



Grant Thornton

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Australian Accounting Standards Board
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Dear Kevin

AASB ED 204 & IASB ED 2010/11 DEFERRED TAX RECOVERY OF UNDERLYING ASSETS

Grant Thornton Australia Limited (Grant Thornton) is pleased to provide the Australian Accounting Standards Board with its comments on ED 204 which is a re-badged copy of the International Accounting Standards Board's (the Board) Exposure Draft ED 2010/11 (the ED). We have considered the ED as well as the accompanying draft Basis for Conclusions, and set out our main comments below. Our responses to the questions in the ED's Invitation to Comment and the AASB's separate questions are set out in the Appendix.

Grant Thornton's response reflects our position as auditors and business advisers both to listed companies and privately held companies, and public and private businesses, and this submission has benefited with some initial input from our clients, Grant Thornton International which is working on a global submission to the IASB, and discussions with key constituents.

The views expressed here are preliminary in nature, and a more detailed Grant Thornton global submission will be finalised by the IASB's due date of 9 November 2010.

While we welcome the Board's efforts to engage with its constituents, and seek ways to make IFRS easier to apply, we do not support the proposals in the ED. We believe that IAS 12's principle that the measurement of deferred tax liabilities and deferred tax assets should reflect the manner in which an entity expects to recover or settle the carrying amount of its assets and liabilities is clear, appropriate and does not warrant an exception.

We accept that, in some jurisdictions and circumstances, applying this principle can be challenging. In our experience this is generally because an entity's intentions for a specific asset may be to use it for a period then sell it (mixed use), calling for a blended approach to

deferred tax measurement. However, the usage period, timing of sale and sale proceeds are all uncertain and subject to change. Accordingly, application of the measurement principle requires the use of estimates and reasoned management judgement. However, in our view this is an inherent feature of a principle-based system and we are not convinced that the challenges are notably onerous in comparison to many other IFRS principles for which no exception is available.

We are also disagree that the proposed scope of the amendment is limited to assets measured using the fair value models of IASs 16, 38 or 40. The Board reasons that using fair value implies recovery of an asset's carrying value through sale, and that the cost model implies recovery through use. We find this analysis unconvincing, given that the measurement model in these IASs is an accounting policy choice. Having said this, we do acknowledge that fair value measurement itself may lead to more significant temporary differences.

If the Board is to create an exception to IAS 12's general principle we recommend that its scope is based only on the asset types most commonly subject to "dual rate" (or dual tax base) regimes, without reference to measurement basis. In our experience these asset categories are investment properties and own use land and buildings.

We note that the AASB plans to issue a separate consultative document outlining the AASB's Tier 2 disclosure proposals. In our view we believe that non-publicly accounting reporting entities should have the option to adopt the IASB's IFRS for SMEs accounting standard which is available for use in most overseas jurisdictions. That standard is far simpler and less costly to use compared to the AASB's Tier 2 RDR accounting standard.

If you require any further information or comment, please contact me.

Yours sincerely

GRANT THORNTON AUSTRALIA LIMITED



Keith Reilly
National Head of Professional Standards

Appendix 1: Response to the invitation to comment questions

Invitation to comment questions

Question 1 – Exception to the measurement principle

The Board proposes an exception to the principle in IAS 12 that the measurement of deferred tax liabilities and deferred tax assets should reflect the tax consequences that would follow from the manner in which the entity expects to recover or settle the carrying amount of its assets and liabilities. The proposed exception would apply when specified underlying assets are remeasured or revalued at fair value.

Do you agree that this exception should apply when the specified underlying assets are remeasured or revalued at fair value?

Why or why not?

We are aware that, in some jurisdictions, recovery of an asset through use or through sale has different tax consequences. The manner of recovery may affect the tax rate, tax base or both. These tax regimes create challenges in applying IAS 12's principle that the measurement of deferred tax should reflect the expected manner of recovery. In our view the primary sources of difficulty are that assets are often "mixed use" (ie recovery will be partly by use and partly by sale), and that intentions may be unclear, undecided and subject to change.

Nonetheless, we do not support the proposed measurement exception (or its proposed scope - see our response to Question 2). We believe that IAS 12's principle that the measurement of deferred tax should reflect the expected manner of recovery of the underlying asset is clear and representationally faithful. Although applying this principle can involve judgement and estimation uncertainly, we suggest that the degree of difficulty so caused is no greater than many other areas of IFRS.

Question 2 – Scope of the exception

The Board identified that the expected manner of recovery of some underlying assets that are remeasured or revalued at fair value may be difficult and subjective to determine when deferred tax liabilities or deferred tax assets arise from:

- a investment property that is measured using the fair value model in IAS 40;
- b property, plant and equipment or intangible assets measured using the revaluation model in IAS 16 or IAS 38;
- c investment property, property, plant and equipment or intangible assets initially measured at fair value in a business combination if the entity uses the fair value or revaluation model when subsequently measuring the underlying asset; and
- d other underlying assets or liabilities that are measured at fair value or on a revaluation basis.

The Board proposes that the scope of the exception should include the underlying assets described in (a), (b) and (c), but not those assets or liabilities described in (d).

Do you agree with the underlying assets included within the scope of the proposed exception?

Why or why not? If not, what changes to the scope do you propose and why?

In view of our objections to the proposed exception, we would prefer that any exception made is tightly focused on the asset categories that are most commonly subject to "dual rate" (or dual tax base) regimes, without reference to measurement basis. In our experience these asset categories are investment properties and own-use real estate (land and buildings).

As noted in our covering letter, we are not convinced that there is a robust basis to link an entity's choice of measurement model with its expected manner of recovery.

Accordingly, we suggest that the scope of any amendment be limited to investment property and other real estate assets, irrespective of measurement model. At the same time, the guidance included in SIC Interpretation 21 'Income Taxes - Recovery of Revalued Non-Depreciable Assets' could be incorporated into IAS 12.

Question 3 – Measurement basis used in the exception

The Board proposes that, when the exception applies, deferred tax liabilities and deferred tax assets should be measured by applying a rebuttable presumption that the carrying amount of the underlying asset will be recovered entirely through sale. This presumption would be rebutted only when an entity has clear evidence that it will consume the asset's economic benefits throughout its economic life.

Do you agree with the rebuttable presumption that the carrying amount of the underlying asset will be recovered entirely by sale when the exception applies?

Why or why not? If not, what measurement basis do you propose and why?

Should the Board decide to introduce the exception, we agree with the use of a rebuttable presumption that the carrying amount of the underlying asset will be recovered entirely by sale. This would offer a pragmatic simplification without eliminating the possibility of applying an expected manner of recovery approach when there clear evidence that the asset's economic benefits will be recovered through use.

Notwithstanding our qualified support, we have some concern that the requirement for clear evidence may be interpreted differently. In practice we expect that entities that prefer not to rebut the presumption will be self-selecting (in that they will not attempt to collect the necessary evidence).

Question 4 – Transition

The Board proposes that the amendments should apply retrospectively. This requirement includes retrospective restatement of all deferred tax liabilities or deferred tax assets within the scope of the proposed amendments, including those that were initially recognised in a business combination.

Do you agree with the retrospective application of the proposed amendments to IAS 12 to all deferred tax liabilities or deferred tax assets, including those that were recognised in a business combination?

Why or why not? If not, what transition method do you propose and why?

Should the amendments be made we support retrospective application subject to the following comment. For deferred tax assets and liabilities relating to assets acquired in a business combination, retrospective restatement would be restatement of goodwill. This may in turn require re-performance of past impairment tests. This leads us to question whether the additional complexity of retrospective restatement is justified on cost-benefit grounds. An alternative would be to adjust retained earnings rather than goodwill in these circumstances.

Question 5 – Other comments

Do you have any other comments on the proposals?

We have no other comments.

Specific AASB questions

1 Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:

- a not-for-profit entities; and**
- b public sector entities**

Apart from our earlier comments, we are not aware of any regulatory issues that may effect the implementation of the proposals.

2 Whether, overall, the proposals would result in financial statements that would be useful to users;

Apart from our earlier comments, we are not aware of any issues that may impact users.

3 Whether the proposals are in the best interests of the Australian and New Zealand economies.

For publicly accountable entities, apart from our earlier comments on the proposals, we are not aware of any reasons that would impact on the interests of the Australian economy and our New Zealand firm may wish to comment direct to the AASB if there are any New Zealand implications.