Mr. W Upton,

Chairman IFRS Interpretations Committee

Dear Mr. Upton,

Draft IFRIC Interpretation DI/2012/1 Levies Charged by Public Authorities on Entities that Operate in a Specific Market (the DI) [Submission deadline for IFRIC 5 September 2012]

I am writing on behalf of BusinessEurope in response to the invitation to comment on the Draft IFRIC Interpretation *Levies Charged by Public Authorities on Entities that Operate in a Specific Market (*the DI).

We do not agree with the finalisation of the DI in its current form for the principal reasons explained below.

Scope of the DI

We think that the defining of the scope of the DI between the specific exclusions of paragraph 4 and the indicative characteristics of paragraph 5 is insufficiently clear to avoid misunderstanding and unintended consequences.

Income taxes, as defined in IAS 12, are clearly out of scope,

However, the exclusion in paragraph 4(b) for taxes due only if a minimum *revenue* threshold is achieved implies that taxes involving thresholds based on other criteria (such as, for example, levels of expense or emissions quantities) would be within the scope. In these cases, the lack of consensus about the obligating event in the instance of a minimum threshold, as described in BC7, could be an obstacle to the consistent application of the DI.

We think that the exclusion of taxes involving thresholds represents a major shortfall in the DI, as it reduces the wider usefulness of the DI and blurs the hard line of the identification of the obligating event which the DI strives to impose. In addition, the lack of consensus in the Interpretations Committee leading to this exclusion underlines the difficulty of agreeing upon the obligating event and, in our view, undermines the robustness of the DI's consensus view that levy expense should neither be anticipated nor deferred.

In addition, the exclusion of levies which represent fines or penalties leads to a further area of uncertainty. If one takes the example of a "cap and trade" emissions quota scheme, in which the initial quotas are set for each entity and granted free of charge, and in which trading of unused quotas is permitted, the total quantity of emissions made in the early periods of the scheme's operation will inevitably exceed the total quantity of quotas available in the market. This will lead to a payment to a government or its agency based on a fixed monetary amount per tonne from one or more entities. If this payment is characterised or interpreted as a fine/penalty it will be outside the scope of the DI, whereas if it is seen as a levy per tonne emitted over the quota it will be within the scope.

Finally, the scope defined in paragraph 5 of the DI is very broad, particularly since the "specific market" referred to in the title of the DI can actually cover any operation in a specific country. It can therefore potentially cover a wide range of taxes which do not qualify as income taxes, including payroll-related taxes, asset-based taxes, emissions quotas and perhaps even sales-based taxes, such as VAT in the UK. It is difficult for us to anticipate what the effect of this might be, but we think there is a risk of unintended consequences.

Privileging form over substance

In our view, most if not all, the levies that are the subject of the DI will be, in substance, taxes created with the intention of raising revenue for national or local authorities, or, in some cases aimed at encouraging certain behaviours in entities. We think that it is important to recognise that the predominant economic function of these levies is to raise funds to finance the authorities for a period of one year or less, on a recurring basis. This is borne out, in our view, by the fact that such taxes are usually chargeable once per year and are often based on a full year's worth of activity. Furthermore, the requirement to collect funds as expeditiously as possible can lead to a deceptive setting of the point at which the 'obligating event' arises. In many instances, the purported trigger event is one that is set for administrative convenience or necessity rather than out of concern for accounting logic. When a levy of the type discussed above is called for payment once per defined period on a recurrent basis, the nature of such a levy is a charge for the entity in respect of the complete period, and income for the levying authority for the complete period. We cannot agree with the premise of the DI that the economic substance of the charge is that it is a charge in respect of just one day in the year of the entity, and we have reason to think that users of financial statements are of the same view. The periodicity of the levy is a strong indicator of the economic life of the charge, and in our view, allocation of the charge to the corresponding period represents the substance of the transaction in many cases. We note that the FASB's Accounting Standards Update N° 2010-27 reached the same conclusion in respect of a specific annual levy raised in the USA.

Interpretations of "Liability" and the obligating event to improve the usefulness of financial information

We note that there are a number of specific provisions in several IFRS's which do not conform to a narrow interpretation of the obligating event such as that used in the DI. These include, for example, the recognition of deferred tax liabilities reflecting future fiscal effects in IAS 12, the recognition of non-vested share-based payments in IFRS 2, the recognition of non-vested pension rights in IAS 19, the recognition of bonuses in IAS 34 and the accounting for employer's payroll taxes and insurance contributions in IAS 34. In our view, the purpose of these provisions is to reflect substance rather than form in order to present the most useful information to the user, and we agree with that approach.

We also note the divergences of opinion among the members of the IASB and the FASB in their joint discussions (joint Boards meeting of September 2010 about the nature of the obligating event in the case of emissions schemes where a levy becomes payable once a defined threshold of emissions is reached. This lack of consensus reflects that of the Interpretations Committee referred to above.

These two elements indicate to us that a broader and deeper review of this topic is required than that that can be achieved through an Interpretation, and that the DI's proposed solution is too polarised and definitive to be useful.

Furthermore, we are not convinced of the relevance of the arguments cited in the DI about the existence or otherwise of a constructive obligation when the entity can avoid it by taking an unrealistic action. The nature of such levies is that there is no normal reciprocal commercial relationship between the authority and the paying entity. The management cannot make a normal economic decision about paying the levy in the same way as it could about ceasing production and paying redundancy costs or paying an entry fee for a franchise. Paying the levy is a consequence of the real economic decisions which are to be made by management and is just one of many factors to be taken into account in that decision.

We think a more appropriate approach is to look at the substance of the levy taking into account both the charging basis and the nominal 'obligating event', and to determine the period to which the charge and obligation relate by assessing the persuasive weight of the circumstances. The charge should then be allocated to that period on a systematic and rational basis, which, for example, would not include the allocation of an annual charge to a single day in the year.

We therefore think that it is not useful to users of financial statements to arrive at a definitive interpretation on the area covered by the scope of this DI. We wonder whether it would not be more helpful for such levies to be dealt with in the scope of a major project on all the various types of charge which could be covered by the broad term 'taxes' or 'levies', other than income taxes. If such an approach were also broadened to include threshold-based levies it might better provide for long-term consistency of treatment for all such items.

Conclusion

We think that the scope of the DI is not sufficiently precise to ensure that it will achieve consistent application across entities and jurisdictions.

The DI is based on what we think is a very theoretical and narrow interpretation of the topic and places too much of its focus on the accounting for the liability, rather than on the transaction as an economic whole. It seems to us to privilege form over substance. We think it will thus result in information which will not represent the economics of the transaction from the entity's standpoint and will therefore, in our view, be unhelpful for the user, who will have to adjust the financial statements to arrive at a useful measure of performance and a forecast of future cash flows.

The DI will introduce divergence from recent US GAAP in at least one instance, while, in our view, potentially not eliminating diversity in practice to any substantial extent.

Consequently, we do not agree with the publication of the DI as an Interpretation.

If you require any further information on any of the above, please do not hesitate to contact me,