



ACCOUNTING FOR INCOME TAX OF PUBLIC SECTOR ENTITIES

Issue

The AASB received a request to consider whether for-profit public sector entities that are required to pay income tax equivalents under the National Tax Equivalent Regime (NTER) should continue to apply AASB 112 *Income Taxes*.

The AASB considered the issue of whether income tax equivalents paid by for-profit public sector entities should continue to be accounted for within the scope of AASB 112. The submitter contended that payments under the NTER are not in the nature of an income tax; rather, they are in the nature of a distribution to owners and should not be within the scope of AASB 112.

Reasons for Not Adding the Issue to the AASB's Agenda

In considering this issue, the AASB noted that income taxes are defined in AASB 112 (paragraph 2) to include 'all domestic and foreign taxes which are based on taxable profits'. Taxable profit is defined in AASB 112 as '...the profit (loss) for a period, determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable (recoverable)' (paragraph 5).

The AASB further noted that in March 2006 the International Financial Reporting Interpretations Committee (IFRIC) considered the scope of IAS 12 *Income Taxes*. The IFRIC decided not to provide guidance on which taxes are within the scope of IAS 12. The IFRIC agenda decision noted, *inter alia*, that:

- the term 'taxable profit' implies a notion of a net rather than gross amount; and
- because taxable profit is not the same as accounting profit, taxes do not need to be based on a figure that is exactly accounting profit to be within the scope.

NTER payments are made in instalments to the State or Territory government on a Pay As You Go basis. The amount of each NTER instalment to be paid by an entity is calculated as the product of multiplying two factors – the entity's instalment income multiplied by an instalment rate. Instalment income is calculated as the net of assessable income and deductible expenses in accordance with the Federal income tax laws. The instalment rate is the rate specified by the Commissioner of Taxation or a self-selected rate as determined by the entity.

The AASB confirmed that, given the method of calculating the amount of NTER, the entity's instalment income has the attribute of a taxable profit, i.e., a net amount and is, in substance, an income tax as defined in AASB 112. The AASB also noted that this conclusion is not affected by constitutional matters as to whether such a tax should be imposed.

The AASB also gave consideration to the nature of the relationship between the State/Territory governments and the entities they own. The AASB noted that the NTER changes the nature of the relationship between the entity and its owner because its operation deprives the owner of the ability to determine the amount and timing of profits it wishes to receive. Additionally, the determination of the amount and timing of NTER payments is consistent with that imposed by the income tax regime the NTER purports to mirror. Accordingly, the AASB decided that the owner (State/Territory government) is not receiving NTER payments in its capacity as an owner.

The AASB also noted that the application of AASB 112 enhances the transparency of an entity's reporting and comparability with other entities within and outside the public sector.

On the basis of the analysis performed and in light of the existing requirements in Australian Accounting Standards, the AASB determined that an amendment to AASB 112 was not necessary. Consequently, the AASB decided not to add this issue to its agenda.