30 July 2009

International Accounting Standards Board
1st Floor 30 Cannon Street
London EC4M 6XH
United Kingdom

(By online submission)

Dear Sir

RESPONSE TO EXPOSURE DRAFT ON INCOME TAX (ED/2009/2)

The Singapore Accounting Standards Council (ASC) appreciates the opportunity to comment on the Exposure Draft on Income Tax issued by the International Accounting Standards Board (IASB) in March 2009.

Our comments on the specific questions to the exposure draft are as follows:

Question 1 - Definitions of tax basis and temporary difference

The exposure draft proposes changes to the definition of tax basis so that the tax basis does not depend on management's intentions relating to the recovery or settlement of an asset or liability. It also proposes changes to the definition of a temporary difference to exclude differences that are not expected to affect taxable profit. (See paragraphs BC17–BC23 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

2 The exposure draft changes the definition of tax basis so that the presumed recovery of an asset is through sale alone. This presumption is arbitrary and restrictive and does not always reflect the economic purpose of holding an asset. Long-lived assets (for example, property, plant and equipment and intangible assets) are held for the production of goods and services and are not held for sale. However, applying the definition in the exposure draft, the tax basis of equipment, for example, is the amount that is deductible against taxable income if the carrying amount of the equipment had been recovered through sale at the end of the reporting period.

3 Yet elsewhere in the exposure draft, the "manner" in which an asset is recovered is not restricted to sale but is contingent on management's expectation of how an asset is to be recovered. For example, in paragraph 9, the exposure draft includes an initial step where an entity does not recognize deferred tax if there is no expected effect on taxable profit when the entity recovers the carrying amount of an asset or settles the carrying amount of a liability (paragraph 9). In this initial step, the entity forms an

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expectation of future taxable profit through the manner in which it recovers the carrying amount of an asset or liability. In Appendix B, Application Guidance, paragraph B14 requires consideration of the assumption about the tax consequences of recovering or settling the asset or liability as would be used by other market participants. This assumption would incorporate expectations of the manner in which an asset is to be recovered. These other paragraphs do not restrict the manner of recovery to sale alone.

4 Further, paragraph 17(b) explains that a temporary difference arises between the carrying amount and tax basis when income or expense is recognized in comprehensive income or equity in one reporting period but is recognized in taxable profit in a different period. This difference is essentially a "timing" difference between accounting and taxable income. There is an apparent inconsistency between the definition of the "tax basis" and other paragraphs of the exposure draft.

5 In our view, the exposure draft's definition of tax basis should not restrict the expected recovery of an asset through sale alone. The definition should be broad enough to incorporate the primary economic purpose(s) of an asset. To restrict the manner of recovery to sale alone is arbitrary and inconsistent with economic reality. Further, the definition of tax basis as it stands potentially create an inherent bias in the exposure draft to under-state the extent of deferred taxes, particularly in jurisdictions where capital gains are not taxable. This bias would contradict the exposure draft's intent to recognize deferred taxes, with minimum exceptions.

Question 2 – Definitions of tax credit and investment tax credit

The exposure draft would introduce definitions of tax credit and investment tax credit. (See paragraph BC24 of the Basis for Conclusions.)

Do you agree with the proposed definitions? Why or why not?

6 Yes, we agree.

Question 3 – Initial recognition exception

The exposure draft proposes eliminating the initial recognition exception in FRS 12. Instead, it introduces proposals for the initial measurement of assets and liabilities that have tax bases different from their initial carrying amounts. Such assets and liabilities are disaggregated into (a) an asset or liability excluding entity-specific tax effects and (b) any entity-specific tax advantage or disadvantage. The former is recognized in accordance with applicable standards and a deferred tax asset or liability is recognized for any temporary difference between the resulting carrying amount and the tax basis. Outside a business combination or a transaction that affects accounting or taxable profit, any difference between the consideration paid or received and the total amount of the acquired assets and liabilities (including deferred tax) would be classified as an allowance or premium and recognized in comprehensive income in proportion to changes in the related deferred tax asset or liability. In a business

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combination, any such difference would affect goodwill. (See paragraphs BC25–BC35 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

7 We recommend the Board to provide illustrations on the types of entity-specific factors and how they affect the recognition of allowances or premiums. The illustrations should provide guidance on how to apply the requirements of paragraph B13, especially how the allowance or premium should be reduced on a pro rata basis.

Question 4 – Investments in subsidiaries, branches, associates and joint ventures

IAS 12 includes an exception to the temporary difference approach for some investments in subsidiaries, branches, associates and joint ventures based on whether an entity controls the timing of the reversal of the temporary difference and the probability of it reversing in the foreseeable future. The exposure draft would replace these requirements with the requirements in SFAS 109 and APB Opinion 23 *Accounting for Income Taxes—Special Areas* pertaining to the difference between the tax basis and the financial reporting carrying amount for an investment in a foreign subsidiary or joint venture that is essentially permanent in duration. Deferred tax assets and liabilities for temporary differences related to such investments are not recognized. Temporary differences associated with branches would be treated in the same way as temporary differences associated with investments in subsidiaries. The exception in IAS 12 relating to investments in associates would be removed.

It proposes this exception from the temporary difference approach because the understanding is that it would often not be possible to measure reliably the deferred tax asset or liability arising from such temporary differences. (See paragraphs BC39–BC44 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not? Do you agree that it is often not possible to measure reliably the deferred tax asset or liability arising from temporary differences relating to an investment in a foreign subsidiary or joint venture that is essentially permanent in duration? Should the ASC select a different way to define the type of investments for which this is the case? If so, how should it define them?

8 We are of a view that the treatment is inconsistent with the overriding principle in the exposure draft to remove almost all exceptions to the temporary difference approach. The exposure draft appears to include a divergent principle to recognize a temporary difference from investments in subsidiaries and joint ventures only when it is "apparent that the temporary difference will not reverse in the foreseeable future". (Appendix B, Application Guidance B5). The restriction of the time horizon to the "foreseeable future" is incongruent with the rest of the exposure draft and creates a dual recognition approach in the exposure draft comprising of partial application for investments and comprehensive application for all others.

9 In addition, the header of this question and paragraph B3 seem to indicate that the exemption applies to foreign branches. However, the wordings in paragraph B5

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only cover foreign subsidiary and foreign joint venture. We believe that foreign branches should be included in the exemption.

10 Lastly, we recommend the Board to incorporate investments in associate and unremitted foreign earnings into the standard as the criteria that investments be "essentially permanent in duration" could similarly be applied to these two situations. For the unremitted foreign earnings, income arising overseas is not subject to tax unless it is remitted to the home countries that are under the "territorial" tax system.

Question 5 – Valuation allowances

The exposure draft proposes a change to the approach to the recognition of deferred tax assets. FRS 12 requires a one-step recognition approach of recognizing a deferred tax asset to the extent that its realization is probable. The exposure draft proposes instead that deferred tax assets should be recognized in full and an offsetting valuation allowance recognised so that the net carrying amount equals the highest amount that is more likely than not to be realizable against taxable profit. (See paragraphs BC52–BC55 of the Basis for Conclusions.)

Question 5A

Do you agree with the recognition of a deferred tax asset in full and an offsetting valuation allowance?

11 The one-step approach in IAS 12 emphasizes the "probable" nature of deferred tax assets whereas the two-step approach in the exposure draft upholds the "more likely than not" principle. In this regard, the existing treatment in IAS 12 is more consistent with the recognition principle in the *Framework* (paragraph 79 of the *Framework*).

Question 5B

Do you agree that the net amount to be recognised should be the highest amount that is more likely than not to be realisable against future taxable profit? Why or why not?

12 We recommend the Board weigh the costs and benefits of such a change, especially the new disclosure requirements.

Question 6 – Assessing the need for a valuation allowance

Question 6A

The exposure draft incorporates guidance from SFAS 109 on assessing the need for a valuation allowance. (See paragraph BC56 of the Basis for Conclusions.)

Do you agree with the proposed guidance? Why or why not?

13 Yes, we agree.

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Question 6B

The exposure draft adds a requirement on the cost of implementing a tax strategy to realise a deferred tax asset. (See paragraph BC56 of the Basis for Conclusions.)

Do you agree with the proposed requirement? Why or why not?

14 The timing of tax deduction for an expense incurred to implement a tax strategy does not follow the timing for realisation of tax benefits. Thus, attempting to match this expense against the deferred tax asset means unnecessary additional work. Furthermore, the expenses may not be easily identified.

Question 7 – Uncertain tax positions

FRS 12 is silent on how to account for uncertainty over whether the tax authority will accept the amounts reported to it. The exposure draft proposes that current and deferred tax assets and liabilities should be measured at the probability-weighted average of all possible outcomes, assuming that the tax authority examines the amounts reported to it by the entity and has full knowledge of all relevant information. (See paragraphs BC57–BC63 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

15 It is easier to determine and understand probable outcomes or most likely outcomes, than probability-weighted outcomes. Being easier to understand, it is therefore more meaningful to present probable outcomes or most likely outcomes. In jurisdictions that do not work on a self-assessment system, like Singapore's, taxpayers are not required by law to provide all relevant information to the tax authorities, but are required only to respond to specific queries posed by the tax authorities. Such queries are limited, unless there is a tax investigation. In such a situation, an accounting treatment that requires assuming that the tax authorities have all information would prejudice the interests of taxpayers that are currently protected by law, since some probability will have to be attached to a fuller investigation by the tax authorities, leading to a provision that could trigger lines of questioning that otherwise would not have been taken by the tax authorities. Hence, for ease of use and for jurisdictions that do not work on a self-assessment system, we recommend the Board to consider for an entity to use probable outcomes.

Question 8 – Enacted or substantively enacted rate

FRS 12 requires an entity to measure deferred tax assets and liabilities using the tax rates enacted or substantively enacted by the reporting date. The exposure draft proposes to clarify that substantive enactment is achieved when future events required by the enactment process historically have not affected the outcome and are unlikely to do so.

(See paragraphs BC64–BC66 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

16 While we agree with the clarification of the definition of "substantive enactment", there is likely to be potential confusion to subsume the term "enacted" in "substantively enacted". The normal English meanings of these two words cannot be the same but the exposure draft uses the term "substantively enacted" to include "enacted" in certain situations (Appendix B, Application Guidance paragraph B26).

Question 9 – Sale rate or use rate

When different rates apply to different ways in which an entity may recover the carrying amount of an asset, FRS 12 requires deferred tax assets and liabilities to be measured using the rate that is consistent with the expected manner of recovery. The exposure draft proposes that the rate should be consistent with the deductions that determine the tax basis, ie the deductions that are available on sale of the asset. If those deductions are available only on sale of the asset, then the entity should use the sale rate. If the same deductions are also available on using the asset, the entity should use the rate consistent with the expected manner of recovery of the asset. (See paragraphs BC67–BC73 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

17 Yes we agree.

Question 10 – Distributed or undistributed rate

FRS 12 prohibits the recognition of tax effects of distributions before the distribution is recognised. The exposure draft proposes that the measurement of tax assets and liabilities should include the effect of expected future distributions, based on the entity's past practices and expectations of future distributions. (See paragraphs BC74–BC81 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

18 Yes, we agree.

Question 11 – Deductions that do not form part of a tax basis

An entity may expect to receive tax deductions in the future that do not form part of a tax basis. SFAS 109 gives examples of 'special deductions' available in the US and requires that 'the tax benefit of special deductions ordinarily is recognized no earlier than the year in which those special deductions are deductible on the tax return'. SFAS 109 is silent on the treatment of other deductions that do not form part of a tax basis.

IAS 12 is silent on the treatment of tax deductions that do not form part of a tax basis and the exposure draft proposes no change. (See paragraphs BC82–BC88 of the Basis for Conclusions.)

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Do you agree that the exposure draft should be silent on the treatment of tax deductions that do not form part of a tax basis? If not, what requirements do you propose, and why?

19 Yes, we agree. Since these deductions do not form part of a tax basis, the principle governing asset recognition in the Framework and contingent gains should suffice to guide entities on the treatment of these deductions.

Question 12 – Tax based on two or more systems

In some jurisdictions, an entity may be required to pay tax based on one of two or more tax systems, for example, when an entity is required to pay the greater of the normal corporate income tax and a minimum amount. The exposure draft proposes that an entity should consider any interaction between tax systems when measuring deferred tax assets and liabilities. (See paragraph BC89 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

20 Yes, we agree.

Question 13 – Allocation of tax to components of comprehensive income and equity

FRS 12 and SFAS 109 require the tax effects of items recognised outside continuing operations during the current year to be allocated outside continuing operations. FRS 12 and SFAS 109 differ, however, with respect to the allocation of tax related to an item that was recognised outside continuing operations in a prior year. Such items may arise from changes in the effect of uncertainty over the amounts reported to the tax authorities, changes in assessments of recovery of deferred tax assets or changes in tax rates, laws, or the taxable status of the entity. FRS 12 requires the allocation of such tax outside continuing operations, whereas SFAS 109 requires allocation to continuing operations, with specified exceptions. The FRS 12 approach is sometimes described as requiring backwards tracing and the SFAS 109 approach as prohibiting backwards tracing.

The exposure draft proposes adopting the requirements in SFAS 109 on the allocation of tax to components of comprehensive income and equity. (See paragraphs BC90–BC96 of the Basis for Conclusions.)

Question 13A

Do you agree with the proposed approach? Why or why not?

The exposure draft deals with allocation of tax to components of comprehensive income and equity in paragraphs 29–34. It intends those paragraphs to be consistent with the requirements expressed in SFAS 109.

Question 13B

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Would those paragraphs produce results that are materially different from those produced under the SFAS 109 requirements? If so, would the results provide more or less useful information than that produced under SFAS 109? Why?

The exposure draft also sets out an approach based on the FRS 12 requirements with some amendments. (See paragraph BC97 of the Basis for Conclusions.)

Question 13C

Do you think such an approach would give more useful information than the approach proposed in paragraphs 29–34? Can it be applied consistently in the tax jurisdictions with which you are familiar? Why or why not?

Question 13D

Would the proposed additions to the approach based on the FRS 12 requirements help achieve a more consistent application of that approach? Why or why not?

21 Q13A to 13 D: Yes, we agree.

Question 14 – Allocation of current and deferred taxes within a group that files a consolidated tax return

FRS 12 is silent on the allocation of income tax to entities within a group that files a consolidated tax return. The exposure draft proposes that a systematic and rational methodology should be used to allocate the portion of the current and deferred income tax expense for the consolidated entity to the separate or individual financial statements of the group members. (See paragraph BC100 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

22 Yes, we agree.

Question 15 – Classification of deferred tax assets and liabilities

The exposure draft proposes the classification of deferred tax assets and liabilities as current or non-current, based on the financial statement classification of the related non-tax asset or liability. (See paragraphs BC101 and BC102 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

23 Yes, we agree.

Question 16 – Classification of interest and penalties

FRS 12 is silent on the classification of interest and penalties. The exposure draft proposes that the classification of interest and penalties should be a matter of accounting policy choice

to be applied consistently and that the policy chosen should be disclosed. (See paragraph BC103 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

24 We will like the Board to provide guidance on the classification of interest and penalties for consistency and to facilitate comparison.

Question 17 – Disclosures

The exposure draft proposes additional disclosures to make financial statements more informative. (See paragraphs BC104–BC109 of the Basis for Conclusions.)

Do you agree with the proposals? Why or why not?

It also considered possible additional disclosures relating to unremitted foreign earnings. It decided not to propose any additional disclosure requirements. (See paragraph BC110 of the Basis of Conclusions.)

Do you have any specific suggestions for useful incremental disclosures on this matter? If so, please provide them.

25 Yes, we agree. However, for the reconciliation of a period's tax expense with tax expense that was based on the parent entity's domestic statutory tax rate, we would like the Board to consider an alternative approach for an entity to use an applicable tax rate that provides the most meaningful information to the users of its financial statements.

Question 18 – Effective date and transition

Paragraphs 50–52 of the exposure draft set out the proposed transition for entities that use IFRSs, and paragraph C2 sets out the proposed transition for first-time adopters. (See paragraphs BC111–BC120 of the Basis for Conclusions.)

Do you agree with these proposals? Why or why not?

26 We agree with the proposals.

27 We hope that our comments will contribute to the IASB's deliberation on this exposure draft. Should you require any further clarification, do contact me. Thank you.

Yours faithfully,

Dexter Tan
Secretary, Accounting Standards Council

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