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EFRAG
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22 January 2016

Re: Draft IFRIC Interpretation DI/2015/1 Uncertainty over Income Tax Treatments

Dear Roger,

We are pleased to have the opportunity to provide our comments in order to contribute to the finalization of the EFRAG comment letter on the Draft IFRIC Interpretation DI/2015/1 *Uncertainty over Income Tax Treatments* (the "draft Interpretation"), issued by the IFRS Interpretations Committee (the "IC").

We appreciate the IC efforts to develop a draft Interpretation to remove the existing diversity in practice for uncertain income tax treatments and we think that the IC should finalise the draft Interpretation.

However, we have the following suggestions:

- to move in the Consensus of the Interpretation the content of paragraph BC18, i.e. that an entity should recognise a current (or deferred) tax liability or asset, if it is probable that the entity will pay or recover an amount in relation to the income tax uncertainty;
- to include in the scope of the Interpretation the accounting for interest and penalties relating to uncertain income tax treatments, because we have observed significant diversity in practice on this topic.

We note that tax disputes may relate to other taxes different from income taxes (eg VAT), which are not covered by this draft Interpretation. In our view, the proposed interpretation might create a potential inconsistency between the accounting for uncertainties related to income taxes and uncertainties related to other taxes. In Italy, we observed diversity in practice in accounting for uncertainties over other taxes. Consequently, we believe that the IASB should address in a comprehensive project this potential inconsistency.

Our detailed responses to the Draft Comment Letter questions are in the Appendix.

Should you need any further information, please do not hesitate to contact us.

Yours sincerely,

Angelo Casò

(Chairman)

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?

We agree with the proposed scope of the draft Interpretation, because IAS 12 does not provide a specific guidance on how uncertainties should be reflected in the accounting for income tax. In our view, this draft Interpretation can fill the gap and limit diversity in practice.

We disagree with paragraph BC9 of the Draft Interpretation, because we think that there is significant divergence in practice on the accounting treatment for interest and penalties relating to income tax disputes. Consequently, the Interpretation should include this issue.

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?

We support the use of a 'probable' threshold for recognition of assets and liabilities. Consequently, we support the draft Interpretation’s proposals on when and how the uncertainty of a tax treatment should be reflected in the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits or tax rates. We think that a ‘probable’ threshold is consistent with IAS 12 and with the Conceptual Framework.

We suggest to highlight in Consensus of the Interpretation the content of paragraph BC18 about the recognition of current (or deferred) tax assets and liabilities, namely, that in case of uncertainties relating to income taxes, the entity should use a “probable” recognition threshold for the recognition of current/deferred uncertain tax assets and liabilities. Moreover, it would be useful to introduce an illustrative example that deals with the fact pattern described in paragraph BC2 (ie. whether 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 and the entity intends to appeal against the additional charge).

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?

We agree with the draft Interpretation's proposal on the determination of whether uncertain tax treatments should be considered individually or on a combined basis. In particular, we agree that the entity should consider uncertain tax treatments separately or collectively, based on the approach that provides the best estimate of the final outcome.

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?

We agree on the draft Interpretation's proposal that the entity in determining uncertain tax treatment should assume that the taxation authority will examine any reported amount and will have a full knowledge of relevant information, until it continues to have the right to examine the entity's tax filings. In our view, this clarification is consistent with IAS 12 (which requires an entity to measure tax assets and tax liabilities on the basis of tax laws) and would clarify that entities should not consider 'the probability of not being detected' when they account for uncertainty over income taxes.

We also agree that if facts and circumstances change, the entity should reassess the prediction of the uncertainty's resolution and the related guidance.

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?

We agree with not introducing new disclosure's requirements, because we think that the current disclosure requirements in IAS 1, IAS 12 and IAS 37 are adequate to provide useful information to users for assessing uncertain tax positions.

We agree that on initial application the entity shall have the option to choose between a limited and a full retrospective application of the draft Interpretation. We also agree that an entity should choose the full retrospective application method only if the entity has the necessary information to do so without the use of hindsight.

Request for inputs from constituents

EFRAG seeks inputs from constituents on whether they have concerns with the potential inconsistency in the recognition of uncertainties related to income taxes on the one hand and the uncertainties relating to other taxes and similar transactions on the other. Please explain how you account for these uncertainties at present, what IFRS you apply, and on this basis, your views on the outcome of the Interpretation.

We think that the proposed interpretation might create a potential inconsistency between the accounting for uncertainties related to income taxes and uncertainties related to other taxes. From a standard setter point of view, we think that uncertainties over all types of taxes (ie income taxes and other taxes) should be accounted for in a consistent way (ie a 'probable' recognition threshold as required by the draft Interpretation should be applied to uncertainties over all types of taxes).

In Italy, we observed diversity in practice in accounting for uncertainties over other taxes. Some entities apply IAS 37 and the 'virtually certain' recognition threshold, other entities consider the payment made to the tax authority as a prepayment and apply a 'probable' recognition threshold. If the IC finalise the draft Interpretation as proposed, we think that many preparers will questioned whether they may apply the Interpretation by analogy.

However, the potential inconsistency between the accounting for uncertainties relating to income taxes and the ones relating to other taxes is a very broad subject, and it cannot be addressed by this Interpretation. In our view, the IASB should address this issue in a comprehensive project.