, or group of uncertain tax treatments.

15 If an entity concludes that it is probable that the taxation authority will accept an uncertain tax treatment, or group of uncertain tax treatments, it shall determine the taxable profit (tax loss), tax bases, unused tax losses, unused tax credits or tax rates consistently with the tax treatment used or planned to be used in its income tax filings.

16 If an entity concludes that it is not probable that the taxation authority will accept an uncertain tax treatment, or group of uncertain tax treatments, it shall reflect the effect of uncertainty in determining the related taxable profit (tax loss), tax bases, unused tax losses, unused tax credits or tax rates. It shall reflect the effect by using one of the following methods:

(a) The most likely amount—the single most likely amount in a range of possible outcomes. The most likely amount may provide the better prediction if the possible outcomes are binary or are concentrated on one value.

(b) The expected value—the sum of the probability-weighted amounts in a range of possible amounts. The expected value may provide the better prediction if the possible outcomes are widely dispersed.

The entity shall use the method that it concludes will provide the better prediction of the resolution of the uncertainty.

17 If an uncertain tax treatment affects both deferred tax and current tax, an entity shall make consistent estimates and judgements for both. For example, an uncertain tax treatment may affect both taxable profits used to determine the current tax and tax bases used to determine deferred tax.

Consideration of changes in facts and circumstances

18 If facts and circumstances change, an entity shall reassess the judgements and estimates required by this [draft] Interpretation. For example, a change in circumstances might change an entity's conclusions about the acceptability of

tax treatments or its estimates of the effect of uncertainty, or both. In such a situation, the entity would reflect this change in its determination of the taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates, in the period of the change.

Disclosures

19 An entity shall determine whether it should disclose judgements made in the process of applying its accounting policy to determine taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates, in accordance with paragraph 122 of IAS 1 *Presentation of Financial Statements*. For example, determinations required by paragraphs 11, 14 and 16 of this [draft] Interpretation might be disclosed as such judgements.

20 An entity shall also determine whether it should disclose information about the assumptions it makes and other estimates used in determining taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates. The entity makes this determination in accordance with paragraphs 125–129 of IAS 1.

21 If an entity concludes that it is probable that the taxation authority will accept an uncertain tax treatment or group of uncertain tax treatments, the potential impact of the uncertainty over the tax treatment(s) would not be reflected in the financial statements. However, the entity shall determine whether the potential impact shall be disclosed as tax-related contingencies in accordance with paragraph 88 of IAS 12. The entity would refer to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, when determining what disclosures should be given in respect of these tax-related contingencies.

Appendix A
Application Guidance

This appendix is an integral part of [draft] IFRIC X. It describes the application of paragraphs 13 and 18 and has the same authority as the other parts of [draft] IFRIC X.

Examination by taxation authorities and consideration of changes in facts and circumstances

A1 This appendix describes the application of paragraphs 13 and 18, which provide guidance about what assumptions an entity should make about the examination by taxation authorities and the consideration of changes in facts and circumstances.

Time limit on taxation authorities' power for examination(s)

A2 If applicable laws and regulations impose a time limit on or after which the taxation authority is no longer able to challenge an entity's tax treatments (sometimes referred to as a statute of limitations), an entity shall reflect this change of circumstances when these rights expire. Before the rights expire, an entity shall also consider the following guidance about the results of examination(s) by taxation authorities.

Results of examination(s) by taxation authorities

A3 If taxation authorities continue to have the right to (re-)examine the amounts even after an examination(s), an entity shall continue to assume that the taxation authorities will (re-)examine any amounts reported to it and have full knowledge of all relevant information when making those examinations.

A4 However, the results of examination(s) by taxation authorities are new facts and circumstances and they may affect an entity's conclusions about the acceptability of tax treatments and its estimates of the effect of uncertainty. An entity may become aware that the taxation authority has challenged a similar tax treatment with another entity that the taxation authority had previously accepted for the reporting entity. This would also be a new fact for the reporting entity.

A5 A taxation authority may explicitly accept an entity's tax treatment during an examination for a specific period. This explicit acceptance is a new fact for tax treatments within the scope of the examination (tax treatments for the specific period) and may affect similar tax treatments for other periods.

A6 A taxation authority may implicitly accept an entity's tax treatment. For example, the taxation authority may review the entity's tax filing that includes tax treatments for a specific period, and it may be silent about those tax treatments. This implicit acceptance is a new fact for tax treatments within the scope of the examination (for example, tax treatments for the specific period). However, this implicit acceptance is not necessarily a new fact for similar tax treatments that are not within the scope of the examination (for example, similar tax treatments for other periods).

Appendix B
Effective date and transition

This appendix is an integral part of [draft] IFRIC X and has the same authority as the other parts of [draft] IFRIC X.

Effective date

B1 An entity shall apply this [draft] Interpretation for annual periods beginning on or after [date]. Earlier application is permitted. If an entity applies this [draft] Interpretation for an earlier period, it shall disclose that fact.

Transition

B2 On initial application, an entity shall apply this [draft] Interpretation either:

(a) without adjusting comparative information, recognising the cumulative effect of initially applying the [draft] Interpretation in the opening balance of retained earnings, or other appropriate components of equity, of the annual reporting period that includes the date of initial application of the [draft] Interpretation. The date of initial application is the date when an entity first applies this [draft] Interpretation and must be the beginning of the annual reporting period.

(b) retrospectively to each prior reporting period presented in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

The retrospective application in accordance with IAS 8 is permitted if the entity has the information necessary to do so and this information is available without the use of hindsight.

B3 An entity shall disclose which method of transition it has applied.

[Draft] IFRIC X *Uncertainty over Income Tax Treatments* Illustrative Examples

These examples accompany, but are not part of, [draft] IFRIC X.

IE1 The objective of these examples is to illustrate how an entity might apply some of the requirements in the [draft] Interpretation based on the limited facts presented. In all of the examples, entities note that the taxation authority would not always examine the amounts reported, but the entities, for the purpose of accounting, make the assumption that the taxation authority will examine the amounts reported to them and have full knowledge of all relevant information, as required by paragraph 13 of this [draft] Interpretation.

Example 1—When one tax treatment is considered independently and when the most likely amount is used to reflect the effect of uncertainty

IE2 Entity A has an unresolved dispute over whether a specific item should be deductible in determining the taxable profit for a specific period. A tax investigator did not accept this tax treatment but the entity appealed against this to the court, which makes a final decision on the acceptability under the tax law. Entity A noted that this uncertain tax treatment affects neither accounting for deferred tax nor tax rates and it concluded that it is probable that the taxation authority will accept the other tax treatments used in its tax filing. Entity A has no similar disputes and it therefore decides that this tax treatment should be considered independently. If the taxation authority does not accept the tax treatment (ie if the court's final decision does not accept the tax treatment), the taxable profit for the specific period will increase by CU100.[1] At the end of the reporting period, Entity A determines that it is not probable that the taxation authority will accept the tax treatment on the basis of an evaluation of all available evidence and that the most likely amount (an additional CU100 of taxable profit) will provide the better prediction of the resolution of the uncertainty. Entity A therefore recognises and measures a current tax liability in accordance with IAS 12 *Income Taxes*, based on a taxable profit that includes CU100 in addition to the amount reported in its tax filing.

Example 2—When multiple tax treatments are considered collectively and when the expected value is used to reflect the effect of uncertainty

IE3 Entity B's tax filing included a number of deductions related to transfer pricing. The taxation authority in its jurisdiction may challenge those tax treatments. Entity B notes that the taxation authority's decision on one transfer pricing matter would affect, or be affected by, the other transfer pricing matters. Entity B determines that the tax treatments should be considered collectively, because it concludes that this will provide the best prediction of the resolution of the uncertainty. At the end of the reporting period, Entity B concludes, on the

1 In these Illustrative Examples, currency amounts are denominated in 'currency units' (CU).

basis of an evaluation of all available evidence, that it is not probable that the taxation authority will accept all of the tax treatments. Entity B notes that this group of uncertain tax treatments affect neither accounting for deferred tax nor tax rates and it concludes that it is probable that the taxation authority will accept the other tax treatments used in its tax filing.

IE4 Entity B estimates the probabilities of what would be added to the taxable profits, as follows:

	Estimated outcome, CU	Individual probability, %	Estimate of expected value, CU
Outcome 1	–	5%	–
Outcome 2	200	5%	10
Outcome 3	400	20%	80
Outcome 4	600	20%	120
Outcome 5	800	30%	240
Outcome 6	1,000	20%	200
		100%	650

IE5 Entity B observes that the possible outcomes are widely dispersed and notes that the most likely amount of CU800 does not provide the better prediction of the resolution of the uncertainty. Entity B therefore concludes that the expected value (CU650) would provide the better prediction of the resolution of the uncertainty.

IE6 Consequently, Entity B recognises and measures a current tax liability in accordance with IAS 12, based on the taxable profit, which includes CU650 in addition to the amount of the taxable profit in its tax filing.

IE7 Entity B notes that the tax treatments may affect income taxes for other tax jurisdictions. It also notes that the relevant tax rules indicate that this particular tax jurisdiction's decision would not affect decisions to be made by taxation authorities in other tax jurisdictions, in respect of these tax treatments. Consequently, Entity B considers tax treatments in income taxes separately for these other tax jurisdictions.

Example 3—When a deferred tax asset is recognised and measured based on the most likely amount for a tax base that reflects the effect of uncertainty

IE8 Entity C acquired a separately identifiable intangible asset for CU100 that has an indefinite life and is, therefore, not amortised in accordance with IAS 38 *Intangible Assets*. It is certain that the full amount of the intangible asset is deductible for tax purposes, but the timing of deductibility (ie period of amortisation under the tax law) is uncertain. Entity C has no similar intangible assets and it therefore decides that this tax treatment should be considered independently.

IE9 Entity C deducted CU100 from taxable income for tax purposes for Year 1. At the end of Year 1, Entity C concludes, on the basis of an evaluation of all available evidence (eg information about disputes for other entities' similar transactions), that it is not probable that this tax treatment will be accepted, although Entity C believes that the entity's interpretation of the tax law could be appropriate and therefore retains the amounts reported to the taxation authorities in the tax return. Consequently, Entity C uses the most likely amount, rather than the amount to be used in its tax filings, to reflect the uncertainty in determining the tax base, because Entity C concluded that this amount would provide the better prediction of the resolution of uncertainty.

IE10 Entity C observes that the most likely amount that the taxation authority will accept as the deductible amount for Year 1 will be CU10. Consequently, the most likely amount for the corresponding tax base for the intangible asset will be CU90.

IE11 At the end of Year 1, Entity C recognises and measures a deferred tax liability by applying the relevant requirements in IAS 12, based on the amount of the temporary difference between the carrying amount of the intangible asset in its financial statements and the most likely amount of the tax base (ie the difference between CU100 and CU90).

IE12 Entity C also concludes that it should reflect the effect of the uncertainty in determining the taxable profit for Year 1, because this uncertain tax treatment also affects the taxable profit. Entity C recognises and measures a current tax liability, based on the estimates and judgements that are consistent with those made for deferred tax accounting. Entity C therefore recognises and measures a current tax liability in accordance with IAS 12, based on the taxable profit that includes CU90, in addition to the amount in its tax filing. (This is because Entity C deducted CU100 from taxable income for Year 1, whereas the most likely amount was CU10. Entity C concluded that it is not probable that the tax treatment will be accepted.)

Basis for Conclusions on [draft] IFRIC X *Uncertainty over Income Tax Treatments*

This Basis for Conclusions accompanies, but is not part of, [draft] IFRIC X.

Introduction

BC1 This Basis for Conclusions summarises the IFRS Interpretations Committee's ('the Interpretations Committee') considerations in reaching its consensus.

Background

BC2 The Interpretations Committee was asked when the recognition of a current tax asset is appropriate if tax laws require an entity to make an immediate payment in respect of a disputed amount. In the situation in the question, a tax examination results in an additional charge but the entity intends to appeal against the additional charge.

BC3 The Interpretations Committee noted that paragraph 12 of IAS 12 *Income Taxes* provides guidance on recognition in such a situation (see also paragraphs BC14–BC16), but observed diversity in practice for various issues on the recognition and measurement of a tax liability or asset in circumstances in which there is uncertainty in the application of the tax law.

BC4 Consequently, the Interpretations Committee decided to develop an Interpretation. The Interpretations Committee identified that the expected benefits from publication of this [draft] Interpretation would be an improvement in comparability among entities, by reducing diversity in practice. It concluded that the expected benefits would outweigh any additional costs.

Scope

BC5 The Interpretations Committee decided that it should not limit the scope of the [draft] Interpretation to any specific situation, for example when an entity has unresolved disputes with a taxation authority. This is because it noted that attempting to limit the scope to specific situations would lead to an arbitrary rule.

BC6 Consequently, the Interpretations Committee decided that the [draft] Interpretation should provide guidance whenever there are uncertain tax treatments that affect accounting under IAS 12.

BC7 The Interpretations Committee understood that uncertainty over tax treatments may affect both current and deferred tax. For example, the timing of deductibility of an intangible asset under a tax law may be uncertain and this may affect both the taxable profit and the tax base of the asset. The Interpretations Committee decided that approaches to reflect the effect of uncertainty in the accounting for deferred tax should be consistent with those for current tax. Consequently, it decided that this [draft] Interpretation should provide guidance for both current and deferred tax.

BC8 The [draft] Interpretation does not change any principles in IAS 12. The Interpretations Committee noted that uncertainty over tax treatments affects the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits or tax rates, which in turn affects an entity's tax liability or asset through the accounting required by IAS 12. Consequently, this [draft] Interpretation provides guidance on how to reflect the effect of uncertainty in the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates.

BC9 Accounting for interest and penalties is not within the scope of this [draft] Interpretation and thus is not addressed, because the outreach conducted to date by the Interpretations Committee has not identified any current evidence of significant diversity in practice.

Consensus

Whether an entity should consider uncertain tax treatments collectively

BC10 The Interpretations Committee noted that the amount of a tax liability or asset could be affected by whether each uncertain tax treatment is considered individually or in combination with other uncertain tax treatments, unless expected values are always used. Consequently, it decided to provide guidance on this matter for the purpose of this [draft] Interpretation. It concluded that an entity should determine whether it should consider uncertain tax treatments individually or together, based on the approach that would provide the better predictions of the resolution of the uncertain tax treatments. For example, if the resolution of uncertainty over an uncertain tax treatment is expected to affect, or be affected by, another uncertain tax treatment, considering them collectively might provide the best prediction. The Interpretations Committee noted that judgement is needed in order to reflect the range of situations that will arise in different jurisdictions.

Examination by taxation authorities

BC11 The Interpretations Committee was informed that there are diverse views on whether the likelihood that the taxation authority may or may not examine the amounts reported should be reflected in the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates.

BC12 The Interpretations Committee noted that paragraphs 46–47 of IAS 12 require an entity to measure the amount of a tax liability or asset based on the tax laws that have been enacted or substantively enacted.

BC13 Consequently, the Interpretations Committee concluded that an entity should assume that the taxation authority will examine the amounts reported to it and have full knowledge of all relevant information, if the taxation authorities have rights to examine the amounts.

Determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates

BC14 The Interpretations Committee identified diversity in practice about whether IAS 12 or IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* provides guidance on recognition, in circumstances in which there is uncertainty about income taxes. The Interpretations Committee noted that income taxes are specifically excluded from the scope of IAS 37. The Interpretations Committee noted that paragraph 88 of IAS 12 refers to IAS 37, but only in relation to guidance on disclosures about tax-related contingencies. The Interpretations Committee also noted that IAS 12, not IAS 37, provides requirements on the recognition and measurement of a tax liability or asset.

BC15 The Interpretations Committee noted that paragraphs 12–14 of IAS 12 provide principles for the recognition of a current tax liability and a current tax asset.

BC16 The Interpretations Committee noted that these paragraphs do not have an explicit recognition threshold, although it thought that paragraph 14 of IAS 12 assumes that an asset meets a 'probable' threshold. The Interpretations Committee noted that IAS 12 does not provide specific guidance for the situation in which there is uncertainty over tax treatments.

BC17 The Interpretations Committee observed that the recognition requirement for deferred tax assets and the objective of IAS 12 refer to a probable threshold. Similarly, paragraphs 4.44 and 4.46 of the *Conceptual Framework for Financial Reporting* refer to a probable threshold for the recognition of assets and liabilities in general.

BC18 Consequently, the Interpretations Committee decided that an entity should recognise a current tax liability or asset, if it is probable that an entity will pay or recover an amount in relation to the uncertainty. It also concluded that a consistent threshold should be set for deferred tax. This means that the probable threshold should be applied to determine whether to reflect the effect of uncertain tax treatments on the determination of the taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates in the [draft] Interpretation.

BC19 The Interpretations Committee observed that setting this explicit threshold for when the effect of uncertainty should be included in those determinations would increase comparability among entities and reduce costs of measurement.

BC20 If an entity concludes that it is not probable that the taxation authority will accept a tax treatment, the Interpretations Committee concluded that the entity should reflect the effect of uncertainty when recognising and measuring current and deferred tax assets and liabilities. The Interpretations Committee also concluded that the entity should use the expected value or the most likely amount to reflect the effect of the uncertainty. It decided that an entity should use the method that it concludes will provide the better prediction of the resolution of the uncertainty.

BC21 The Interpretations Committee observed that this approach would be similar to the International Accounting Standards Board's and the US Financial Accounting Standards Board (FASB)'s approach in their converged Standard on revenue from contracts with customers. The Standard on revenue from contracts with customers would require an entity to use judgement on whether to use the expected value or the most likely amount in estimating the amount of variable consideration.

BC22 The Interpretations Committee considered whether to also permit or to require the use of a 'cumulative-probability approach' (ie the measurement method used in US GAAP).[2] It noted that the introduction of this method would make an entity's judgements to be required by this [draft] Interpretation more complex. This is because it would be more complex for an entity to determine the best among three methods (ie expected value, most likely amount and the measurement method used in US GAAP) than the better of two methods (ie expected value and most likely amount). It also noted that no existing Standard in current IFRS uses the cumulative-probability approach, whereas the expected value and the most likely amount are commonly used in IFRS.

BC23 Furthermore, the Interpretations Committee noted that paragraph 46 of IAS 12 implies the use of the best estimate approach to measure a current tax liability or asset, but US GAAP does not use a best estimate approach. It thought that the introduction of the approach used in US GAAP might conflict with the principle described in paragraph 46 of IAS 12.

BC24 Consequently, the Interpretations Committee did not propose either to permit or to require the measurement approach used in US GAAP.

Consideration of changes in facts and circumstances

BC25 A question was raised about the implication of the assumption about the examination by taxation authorities. In particular, the Interpretations Committee was asked how this assumption affected the entity's ability to derecognise a liability. The Interpretations Committee concluded that an entity should reassess its judgements if facts and circumstances change. It also concluded that it should provide application guidance to address the question.

BC26 In some tax jurisdictions, there is a time limit on or after which the taxation authority is no longer able to challenge an entity's tax treatments (sometimes referred to as a statute of limitations). The Interpretations Committee observed that an entity should make the assumption described in paragraph 13 of this [draft] Interpretation until the time limit has been reached. This is because the taxation authority has the right to examine the amounts until that time. The Interpretations Committee observed that, on or after the time limit, the entity should reflect the changed rights of the taxation authority in the entity's accounting, because the taxation authority no longer has the right to examine the amounts. Before this time limit is reached or if there are no time limits, the original assumption should continue, because the taxation authority still has the right to examine the amounts.

BC27 If the taxation authority continues to have the right to (re-)examine the amounts after the implicit or explicit acceptance by the taxation authority, the Interpretations Committee concluded that an entity should continue to assume

2 FASB ASC Section 740-10 *Income Taxes—Overall*.

that the taxation authority will (re-)examine any amounts reported to it and have full knowledge of all relevant information when making those examinations, because the taxation authority still has the right to examine the amounts. However, the Interpretations Committee noted that the results of the examination(s) might change the entity's conclusions about the acceptability of tax treatments or its estimates of the effect of uncertainty, or both, because they could constitute new facts and circumstances.

BC28 If a taxation authority has implicitly or explicitly accepted an entity's tax treatment, the Interpretations Committee concluded that this would be a new fact for the entity.

BC29 Taxation authorities may explicitly accept an entity's specific tax treatment during an examination for a specific year (for example, Year 2). The Interpretations Committee observed that this explicit acceptance would be a new fact for the tax treatments within the scope of the examination (ie those for Year 2) and may affect similar tax treatments (for example, similar tax treatments for Year 1 and Year 3). This is because the explicit acceptance may indicate that the taxation authority has a specific view on a specific type of tax treatments.

BC30 Taxation authorities may implicitly accept an entity's tax treatment. For example, the taxation authority may review the tax return including specific tax treatments for a particular year (for example, for Year 2), and not specifically raise any concerns about those tax treatments and give no indication that it will re-open the review for the year. The Interpretations Committee observed that this implicit acceptance would be a new fact for the tax treatments within the scope of the examination (those for Year 2) but not necessarily a new fact for similar tax treatments that are not within the scope of the investigation (for example, similar tax treatments for Year 1 and Year 3). This is because the implicit acceptance does not necessarily mean that the taxation authority has a specific view for such tax treatments.

Disclosure

BC31 The Interpretations Committee noted that IAS 1 *Presentation of Financial Statements*, IAS 12 and IAS 37 provide disclosure requirements that may be relevant to uncertain tax treatments. Consequently, it decided to highlight in the [draft] Interpretation the relevance of these existing disclosure requirements, because it would be helpful for entities, but it decided not to introduce new disclosure requirements. It noted that paragraph 88 of IAS 12 refers to IAS 37 only for the purpose of the disclosure of tax-related contingent liabilities and assets, whereas paragraph 5 of IAS 37 explains that IAS 37 is not applied to provisions, contingent liabilities or contingent assets related to income taxes, which are addressed in IAS 12. Consequently, it concluded that IAS 37 should be referred to only for the purpose of determining what disclosure should be given and that IAS 37 does not apply to the recognition of income taxes.

Transition

BC32 The Interpretations Committee proposes that an entity should apply the [draft] Interpretation, recognising the cumulative effect of initially applying the [draft] Interpretation in retained earnings or other appropriate components of equity, at the start of the reporting period in which an entity first applies the [draft] Interpretation, without adjusting comparative information. This is because full retrospective application in accordance with the general requirements of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* would often be impossible without the use of hindsight in the application of the [draft] Interpretation. However, the Interpretations Committee decided that full retrospective application should be permitted if an entity has the information necessary to do so without using hindsight.

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