Ernst & Young
200 George Street
Sydney NSW 2000 Australia
GPO Box 2646 Sydney NSW 2001

Tel: +61 2 9248 5555
Fax: +61 2 9248 5959
ey.com/au

Ms Kris Peach
Chairperson
Australian Accounting Standards Board
PO Box 204
Collins St West VIC 8007

23 February 2018

AASB Draft Appendix to the Tax Transparency Code

Dear Ms Peach

Ernst & Young is pleased to submit its comments on the AASB Draft Appendix to the Tax Transparency Code ("TTC"). Our detailed responses to this guidance are contained in Appendix A: *Feedback on the content of the AASB Draft Appendix to the Tax Transparency Code* to this letter.

Overall we support the effort of the Australian Accounting Standards Board ("the Board" or the "AASB") to assist entities meet the TTC recommendations for the suggested tax reconciliation and calculation of the TTC effective tax rate (ETR) by issuing guidance outlying factors to consider in preparing and presenting tax disclosures for the purpose of the TTC.

However, as detailed in our responses to specific questions posed in the draft Appendix and other matters, we note that the AASB provided recommendations beyond what was requested by the Board of Taxation and some of these seem to create inconsistencies with the objectives of the TTC. There are also several examples of inconsistency between the guidance and illustrative examples provided. Additionally, to assist preparers meet the objectives of the TTC, we believe that the illustrative examples should also be expanded to cover common scenarios. We refer to our specific comments on these matters in Appendix A.

Should you wish to discuss this letter with us, please contact Melissa Sim on (02) 9276 9965 or Clare Jassal on (02) 9276 9667.

Yours faithfully

Ernst + Young

Ernst & Young

Appendix A: Feedback on the content of the AASB Draft Appendix to the Tax Transparency Code

1. **Whether the guidance outlining factors to consider in preparing and presenting tax disclosures for the purposes of the TTC is useful**

While we consider the factors to consider in preparing and presenting tax disclosures for the purposes of the TTC to be useful, we believe that the AASB guidance provides recommendations that are in addition to the requirements of the TTC.

The Board of Taxation requested that the AASB develop guidance to assist entities meet the recommendations provided in the TTC for the suggested tax reconciliation and calculation of the TTC ETR. The AASB guidance however extends beyond this objective.

Location of Part A disclosures

The TTC gives preparers a choice of whether Part A disclosures are to made within an improved tax disclosure in the entity's Australian general purpose financial reports or via publication of a 'taxes paid' report or another document. The draft Appendix focuses on (amongst other things) 'duplication and cross referencing' in order to determine where to disclose such information (paragraph 21). Although useful, this guidance goes above and beyond the areas the Board of Taxation was seeking recommendations on and it is unclear whether a 'taxes paid' report should actually standalone which would make consideration of duplication and cross-referencing redundant.

Application of ASIC Regulatory Guide 230 Disclosing non-IFRS financial information (RG 230)

The draft Appendix notes that ETRs are considered non-IFRS measures and that accordingly, both the accounting and TTC ETRs should be presented together, regardless of where the TTC ETRs are located (paragraph 45). While we agree that this is best practice and RG 230 is required to be applied if disclosures accompany the financial statements, it is unclear why this is always the case where disclosures are made within in a separate taxes paid report.

The AASB note that RG 230 sets out ASIC's views in respect of the interpretation and application of the *Corporations Act 2001* providing non-IFRS information inside and outside the financial statements (paragraph 26). We are unclear on the basis on which RG 230 is relevant to a separate taxes paid report and hence why it continues to be referenced in the guidance in this manner.

In addition, we have detailed comments on some aspects of the guidance. Where not covered in other specific questions we have addressed in question 7 regarding other matters.

2. **Whether the TTC effective tax rates should be calculated using accounting profit determined in accordance with accounting standards as the denominator, or an alternative denominator where considered useful (e.g. underlying earnings) or if, as currently proposed in this guidance the TTC effective tax rate should be based on either, as considered appropriate by the entity? Please indicate reasons why you prefer one or the other, and the impact, if any, on comparability with other entities**

Per section 8.1 of the TTC, the Board of Taxation recommends that the AASB establish "*a common definition of ETR to ensure consistency and comparability of disclosures made under the TTC*". In order to create consistency and comparability, ideally accounting profit determined in accordance with accounting standards should be used as the denominator. However entities also commonly report alternative profit measures (non-IFRS financial information) in the notes to the financial statements on the basis that they are useful for investors and other users of this information. Where such measures are not misleading, we agree with the calculation of TTC ETR using an alternative measure.

RG 230 indicates when it is and is not appropriate to use non- IFRS financial information. We recommend similar guidance/cross-reference to this guidance would be useful in the Appendix to the TTC to ensure relevant disclosures are being made.

3. Whether further guidance in relation to Part B TTC disclosures would be useful, and if so, what specific matters should be addressed?

Per the TTC, Part B disclosures should include information on an entity's tax policy, tax strategy and governance, total tax contribution and international related party dealings.

This information will be entity specific, and therefore we do not believe further guidance in relation to Part B TTC disclosures would be useful, as this may encourage boilerplate or generic disclosures.

Entities should be encouraged to determine the degree and content of disclosure that best communicates relevant information on their tax strategies in order to add value, understanding and context to users of tax information without obscuring important information, in line with the objectives of the TTC.

4. Whether the illustrative examples are helpful, and if not, why not?

We believe the examples provided in the Appendix are helpful. However, treatment of certain specific transactions:

- May not be consistent with the guidance
- May be seen as interpreting accounting standards
- Does not appear to be complete so may encourage incomplete disclosures.

We note that both examples calculate the ETR as 'accounting' income tax expense divided by accounting profit. The TTC notes that the ETR should be calculated as 'company income tax expense' divided by accounting profit and paragraphs 29-31 of the draft Appendix refer to the TTC ETR as being calculated based on 'company tax expense', which in table 1 appears to refer to the taxes incurred by an entity which from an accounting point of view might have been intended to equate with 'current tax expense' (whether recognised in profit or loss, other comprehensive income or equity) only (and exclude 'deferred tax expense'). Further, the example does not address amounts recognised in other comprehensive income which per the above definition ought to be included in the calculation. We would recommend the example and guidance is updated to specifically indicate how amounts recognised in other comprehensive or equity should be dealt with.

The guidance should clarify which basis is correct. A current tax basis is consistent with the analysis in paragraph 70 of the draft Appendix regarding non-deductible impairments but is not reflected as such in the examples due to the inclusion of the deferred tax expense.

We note inconsistent use of the terms "current/company/income" tax expense (paragraph 53). The guidance appears to be using different terms interchangeably. We recommend consistent use of terminology. This then flows to the examples as the disclosures shown do not actually present the disclosures as required by the TTC being a reconciliation between income tax expense to income tax paid or payable, (in this respect we note the reconciliations required by the TTC are based on 'income tax expense' whereas the ETR calculation required is based on 'company tax expense' which per the draft guide are two different numbers but this is not the presentation provided in the example disclosures).

In addition we note the following specific comments on each of the examples in the draft Appendix in addition to the general comments above.

Illustrative example 1:

- If any deferred tax expense is to be included in the calculation of the final income tax expense, we would expect that this would be a positive number, not negative as shown in the example.

Illustrative example 2

- With regard to the treatment of the research and development (R&D) tax offset in the example, we highlight that there are different views as to whether an R&D tax offset should be treated as an income tax under AASB 112 *Income Taxes* or a government grant under AASB 120 *Accounting for Government Grants and Disclosure of Government Assistance*. This can depend on the type of R&D tax offset which varies by the size of an entity. We would recommend that either a) an assumption is made in the example to clarify which Standard this grant falls under (as we do not believe it is appropriate to interpret the accounting standards) or b) replace the example.
- Utilisation of tax losses has been included as a recurring item within the reconciliation of accounting profit to income tax expense and income tax payable. While it would be expected that this would appear in the tax payable reconciliation for a given year, this does not impact what is incurred (rather it is a means to offset payments) and therefore this disclosure does not seem to be required.
- The share of associate's post-tax profit has not impacted deferred tax balances. If this is the case, it should be noted in the example that while no deferred tax balance has been created, this will not always be the case as temporary differences can arise on investments in associates.
- Footnote 2 to the ETR calculation notes the exclusion of PRRT of A$12,000 resulted in 2% difference between the accounting and TTC ETRs. The example does not clarify whether the affect is the same for both the global and Australian TTC ETR which may create confusion. The footnote should clarify the different impact between Australia and global.

5. Whether an illustrative example setting out Part A TTC disclosures for an entity that incurs tax losses for a financial year would be helpful?

Yes, we believe that an illustrative example setting out Part A TTC disclosures for an entity that incurs tax losses for a financial year would be helpful to entity's preparing and presenting tax disclosures for the purposes of the TTC given the limited number of examples currently available.

6. Whether the guidance, when finalised, should be issued as AASB extrinsic material (e.g. a Practice Statement) or as an Appendix to the TTC

Given that The Board of Taxation requested that AASB develop guidance to assist businesses meet the minimum standards required by the TTC, we believe the guidance, when finalised, should be issued as an Appendix to the TTC to support the effective operation of the TTC.

7. Whether there are any other matters pertaining to Part A of the TTC that this Appendix should cover.

Guidance for calculating TTC ETR

Definition of "global operations"

Paragraph 36 defines an entity's "global operations" as their worldwide consolidated group which includes all entities consolidated in accordance with AASB 10 *Consolidated Financial Statements* if there is Australian parent or IFRS 10 *Consolidated Financial Statements* or an equivalent accounting standard where the parent is not Australian. This definition does not clarify how the "global operations" of an investment entity would be identified if it does not present consolidated financial statements due to having to measure all of its subsidiaries at fair value.

Amended assessments

It is noted by the AASB that where any material under or overstatements, interest, penalties or refunds relating to prior year assessments are eliminated for the current year, the prior year ETR calculation should be restated and an explanation provided for the change (paragraph 31). Given there is no requirement in the TTC for comparative information to be presented, we understand that this guidance was included by the AASB based on best practice. The reason for this inclusion should be clarified.

Also, the AASB note in paragraph 74, '*the income tax effect of an error should be recognised in the same way as the transaction giving rise to the error itself. An amended assessment that is associated with the correction of a material prior period error is unlikely to be reflected in the current year ETR. The effect of some other amended assessments e.g. some amended assessments initiated by the tax authority reflecting will affect the ETR where it relates to an item recognised in profit or loss rather than in other comprehensive income*'. The guidance here is unclear as:

- Paragraph 31 does not make such a distinction between errors and other amendments as suggested by paragraph 74
- As noted in question 4, the treatment of amounts recognised in other comprehensive income is unclear
- The last sentence in paragraph 74 appears to be jumbled and does not read clearly.

Penalties

The AASB guidance notes that where an entity incurs a penalty, the amount is recognised as an expense in profit or loss and where a penalty is non-deductible for income tax purposes, it will represent a permanent difference in the period in which the penalty is incurred.

In an agenda decision issued by the IFRS Interpretations Committee in September 2017 the Committee observed that entities do not have an accounting policy choice between applying IAS 12 *Incomes Taxes* and applying IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* to interest and penalties. In effect each tax regime will need to be assessed separately to determine whether penalties and interest should be accounted for under IAS 12 or IAS 37. We do not believe this is an appropriate place to interpret the accounting standards with respect to the Australian tax regime.

Other

Figure 1 on page 7 includes a statement "where TTC disclosures are made in the financial statements and have not been audited…". It would be better if the guidance references that this information could be included as an appendix to the financial statements/addendum as under the Corporations Act, our responsibility is to form an opinion that the financial report is in accordance with accounting standards and gives a true and fair view.

Paragraph 24 also refers to TTC disclosures made in a separate 'taxes paid' report and whether the separate report is included or excluded from the financial statement audit. We question the need for clarity around the audit of taxes paid report as this does not form part of the financial statements.

Paragraph 50 refers to Attachment 2 however there is no Attachment 2 to the guidance document.