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8 NOV 2010

IASB

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UNITED KINGDOM

Re : Exposure Draft ED/2010/11 Deferred Tax – Recovery of Underlying Assets

Dear Sir/Madam,

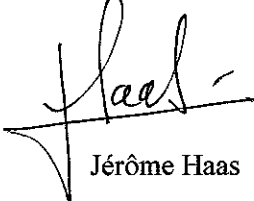
I am writing on behalf of the ANC to give you our comments on the above-mentioned Exposure Draft (ED). Our detailed comments are set out in the attached Appendix.

The ANC disagrees with the proposal to create an exception to the principle underlying IAS 12 on the basis that such principle may create difficulties in some jurisdictions. In our view the issue could be resolved through guidance aimed at clarifying how the expected manner of recovery in a “dual manner” should be accounted for in terms of its tax consequences.

The ANC also disagrees with the scope extension, both beyond the scope of SIC-21 and beyond the practical issues raised which triggered the Board’s intervention, and has concerns about the unintended consequences such proposals may have.

We hope you find these comments useful and would be pleased to provide any further information you might require.

Yours sincerely,



Jérôme Haas

APPENDIX

Exposure Draft INCOME TAX

Question 1 – Exception to the measurement principle

The Board proposes an exception to the principle in IAS 12 that the measurement of deferred tax liabilities and deferred tax assets should reflect the tax consequences that would follow from the manner in which the entity expects to recover or settle the carrying amount of its assets and liabilities. The proposed exception would apply when specified underlying assets are remeasured or revalued at fair value.

Do you agree that this exception should apply when the specified underlying assets are remeasured or revalued at fair value?

Why or why not?

Whilst we understand the fact that the Board seeks to resolve issues generated by IAS 12 in some jurisdictions, the ANC disagrees with the Board making an exception to the core principle of IAS 12.51, because “applying this principle can be difficult or subjective in some jurisdictions” (BC3).

A first reason for disagreeing is that the proposals may generate other difficulties in other jurisdictions where tax consequences on sale or use follow a different pattern from that envisaged by the Board in BC3.

Also, in its response to ED/2009/02, the CNC was opposed to the proposal according to which the tax basis was supposed to be determined on a sale or settlement basis at reporting date, as it does not take into account the entity’s business model and will not therefore always be consistent with expected cash flows, and thus may not result in decision-useful information. The ANC still fully adheres to this statement.

Regarding investment property measured using the cost model, the ANC notes that BC 12 considers the expected manner of recovery to be less subjective and less difficult because of the general presumption that the asset’s carrying amount is recovered by use to the extent of the depreciable amount and by sale to the extent of the residual value. Therefore the ANC wonders why such reasoning could not (and should not) also be applied to investment property at fair value.

Indeed, the ANC considers that the difficulties or subjectiveness that the Board wishes to solve, in the case of investment property measured using the fair value model, would be better addressed through targeted guidance as to how the principle defined in IAS 12.51 is to be applied, especially with respect to :

- how the expected manner of recovery in a “dual manner” should be accounted for in terms of its tax consequences, including as regards recovery through the sale of entity-wrappers as described hereafter;
- how, in accordance with the provisions in IAS 1 regarding judgments made and sources of uncertainty, any change in such manner of recovery expectations are to be transcribed in the notes with the view to helping users assess the amount, timing and uncertainty of reported tax amounts.

Dealing with the consequences around entity-wrapper issues

The ANC considers that the guidance called for above should also address the consequences of situations encountered in some jurisdictions, where the tax consequences vary depending on whether an asset is sold within an entity-wrapper (ie the shares of the entity are sold and the entity holds a unique asset) or directly by the entity. Indeed, in such jurisdictions, the tax consequences of selling the asset within an entity-wrapper are more favourable than by selling the asset directly thus leading effectively, when the sale is envisaged, to such sale of shares in the entity which holds this sole asset.

Question 2 – Scope of the exception

The Board identified that the expected manner of recovery of some underlying assets that are remeasured or revalued at fair value may be difficult and subjective to determine when deferred tax liabilities or deferred tax assets arise from:

(a) investment property that is measured using the fair value model in IAS 40;

(b) property, plant and equipment or intangible assets measured using the revaluation model in IAS 16 or IAS 38;

(c) investment property, property, plant and equipment or intangible assets initially measured at fair value in a business combination if the entity uses the fair value or revaluation model when subsequently measuring the underlying asset; and

(d) other underlying assets or liabilities that are measured at fair value or on a revaluation basis.

The Board proposes that the scope of the exception should include the underlying assets described in (a), (b) and (c), but not those assets or liabilities described in (d).

Do you agree with the underlying assets included within the scope of the proposed exception?

Why or why not? If not, what changes to the scope do you propose and why?

The ANC disagrees with the scope of the exception.

Extension and limitation of the scope of the exception

The ANC understands that the initial issue was related to investment property measured at fair value, as the concerns raised in practice have primarily arisen in relation to such assets (BC14). The Board has decided to extend the scope of the proposals to assets measured under IAS 16 and IAS 38 using the revaluation model whether acquired or not in a business combination, as well as for investment property; because of the absence of underlying difference between regularly fair valuing assets through a revaluation model and applying a fair value measurement model (BC15).

The ANC disagrees with the statement in BC15 in as much as the accounting consequences of those two models are completely different thus reflecting underlying differences in the lines of thought.

On the contrary, in BC18, the Board justifies the non-extension of the scope to other assets and liabilities measured at fair value (such as financial instruments and biological assets) because the issues encountered in practice seem to relate to investment property and property, plant and equipment and intangible assets. Such statement contradicts BC14 which, as mentioned above, states that issues have primarily arisen in relation to investment property. The Board also seems concerned about unintended consequences of such an extension.



The ANC is concerned about the unintended consequences the proposals may have overall.

Superseding SIC-21

The ANC understands that the proposals are also expected to supersede SIC-21 which dealt with the recovery of revalued non-depreciable assets either under IAS 16 or IAS 40.

As previously mentioned, the ANC is not convinced by the arguments provided by the Board in BC15 to justify such an extension of the initial scope identified. As SIC-21 deals only with non-depreciable assets (in practice mostly land), the initial proposals regarding investment property measured at fair value already represent an extension of SIC-21's scope to assets that are or would be considered depreciable. Apart from being opposed to the exception for the reasons set out in our response to question 3, the ANC is concerned about such extension proposed by the Board to categories of depreciable assets absent the evidence of difficulties and subjectiveness in those cases. The ANC also notes that SIC-21 has in some cases been analogised as regards intangible assets with an indefinite useful life and considers that it may be worthwhile to address the consequences that superseding SIC-21 may have as regards the tax consequences on those assets.

We also refer to our comments in question 1 relative to the presumption indicated in BC12.

Question 3 – Measurement basis used in the exception

The Board proposes that, when the exception applies, deferred tax liabilities and deferred tax assets should be measured by applying a rebuttable presumption that the carrying amount of the underlying asset will be recovered entirely through sale. This presumption would be rebutted only when an entity has clear evidence that it will consume the asset's economic benefits throughout its economic life.

Do you agree with the rebuttable presumption that the carrying amount of the underlying asset will be recovered entirely by sale when the exception applies?

Why or why not? If not, what measurement basis do you propose and why?

The ANC disagrees with the rebuttable presumption according to which the carrying amount of the assets scoped in the ED should be considered to be recovered entirely through sale unless an entity has clear evidence that it will consume the asset's economic benefits throughout its economic life for the following reasons.

Indeed the ANC finds no compelling arguments to justify the fact that the measurement base of the asset would drive the expected manner in which the carrying value of the asset is expected to be recovered as both in the cases of IAS 16.6/IAS 38.8 regarding revaluation and of IAS 40.5 regarding investment property (and regardless of whether the asset is acquired in a business combination or not), an accounting choice exists. In other words, even though the objective of classification of the underlying assets under the related accounting standard is the same, different accounting choices are available. Thus, since an accounting choice is available, it does not logically follow that strict constraints regarding tax consequences should be drawn from such choice.

In our view, there is therefore no contradiction in measuring investment property under the fair value model whilst expecting to recover the carrying value of the asset both through use and subsequently through sale and we therefore disagree with BC21b. In this respect, the ANC considers that the statement made by the Board in BC19 according to which "the unit of account applied in determining the manner of recovery in the Standard is the underlying asset as a whole, not the individual temporary differences" contradicts the dual manner of expected recovery referred to in BC12.

The ANC considers that the rebuttable presumption proposed is akin to a rule that could result in exonerating entities from trying to assess the manner in which they expect to recover the carrying value of the underlying asset, unless they consider that they could obtain a more favourable result with the other manner of recovery.

Moreover, the ANC considers that the condition to rebut the presumption “clear evidence” is set at a rather high level. In this respect, the ANC wonders what type of evidence would be required to prove that the entity expects to recover the carrying amount of the asset through use. In addition, it seems to us that, as currently drafted, the burden of proof lies with those entities which currently do not appear to have any issue in applying the standard.

The ANC considers that difficulties and subjectiveness in the expected manner of recovery occurs whatever the accounting choice made in terms of measurement of the underlying asset.

Question 4 – Transition

The Board proposes that the amendments should apply retrospectively. This requirement includes retrospective restatement of all deferred tax liabilities or deferred tax assets within the scope of the proposed amendments, including those that were initially recognised in a business combination.

Do you agree with the retrospective application of the proposed amendments to IAS 12 to all deferred tax liabilities or deferred tax assets, including those that were recognised in a business combination?

Why or why not? If not, what transition method do you propose and why? *

Although we disagree with the proposals, the ANC agrees with the fact that such amendments be applied retrospectively. We would, however, in this case mention the following concerns regarding the recovery of recognised deferred tax assets.

Consequences on recognised deferred tax assets

The IASB rightly mentions in BC25 and BC26 the consequences that the proposals may have on recognised deferred tax assets. However, the Board does not draw any conclusion in this respect. The ANC understands that such impacts may cause considerable concerns to preparers who may no longer be able to recognise some or all of their deferred tax assets. The ANC is all the more concerned that, as previously mentioned, the proposals are arbitrary and do not purport to adequately reflect the manner in which the carrying value of such assets is expected to be recovered, not in the least to say that they appear to be anti-economic.

Question 5 – Other comments

Do you have any other comments on the proposals?

None other than mentioned in the previous questions.

**** In other words, should the IASB consider finalising its proposals as they currently stand, we would ask you to daily consider the abovementioned issues and we stand ready to discuss them further to ensure that non intended consequences are avoided.***

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