

This Agenda Paper discusses the application of AASB 112 *Income Taxes* to a superannuation plan or approved deposit fund.

Background

1. Paragraph 30 of AAS 25 *Financial Reporting by Superannuation Plans* states, in part, that:

“Expenses of a superannuation plan may include benefits accruing to plan members and beneficiaries as a result of membership of the plan during the period, general administration expenses, expenses directly related to investment activities, income tax expenses (including capital gains tax) determined in accordance with the provisions of Australian Accounting Standard AAS 3 ‘Accounting for Income Tax (Tax-effect Accounting)’ and other expenses...”
2. The reference to AAS 3 is ambulatory and is currently read as relating to AASB 112 *Income Taxes*. Accordingly, superannuation plans currently apply AASB 112. It is also relevant to note that, when applicable, superannuation plans also apply UIG Interpretation 1019 *The Superannuation Contributions Surcharge* (September 2004). Although the superannuation contributions surcharge no longer applies, balances relating to the surcharge remain in the accounts of some members of defined benefit superannuation plans.

The application of AASB 112 under a replacement Standard for AAS 25

3. The application of AASB 112 by a superannuation plan or approved deposit fund (ADF) gives rise to deferred tax liabilities and/or assets in respect of a number of items, including:
 - (a) unrealised losses and unrealised gains on investments;
 - (b) accrued investment income and expenses; and
 - (c) contributions receivable.
4. From discussions with members of the Project Advisory Panel, staff have been unable to identify any substantive superannuation-specific issues arising from the current application of AASB 112 by a superannuation plan or an approved deposit fund (ADF). Moreover, the requirements in AASB 112 are not necessarily inconsistent with the Board’s decisions to date in relation to its comprehensive review of AAS 25. For instance, deferred tax assets and liabilities attributable to investments held by a superannuation plan or ADF may be considered to be measured at their realisable value if the asset was sold or the superannuation plan were wound up on the reporting date.

Staff view 1

Staff consider that, under a replacement Standard for AAS 25, a superannuation plan or ADF should be required to apply AASB 112 and, when applicable, UIG Interpretation 1019.

Implications of applying AASB 112 in the context of a fair value model

5. Although the requirements in AASB 112 are not necessarily inconsistent with the Board's decision that a superannuation plan or ADF should fair value all of its assets and liabilities, the application of AASB 112 in the context of a fair value model does raise a question about whether the possible difference between, for instance, the timing of the recognition of a tax liability and the payment of tax on the gain from sale should be acknowledged through discounting.
6. At its November 2006 meeting, the Board agreed that the appropriate accounting treatment for superannuation entities needs to be consistent with, among other things, the IASB's views on fair value accounting. If a deferred tax asset or liability were to be measured in accordance with the IASB's proposals in its *Fair Value Measurements* (FVM) Discussion Paper, it would arguably (where necessary) be discounted to its present value. For instance, the fair value measurement of a deferred tax asset or liability in accordance with the income approach would require a superannuation plan or ADF to use:

“...valuation techniques to convert future amounts (for example, cash flows or earnings) to a single present amount (discounted). The measurement is based on the value indicated by current market expectations about those future amounts. Those valuation techniques include present value techniques...” (paragraph 18(a) of the FVM Discussion Paper)
7. In contrast to the proposed approach under the IASB's FVM, AASB 112 prohibits discounting of deferred tax assets and liabilities. Paragraph 53 of AASB 112 states that:

“Deferred tax assets and liabilities shall not be discounted.”
8. Superannuation plans currently recognise deferred tax assets and liabilities that may not be reversed in the short-term. Such deferred tax assets and/or liabilities may arise from a number of situations, including:
 - (a) the recognition of unrealised losses or gains on investments the trustee intends the plan or ADF to hold over the longer term; and
 - (b) the recognition of contributions receivable in relation to defined benefit members.
9. However, the circumstances under which a superannuation plan or ADF recognises a deferred tax asset or liability are generally not unique to such entities. Accordingly, a different treatment for a superannuation plan or ADF would not appear to be justified. For instance:
 - (a) managers of non-superannuation entities that apply IFRSs may plan for their entities to hold investments over the longer term. These entities, however, are not permitted to discount any deferred tax assets or liabilities arising from unrealised losses or gains on such investments. Accordingly, either permitting or requiring a superannuation plan or ADF to discount any deferred tax assets or liabilities that will not be reversed in the short-term would diminish the comparability of the financial statements of such entities with the financial statements of non-superannuation entities; and
 - (b) paragraph 54 of AASB 112 states, in part, that:

“The reliable determination of deferred tax assets and liabilities on a discounted basis requires detailed scheduling of the timing of the reversal of each temporary difference. In many cases such scheduling is impracticable or highly complex. Therefore, it is inappropriate to require discounting of deferred tax assets or liabilities...”

Contributions receivable that are based on an enforceable contract aside, it is likely that a superannuation plan or ADF will face the same difficulties in estimating the timing of the reversal of their deferred tax assets and liabilities that other entities do with respect to their deferred tax assets and liabilities. Accordingly, contributions aside, the arguments in AASB 112 against deferred tax assets and liabilities being discounted would appear to apply equally to superannuation and non-superannuation entities.

10. With respect to contributions receivable, it is relevant to note that:
- (a) all member contributions that are deducted from an employee’s salary or wages are required to be remitted promptly to a superannuation plan (within 28 days of the end of the month in which the deduction was made);
 - (b) Superannuation Guarantee contributions are required to be paid quarterly; and
 - (c) ‘top up’ employer contributions in relation to a deficiency in assets attributable to a superannuation plan’s defined benefit members compared with the members’ accrued benefits would normally be received by the plan within 3 to 5 years of the actuarial review that formally identifies the deficiency.

Accordingly, a deferred tax liability arising from the recognition of contributions receivable would normally be expected to be reversed within 3 to 5 years. On this basis, the difference between discounting and not discounting a deferred tax liability arising from the recognition of contributions receivable may not be significant.

Staff view 2

On balance, staff consider that, consistent with paragraph 53 of AASB 112, deferred tax assets and liabilities held by a superannuation plan or ADF should not be discounted.

