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Mr. Wolf Klinz
EFRAG Financial Reporting Board Chair
35 Square de Meeûs
1000 Brussels
Belgium

Comment letter on the EFRAG Draft Comment Letter on the Exposure Draft *Provisions—Targeted Improvements*, Proposed amendments to IAS 37

Dear Mr Klinz,

Thank you for the opportunity to comment on the EFRAG draft comment letter (EFRAG DCL). Our main concern is that the amendments could lead to earlier recognition of bank levies compared to the existing treatment in accordance with IFRIC 21 *Levies*. We are against such a fundamental change of the current practice. We also consider that it goes beyond what targeted improvement should be focused on. Please find below our comments on the specific questions raised by EFRAG.

Kind regards,

Gabriele Tauböck
Head of Group Accounting

EFRAG Questions to Constituents

Paragraphs 7 to 8 list arguments in favour and against the proposals in the ED on when a present obligation exists as a result of a past event.

1.1 Do you have additional arguments in favour and against the proposals?

1.2 Do you support (some of) the proposals, or would you prefer the current requirements as reflected in IFRIC 21? Would your answer depend on the type of provision being considered (e.g. reciprocal versus non-reciprocal transactions)? If so, for which types of provisions would you support/not support the proposals?

1.3 The ED proposes to maintain the requirements that a provision should only be recognised if (1) it is probable that an entity will be required to transfer an economic resource to settle the obligation; and (2) a reliable estimate can be made of the amount of the obligation. It will still be specified that it is only in extremely rare cases that an entity will not be able to make a reliable estimate of the amount of the obligation. Do you consider that these requirements should be amended following the proposals of the ED on when an entity has a present obligation?

1.4 Would the proposals have any economic impact on some sectors (e.g. sectors in which funds have to be set aside to cover provisions)?

1.5 Could you foresee the proposals resulting in any unintended consequences? If so, which?

1.6 Do your answers to the question above depend on whether you consider the proposed requirements in relation to the annual financial report or in relation to an interim financial report? If so, please specify how your answers differ for the two types of financial reports.

Targeted improvements should not fundamentally change the established practice for recognising levies based on IFRIC 21 requirements. As a result, we fully support the arguments in paragraph 8 of the EFRAG DCL against the proposals in the ED.

In situations when a levy is charged only if an entity takes two (or more) separate actions which span over more periods we do not consider it is the first action which leads to recognising the provision. This action means that the entity just generates the tax basis, i.e. it relates to the measurement rather than recognition of the liability.

As mentioned in the EFRAG DCL, the matching principle should not apply between revenues from business with customers and payments to the government. We also note that often other measures than revenue are used as the tax basis for bank levies, such as (adjusted) balance sheet total. Also, levies are not reciprocal since they do not bring additional resources to the entity. It this situation the driver for the liability recognition should be the legal obligation arising in the year to which the levy officially relates.

In addition to the arguments mentioned in the EFRAG DCL we would like to highlight following:

- Levies are a highly political topic. The respective tax bases, such as (adjusted) balance sheet total, profit or revenue, and the tax rates are determined by the government to ensure sufficient funds for the budget. Levies are often industry specific. Compared to standard income taxes, this creates some more space for affected entities to enter the legislative procedures and negotiate the tax rates or continuation of the levies with the government. However, recognising a provision for a levy in an earlier period could undermine the position of entities in such negotiations. Governments could ask why entities should be worried about levies which have already been expensed. In this respect we note that in one jurisdiction where Erste Group operates for bank levies the tax base is calculated from the financial statements of the *second tax year* preceding the current tax year.
- As to the criticism of IFRIC 21 by some users mentioned in paragraph 7 of the EFRAG DCL we note that since its application started in 2014 we have never received feedback from our users regarding appropriateness of the IFRIC 21 treatment. IFRIC 21 has been incorporated in their models and the proposed change could potentially disrupt established practices.

As a result, we consider that the existing treatment of levies in IFRIC 21 is superior. We acknowledge that there are benefits in aligning the IAS 37 provision definition with the liability definition in the Conceptual Framework (CF). A solution should be found where the amended provision definition would also be aligned or coexist with the levies treatment as currently applied under IFRIC 21. In this regard, it may be necessary to revisit the requirement in paragraph 4.33 of the CF that an entity preparing its financial statements on a going concern basis has no practical ability to avoid a transfer (that could be avoided only by liquidating the entity or by ceasing to trade).

EFRAG - Question to Constituents

2.1 Although EFRAG assesses that the proposals related to the expenditure required to settle an obligation will result in useful information, it notes that performing an assessment of the internal cost (e.g., the cost of the internal legal department) related to settling obligation of the given type may be associated with uncertainty and cost.

Do you foresee any complexity/costly process in determining the costs that relate directly to settling the obligation(s) (which include both incremental costs and other directly attributable costs)? Please explain.

We consider that the inclusion of 'other costs that relate directly to settling obligations of that type' in paragraph 40A(b) of the ED would benefit from providing examples of such costs. This would assure a consistent approach in identifying appropriate 'other costs' amongst various types of IAS 37 provisions. If not, the change might trigger lengthy discussions with auditors with regards to finding a harmonised application especially in groups with complex international structure.

EFRAG - Questions to constituents

3.1 In cases when regulation describes the rate(s) to be used or determined to discount certain provisions within the scope of IAS 37, do you agree with the proposal to use a risk-free rate(s) or would you prefer to use the rate prescribed by the applicable regulation? Please explain.

3.2 Do you consider that the IASB should specify whether an entity should include or exclude inflation expectations when estimating the future expenditure required to settle its present obligation and then discounting this amount (see paragraph 52)? If so, please explain how the IASB could address the issue.

3.3 Would you expect that in practice, differences between how provisions acquired in a business combination would be accounted for at the day of acquisition and subsequently would result in day-2 losses being reporting in profit or loss (see paragraph 49(b) above)? If so, how would you recommend the issue to be solved?

We agree with the IASB proposal to use a risk-free rate with no adjustment for non-performance risk. We do not consider that additional gudiance would be necessary.