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EPSAS issue paper on the accounting treatment of taxes

Paper by Ernst & Young on behalf of Eurostat

- for discussion

Accounting treatment of taxes with a view to financial reporting requirements under the future European Public Sector Reporting Standards (EPSAS)

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1. Objectives of the Issue Paper

The aim of this paper is to develop an analysis of the accounting treatment of taxes with a view to financial reporting requirements under the future European Public Sector Accounting Standards (EPSAS).

This paper takes into account:

- ▶ The main categories of taxes in the European Union (EU);
- ▶ The approaches taken – including analysis of how these categories of taxes are accounted for – at an accounting standard level: International Public Sector Accounting Standards (IPSAS), European Accounting Rules (EAR), International Financial Reporting Standards (IFRS) and the European System of Accounts (ESA); and
- ▶ The approaches taken – including analysis of how these categories of taxes are accounted for – in five Member States (France, Latvia, Lithuania, Malta and the United Kingdom). In the PwC Report from 2014 France, Latvia, Lithuania and the United Kingdom were assessed as having a high accounting maturity.¹

The Issue Paper addresses the following questions that were raised by Eurostat:

- ▶ For which main categories of taxes do problematic points/issues with regards to recognition and measurement arise?
- ▶ Are the problematic points/issues with regards to recognition and measurement of tax satisfactorily treated in IPSAS?
- ▶ Which categories of taxes should be treated by future EPSAS standards or guidance taking into account materiality and comparability considerations?
- ▶ Would supplementary guidance on some aspects of the treatment of taxes be necessary and what would this look like?
- ▶ What would the consequences be for a possible convergence between EPSAS and ESA?
- ▶ What way forward is recommended on taxes and what would be a good approach for organising future discussions with the EPSAS stakeholders?
- ▶ Are there any implications that should be noted for other non-exchange revenues from the conclusions on taxes?

¹ See PwC, Collection of information related to the potential impact, including costs, of implementing accrual accounting in the public sector and technical analysis of the suitability of individual IPSAS standards, 2013/S 107-182395, 1 August 2014, p. 36 and 92.

2. Background

Given that taxes are the major source of revenue for many public administrations, the accounting for taxes is an essential element of public sector accounting. According to the PwC report from 2014 the most important sources of non-exchange revenue for (central) governments consist of VAT, corporate income tax and personal income tax.²

IPSAS 23, *Revenue from Non-exchange Transactions (Taxes and Transfers)*, prescribes requirements for the financial reporting of tax revenues under the accrual basis of accounting (see IPSAS 23.1 and 23.2).³ The public consultation on the assessment of the suitability of the IPSAS for the Member States stated the incompleteness of IPSASs with respect to public sector accounting requirements (e.g. with regard to taxation) as one of the main arguments against their implementation.⁴

With respect to recognition of tax revenues the empirical study by PwC in 2014 showed that on average 14 out of 28 central governments in Europe recognise revenue from taxes when cash is received, and about 9 out of 28 recognise it when taxes are declared (tax return; see the graph on the following page).⁵ Only very few central governments use the 'time adjusted cash' method in their own public sector accounting/financial reporting, or attribute the revenue to the taxation period, with asset recognition based on (year-end) estimates and the use of macro-economic indicators or historical trends/data. The following graph summarizes these findings:

² See PwC, Collection of information related to the potential impact, including costs, of implementing accrual accounting in the public sector and technical analysis of the suitability of individual IPSAS standards, 2013/S 107-182395, 1 August 2014, p. 109.

³ The ISPASB has an ongoing public sector specific project on revenue. This paper does not cover that ongoing project in detail, but draws some background material from it.]

⁴ See European Commission/Eurostat, Public consultation - Assessment of the suitability of the International Public Sector Accounting Standards for the Member States, Summary of Responses, Luxembourg, 18 December 2012, p. 5.

⁵ See PwC, Collection of information [...], p. 110.

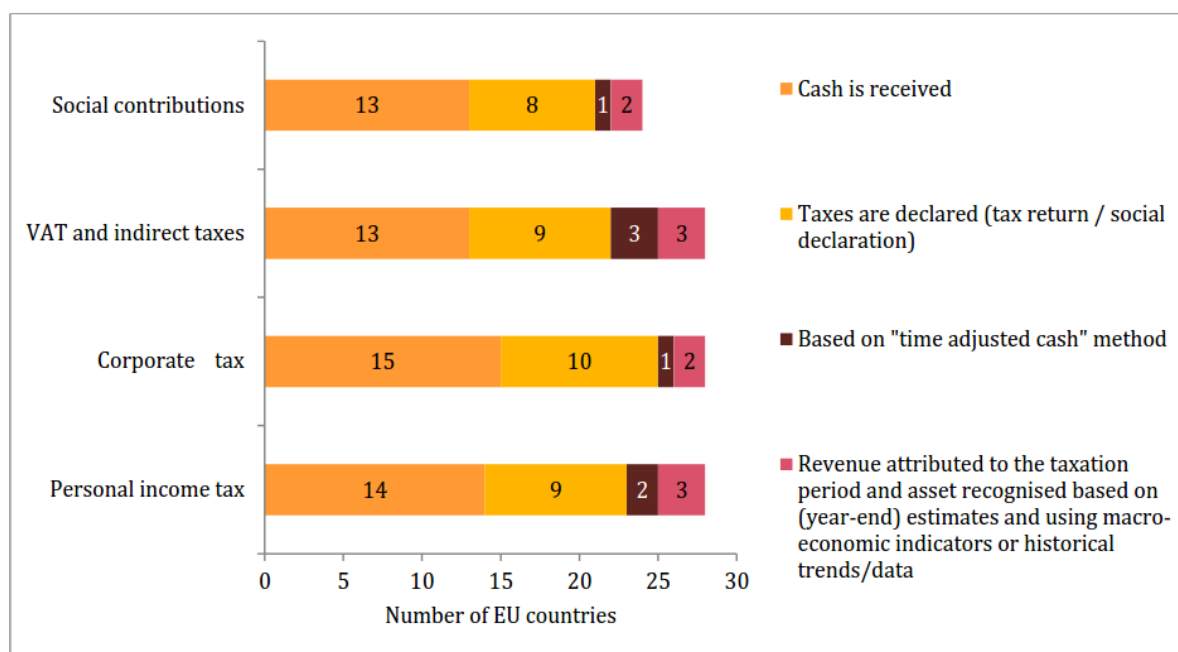


Figure 5: Timing of recognition of revenue from taxes⁶

Against the background of these practical issues it was recommended that the development of practical implementation guidance should be considered for the main sources of tax revenue for EU Member States (personal income tax, corporate income tax and VAT) to ensure consistent application in similar circumstances.⁷ The European Commission's report from 2013 concluded that "implementation [of EPSAS; added by authors] would be in steps over the medium term, focusing at first on the accounting issues where harmonisation is most important, such as revenue and expenditure (taxes and social benefits, liabilities and financial assets).

This Issue Paper will take stock of the issues raised.

⁶ See PwC, Collection of information [...], p. 110.

⁷ See *ibid*, p. 130 and 138.

3. Taxation in the European Union

Taxes are the most important source of non-exchange revenue for EU Member States. Each Member State communicates detailed statistical information on tax revenue to Eurostat on the basis of the European System of Accounts (ESA) 2010 transmission programme of data.⁸ The most recent tax data prepared on this basis and published by Eurostat relates to the 2014 tax revenues.⁹ For each Member State, it provides a breakdown of total tax revenue by category of taxes. The results of this aggregation are presented in the graph below and show the importance of each category of taxes as a percentage of total tax revenue in the EU for the year 2014.

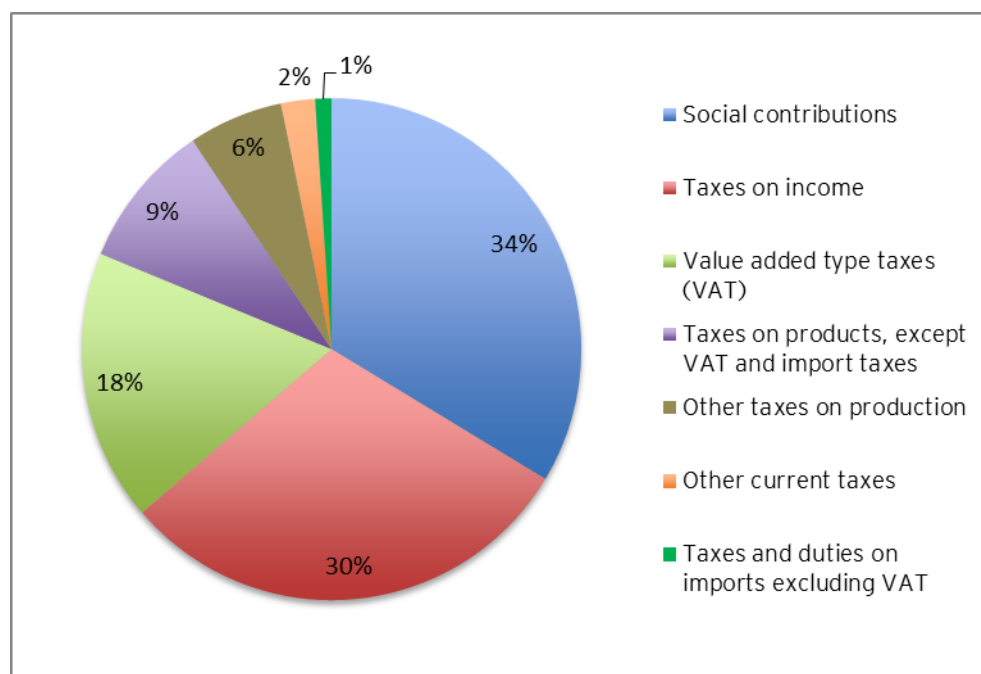


Figure 1: Categories of taxes as a percentage of total EU tax revenue in 2012

Based on the above figure it can be concluded that the main categories of taxes in the EU are social contributions (34%), followed by taxes on income (30%) and VAT (18%). Taken together, these three categories of taxes account for 82% of the total tax revenue in the EU.

⁸ See Eurostat, European System of Accounts (ESA) 2010 - Transmission programme of data, 2014, Table 9. 'Detailed tax and social contributions receipts by type and receiving subsector'. This statistical reporting is based on the codes and categories defined by the ESA 2010. The legal requirement for transmission of this data is 9 months after the end of the calendar year.

⁹ Based on the Tax revenue statistics as published on the website of Eurostat (http://ec.europa.eu/eurostat/statistics-explained/index.php/Tax_revenue_statistics).

The following chart combines the three main categories of taxes identified at an EU level and shows their importance at a Member State level as a percentage of total national tax revenue.

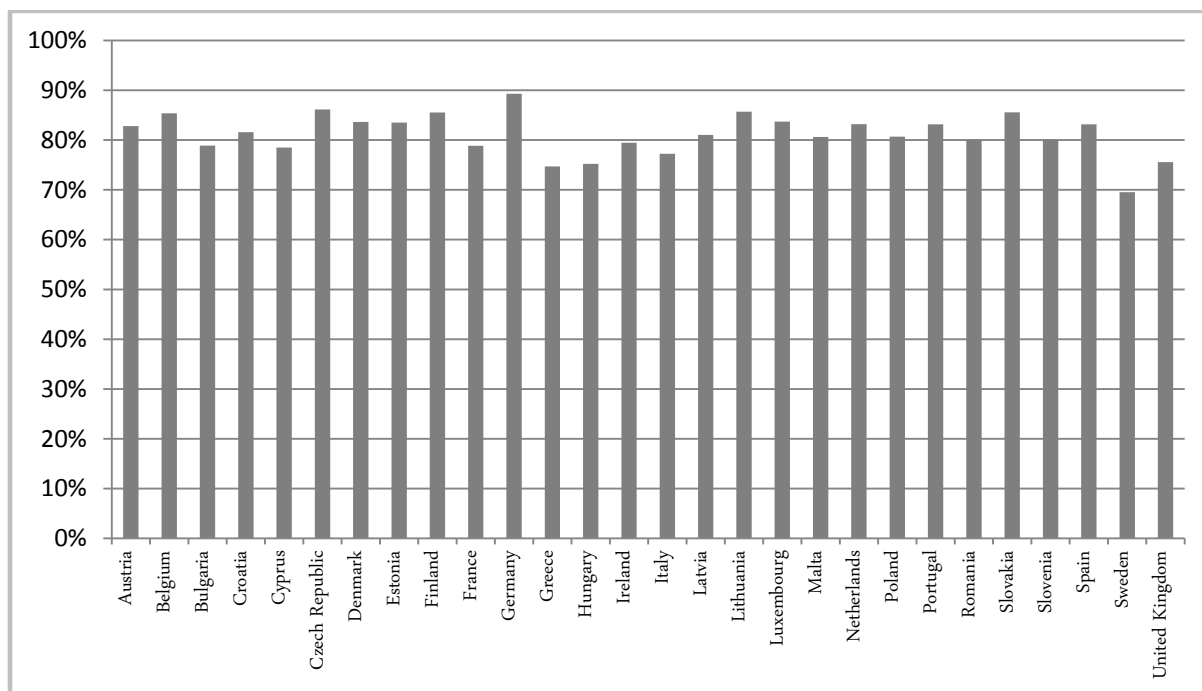


Figure 2: Combined share of the three main categories of taxes as a percentage of total national tax revenue per Member State in 2014

The three main categories of taxes (i.e. social contributions, taxes on income and VAT) account for 75% or more of total national tax revenue on a Member State level. This indicates that the three main categories of taxes account for the bulk of government tax revenue not only at an aggregated EU level but also at an individual Member State level. Annex 1 “EU tax revenues, breakdown by Member State and category of tax in 2014” provides an overview of tax revenue in the 28 Member States, including a breakdown of total tax revenue per category of tax.

The sections below focus on taxes on income and VAT and describe these two categories in more detail based on the definitions provided in the ESA 2010. Besides that, they analyse how these types of taxes are levied in the Member States and also identify whether European Regulations or Directives are in place, as this would suggest a certain level of harmonization between the Member States with regard to the levying and collection of these taxes.

Social contributions have been left out of the scope of the analysis. According to BC26 of IPSAS 23, IPSAS 23 does not exclude from its scope compulsory contributions to social security schemes that are non-exchange transactions. However, IPSAS 23 also states determining whether or not compulsory social contributions give rise to exchange or non-exchange transactions depends on the particular arrangements of a given scheme and requires professional judgement. As a consequence either IPSAS 23 applies or “principles established in international or national standards addressing such schemes.”¹⁰ Therefore, it

¹⁰ See BC26 of IPSAS 23.

depends on the characteristics of a social contributions scheme whether IPSAS 23 applies or not. It also has to be noted that social contributions are excluded from the scope of the IPSASB's new project on "Revenues".¹¹

3.1 Taxes on income

Taxes on income accounted for 30% of total EU tax revenue in 2014. This category is mainly composed of personal income taxes and corporate income taxes.

Taxes on income are covered under code D.51 in the ESA 2010 and are defined as taxes on incomes, profits and capital gains. They are assessed on the actual or presumed incomes of individuals, households, corporations or non-profit institutions (NPIs). This also includes taxes assessed on holdings of property, land or real estate where these holdings are used as a basis for estimating the income of their owners.

The levying of both the personal income taxes and the corporate income taxes is comparable in each Member State. In fact, the levying of these taxes typically follows the following sequence: (1) Taxable income is earned by the taxpayers during the taxation period (year N); (2) Tax "prepayments"¹² (e.g. PAYE¹³ tax) are made by taxpayers throughout year N; (3) Taxpayers file their tax return in year N+1. The tax returns include any tax credits or deductions that taxpayers are making use of in order to reduce their tax liability; (4) Government conducts its own assessment of the tax amounts due and sends the notification for final settlement to the taxpayer; (5) The final settlement takes place, resulting in either an additional payment by the taxpayer (where total prepayments amount to less than the final amounts due), or a tax refund by government (where total prepayments amount to more than the final amounts due).

¹¹ See Agenda Paper 6 of IPSASB Meeting from June 23-26, 2015 in Toronto, para. 111. The IPSASB's project on Social Benefits does consider social contributions, however only in the context of accounting for social insurance programs using the insurance approach.

¹² "Prepayments" also comprise payments by the taxpayer before the taxes are declared or assessed by government.

¹³ Pay-as-you-earn (abbreviation: PAYE).

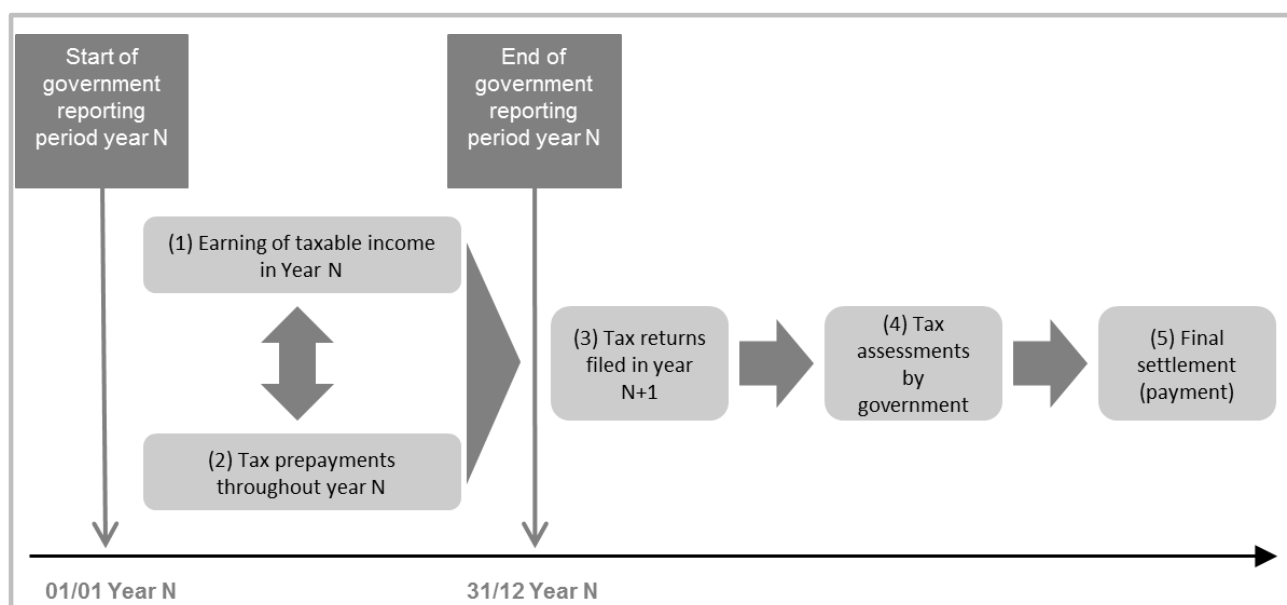


Figure 3: Flow chart of income tax levying

Annex 2 provides a comparison of the main features of the personal income tax systems across the 28 Member States. Annex 3 provides a similar comparison for the corporate income tax systems. The annexes have been prepared based on the 2015 edition of the Eurostat publication "Taxation trends in the European Union"¹⁴.

3.2 Value-added type taxes

VAT accounted for 18% of total EU tax revenue in 2014. These taxes are covered under code D.211 in the ESA 2010 and are defined as taxes on goods or services collected in stages by enterprises and which are ultimately charged in full to the final purchaser. The common feature of VAT is that producers are obliged to pay to the government only the difference between the VAT on their sales and the VAT on their purchases for intermediate consumption and gross fixed capital formation.

Through Council Directive 2006/112/EC¹⁵, a common system for VAT has been put in place in the EU. The levying of VAT in the European Union typically follows the following sequence: (1) VAT is paid at each stage of the production process, up to and including the sale of goods or services to the final consumer; (2) VAT that was paid by corporates on their own business purchases results in a VAT receivable for the corporations; (3) Each corporate is registered with the tax authorities in the EU country where the business is established and charges VAT to its customers; (4) VAT paid by the customers to a corporation and collected by the corporation results in a VAT payable by the corporation; (5) The accumulated amounts of VAT payable and VAT receivable are reported to the tax authorities in periodic VAT returns; (6) The final settlements take place on a periodic basis,

¹⁴ See Eurostat, Taxation trends in the European Union - Data for the EU Member States, Iceland and Norway, 2014 edition (http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2014/report.pdf).

¹⁵ Council Directive 2006/112/EC of 28 November 2006 on the common system of value-added tax (OJ L 347, 11 December 2006, p. 1-118).

resulting either in an additional VAT payment (where VAT payable exceeds VAT receivable) or in a VAT refund (where VAT receivable exceeds VAT payable).

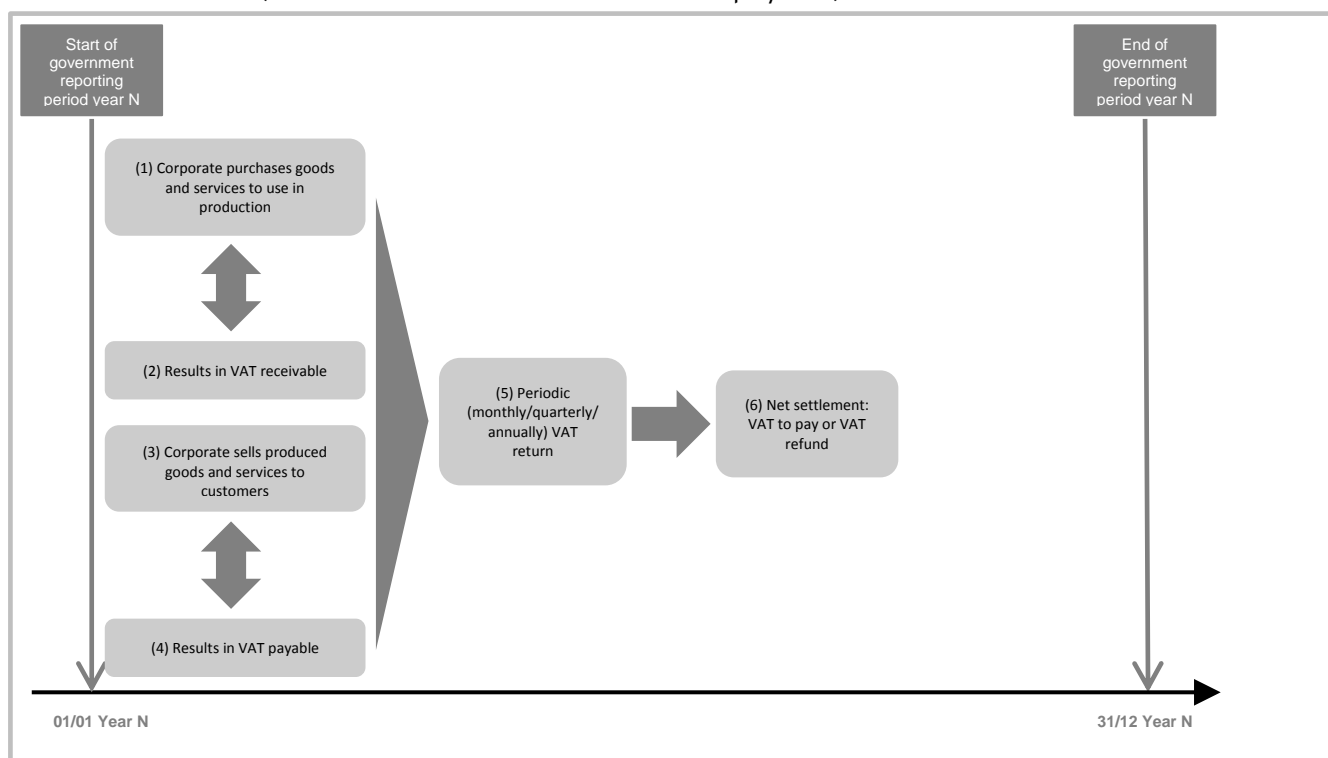


Figure 4: Flow chart of VAT levying

Annex 4 provides a comparison of the VAT rates across the 28 Member States. It has been prepared based on the 2015 edition of the Eurostat publication "Taxation trends in the European Union"¹⁶.

¹⁶ See Eurostat, Taxation trends in the European Union - Data for the EU Member States, Iceland and Norway, 2014 edition (http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2014/report.pdf).

4. Difficulties when accounting for taxes under the accrual principle

Under the accrual basis of accounting, transactions and other events are recorded in the financial statements when they occur, and not when payments are due or actually made. Hence, events that generate the tax claim/receivable (or similar) should be recorded when the activities, transactions or other events that generate the liability to pay taxes take place, i.e. when the taxable event¹⁷ occurs.¹⁸ From an accounting point of view, one of the main difficulty arises from the fact that the final amount of taxes due (the final settlement) will usually only be known after the end of the annual reporting period during which the taxable event occurred. Therefore, when taxes are recognized based on the taxable event, there is a risk of over-recording tax revenues. Another problem in that context is that for governments, recording revenue and claims at the time of the underlying event can be particularly difficult, since often government records for taxes are on a cash basis.¹⁹

In the following, the inherent revenue recognition difficulties will be illustrated for taxes on income and VAT.

4.1 Difficulties regarding the timing of tax revenue recognition for taxes on income

According to ESA 2010 income taxes comprise a) taxes on individual or household income, b) taxes on the income or profits of corporations, c) taxes on holding gains and d) taxes on winnings from lotteries or gambling, payable on the amounts received by winners.²⁰

Taxes on individual or household income consist of personal income taxes, including those deducted by employers (pay-as-you-earn taxes, so-called PAYE-taxes) and surtaxes. Such taxes are usually levied on the total declared or presumed income from all sources of the person concerned: compensation of employees, property income (e.g., interest, dividends, rent, royalty incomes), and pensions (taxable portions of social security, pension, annuity, life insurance, and other retirement benefit distributions), etc., after deducting certain allowances in accordance with tax laws. Taxes on the income of the owners of unincorporated enterprises also fall under that category.

Taxes on the income of corporations consist of corporate income taxes, corporate profits taxes, corporate surtaxes, etc. Such taxes are usually assessed on the total incomes of corporations. This covers income from all sources and not simply profits generated by production.

Some of the above mentioned sub-types of income taxes are less complex (e.g. PAYE-taxes), whereas some of them are more complex (e.g. interest income, rent or pensions). Therefore, the complexity of revenue recognition for income taxes varies dependent on the sub-type of income taxes.

¹⁷ The taxable event is the event that the government, legislature or other authority has determined will be subject to taxation (see IPSAS 23.7).

¹⁸ See IMF, GFS Manual 2014, para. 5.10.

¹⁹ See ESA 2010, para. 20.172.

²⁰ See ESA 2010, para. 20.174.

According to IPSAS 23.65 the taxable event for income taxes is the earning of assessable income during the taxation period by the taxpayer. As a result, according to the accrual principle, income taxes should be attributed to the period in which the income is earned, even though there may be a significant delay between the end of the reporting period and the time at which it is feasible to determine the actual liability of the taxpayer.

The main difficulty when accounting for income taxes under the IPSAS accrual accounting principles stems from the fact that even though the final amounts of taxes due are not yet known at the end of the reporting period, the related tax revenue needs to be recorded in accordance with the occurrence of the taxable event, even if this involves uncertainty and - as a consequence - corrections (after balance sheet date) of the revenue recorded.²¹ Since the final amounts of taxes due are not yet known (with certainty) at the end of the reporting period, they will need to be estimated in order to determine the amount of tax revenue to record in the financial statements. This estimate must be reliable²², otherwise the recognition criteria will not be met and no revenue will be recognized.

The difficulty of making a reliable estimate depends on the timing of the filing of the tax returns and the timing of the government's tax assessment. For example, in those cases where tax returns are available to the government or where government performs the tax assessments before the financial statements are authorized for issue²³, the information these contain can be used in the preparation of the financial statements. This means that the tax returns or assessments are made in time to serve as a basis for estimating the final amounts of taxes due in accordance with the accrual principle.

The following figure provides an illustrative example of a situation where the tax return is filed before the authorization date of the financial statements:

²¹ Such corrections are typically accounted for as changes in accounting estimates in subsequent periods. As a consequence financial statements need to be adjusted only prospectively.

²² The terms "reliable" and "reliability" are used in this paper in the meaning of "faithful representation" as outlined in IPSASB's Conceptual Framework.

²³ The date of authorization for issue is the date on which the financial statements have received approval from the individual or body with the authority to finalize those statements for issue. According to IPSAS 14.8, the date of authorization for issue of the financial statements is jurisdiction-specific.

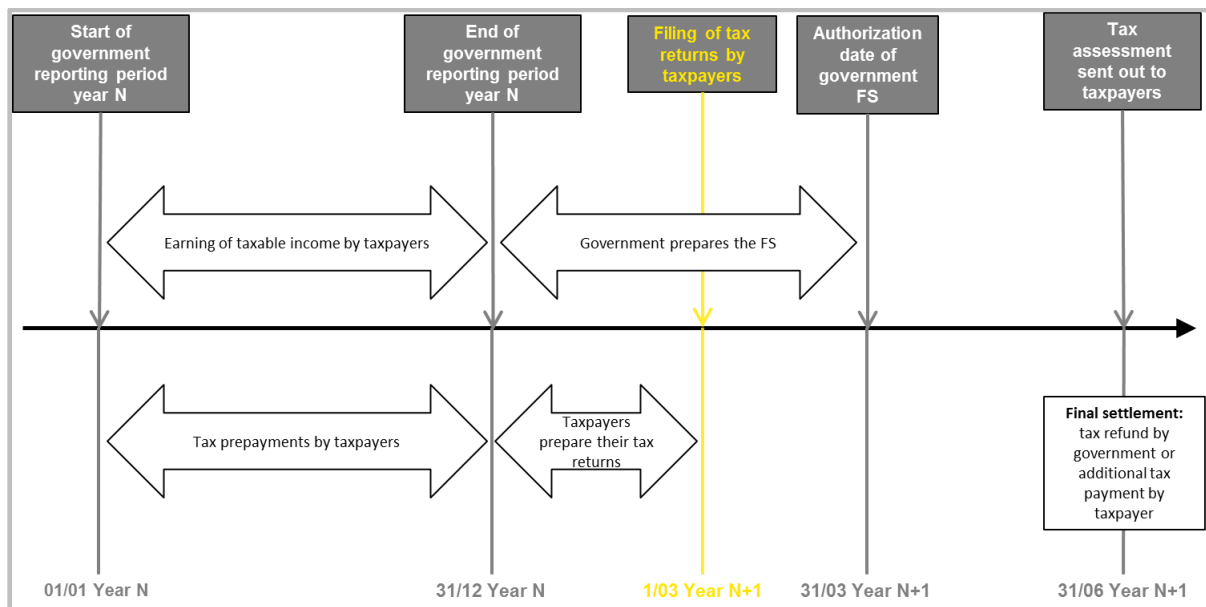


Figure 5: Income tax returns filed before the government financial statements (FS) are authorized for issue

In situations like that, government can already make an estimate based on the income declared by the taxpayer. In contrast, where tax returns and assessments are only obtained after the authorization date of the financial statements, they arrive too late to be considered in the preparation of the financial statements. In these cases, the tax returns and assessments cannot be used as a basis for estimating the final amounts of taxes due.

The following figure provides an illustrative example of a situation where the tax return is filed after the authorization date of the financial statements:

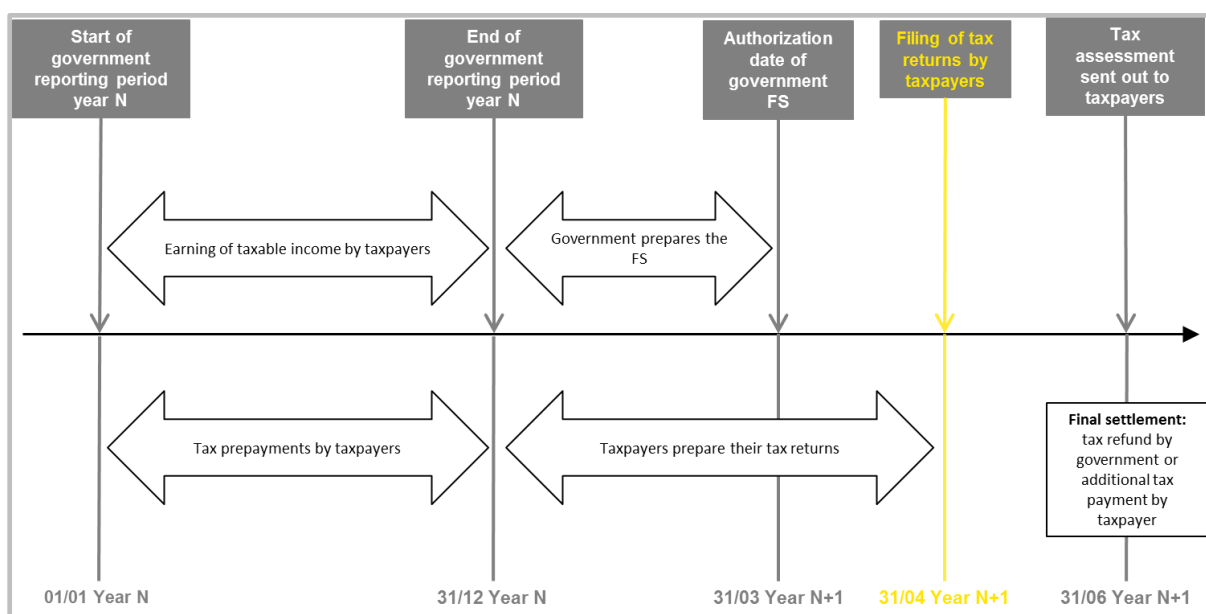


Figure 6: Income tax returns filed after the government financial statements (FS) are authorized for issue

The principal difficulty when accounting for income taxes under the accrual principle stems from the timing difference between, on the one hand, the authorization date of the government financial statements and, on the other hand, the filing of the tax returns by the taxpayers. In fact, governments usually rely on the tax returns in order to assess the total amounts of taxes due for the period and the related tax relief in the form of tax credits or deductions. The timing difference implies that, at the moment of preparing the financial statements, the government has not yet received detailed information contained in the tax returns. As a consequence, it will be more difficult for the government to determine whether the revenue recognition criteria under IPSAS 23 are met at the end of the reporting period. Next to that, revenue measurement will be complex because estimates will need to be made without any input from tax returns.

Tax expenditures, i.e. tax incentives provided by government, or expenses paid through the tax system are a further problem area with respect to the revenue recognition of income tax revenue. IPSAS 23 distinguishes between two different concepts, namely 'Expenses paid through the tax system' on the one hand and 'Tax expenditures' on the other hand, and requires different accounting treatments for both.

Expenses paid through the tax system	Tax expenditure
Sometimes governments use the tax system to provide benefits to taxpayers that would otherwise be paid using another payment method. For example, a government may pay part of a resident's health insurance premiums to encourage the uptake of such insurance, either by reducing the taxpayer's tax liability or by directly making a payment to the insurance company. In these cases, the amount is payable to recipients irrespective of whether they pay taxes. Therefore, this amount represents an expense of government also in the case when the government reduces the taxpayer's liability through the tax system and should be recognized as such in the statement of financial performance, i.e. to recognize an expense and to increase tax revenue for that amount.	Sometimes governments use the tax system to encourage certain behaviour. This is for example the case when government permits homeowners to deduct mortgage interest from their gross income when calculating their tax assessable income. Since this kind of deductions is only available to tax payers, it is to be treated as foregone revenue. Consequently, tax expenditures do not give rise to assets, liabilities, revenue or expenses of government under IPSAS.

Expenses paid through the tax system are recorded as expenses under IPSAS, whereas tax expenditures are set off and therefore not transparently visible.

Governments often use the tax system to encourage certain economic behaviour and discourage other behaviour. From an accounting perspective tax expenditures are foregone revenue and not expenses. They do not give rise to inflows or outflows of resources.

In some jurisdictions, the government uses the tax system as a method of paying to taxpayers benefits that would otherwise be paid using another payment method (e.g. directly depositing the amount in a taxpayer's bank account). In these cases, the amount is payable irrespective of whether the individual pays taxes. IPSAS 23.71 requires that taxation revenue shall not be reduced for such expenses paid through the tax system. As a consequence IPSAS 23 requires to account for expenses paid through the tax system as

two separate transactions, i.e. tax revenue recognition through the settlement of the tax liability by the taxpayer and the payment by the government. Taxation revenue should therefore be increased for the amount of any of these expenses paid through the tax system.

The actual use of tax expenditures or claims made by taxpayers with regard to expenses paid through the tax system can only be determined when tax declarations were assessed by the tax authorities. Therefore, the calculation of income tax revenue using statistical models might have some insecurity factors with regards to the use of tax expenditures by taxpayers or claims made by taxpayers with regard to expenses paid through the tax system.

4.2 Difficulties regarding the timing of tax revenue recognition for value-added type taxes

According to IPSAS 23.65 (b) the taxable event for VAT is the undertaking of taxable activity during the taxation period by the taxpayer.

In the case of VAT, returns are filed, and the corresponding amounts collected, throughout the year with sufficient periodicity for government to know the major part of VAT revenues with certainty by the end of the reporting period. Accounting for revenue from VAT will therefore be less complex than for revenue from income taxes. Difficulties are expected in relation to those VAT returns that are obtained after the authorization date of the financial statements (if any).

The following figure provides an illustrative example of a situation where VAT returns are filed on a quarterly basis, with the last return for the year arriving before the authorization date:

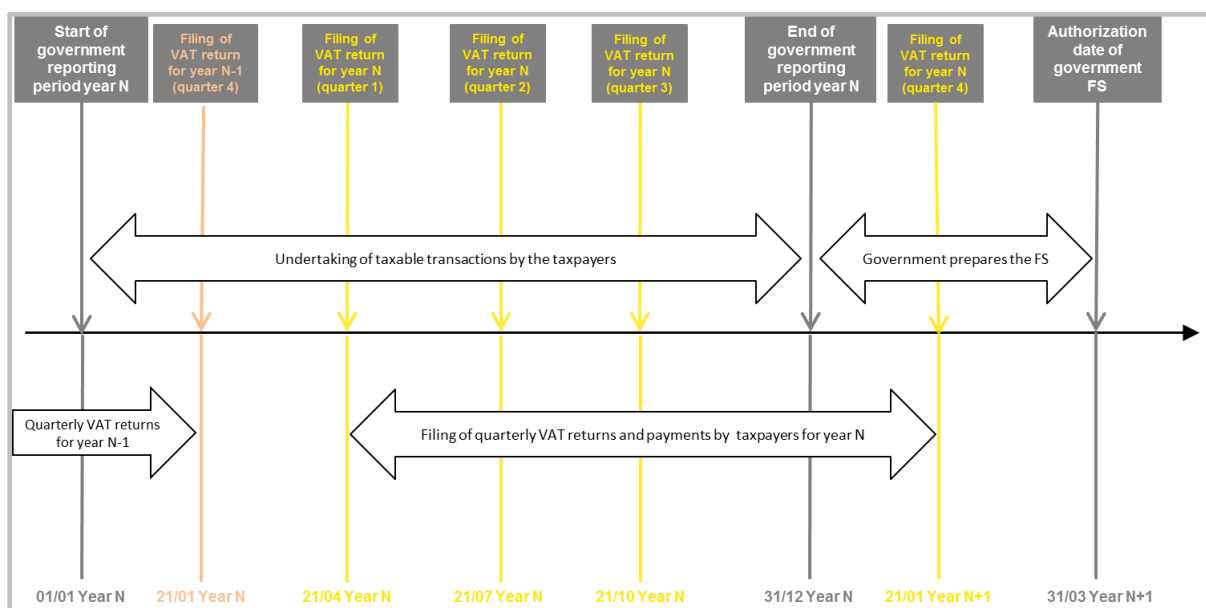


Figure 7: All VAT returns filed before the government financial statements (FS) are authorized for issue

Cross border transactions within the EU but also with non-EU countries are a further complexity with regard to the revenue recognition of tax revenue from VAT. In recent years

also the missing trader fraud (also known as carousel fraud) has caused significant problems with the revenue recognition of VAT by Member States.

4.3 Approaches used for the revenue recognition of taxes

For the recognition of tax revenues the following three main approaches can be identified:

1. **The taxable event approach:** The underlying approach for tax recognition of IPSAS 23 is the taxable event approach. IPSAS 23 refers for the revenue recognition of taxes to the recognition of the related asset, i.e. the tax receivable. IPSAS 23.59 requires that an asset should be recognized in respect of taxes when (a) the taxable event occurs and (b) when the asset recognition criteria are met. IPSAS 23.60 clarifies that resources arising from taxes satisfy the definition of an asset when the entity controls the resources as a result of a past event (the taxable event) and expects to receive future economic benefits or service potential from those resources. The identification of the taxable event for a certain category of taxes is therefore one crucial part for the recognition of tax revenue. IPSAS 23.60 then outlines that “resources arising from taxes satisfy the criteria for recognition as an asset when it is probable that the inflow of resources will occur and their fair value can be reliably measured.” According to IPSAS 23.60 the degree of probability attached to the inflow of resources is determined on the basis of evidence available at the time of initial recognition. This includes, but is not limited to, disclosure of the taxable event by the taxpayer. IPSAS 23.68 adds that where there is a separation between the timing of the taxable event and collection of taxes due, an entity may reliably measure assets arising from taxation transactions by using, for example, statistical models based on the history of collecting the particular tax in prior periods. Under the taxable event approach prepayments of taxes would be recognized as revenue in the period when the prepayments are received.
2. **The tax assessment approach:** As outline before, the time lag between when the taxable event occurs and the point in time when the final tax amount due is determined impairs a reliable measurement of tax revenues. Therefore, under the tax assessment approach the point in time when the tax authorities have made their tax assessment and have issued a tax assessment to the taxpayer is used for recognizing tax revenues. The main advantage of that method is that only such tax revenues will be shown in the financial statements that have already been subject to an assessment and therefore have a higher certainty of existence. It has to be noted that under the tax assessment approach it is possible that prepayments of taxes are recognized as revenue when cash from prepayments is received. These prepayments will be considered when taxes are assessed. Therefore, under the tax assessment approach taxes might not only be recognized when they are “due and payable”. According to ESA 2010, using the tax assessment approach is acceptable (though not the ideal approach, given the risk of over-recording) to determine the point in time for recording tax revenue.²⁴ Given that taxpayers often have the right to object to a tax assessment issued by tax authorities the tax assessment approach might also lead to adjustments of tax revenue in subsequent periods. A different approach compared to the tax assessment approach is the tax declaration approach. Under the tax declaration approach taxes are generally recognized when

²⁴ See ESA 2010, para. 20.175.

the entity receives the tax declaration by the taxpayers. Therefore, compared to the tax assessment approach, tax revenues are recognized earlier under the tax declaration approach. In cases where the differences between what has been declared by a taxpayer and what has been assessed by the tax authority are low the tax assessment approach and the tax declaration approach can lead to similar results in terms of revenue recognition of taxes. With regards to revenue recognition of tax prepayments two different approaches are in principle possible under the tax declaration as well as the tax assessment approach. Tax revenues from tax prepayments can either be recognized when the tax prepayments are received or they can be recognized only when the tax declaration is received or the tax assessment is performed. For example in France revenue from income taxes are only recognized when the tax declaration is received (see Chapter 5.2).

3. **The time-adjusted cash method:** According to the time-adjusted cash method tax revenue is calculated based on cash received from taxpayers. Where appropriate, time-adjustments are made so that tax payments are attributed to the period when the activity generating the liability took place. The MGDD provides the following example:²⁵ If there is a 1-2 month lag between VAT being accrued and it being paid by corporations to the tax authorities, then the cash received in the first 1-2 months of the year will be allocated to the previous year. Under ESA 2010 the time-adjusted cash method is considered as an acceptable proxy for accruals.²⁶ The time-adjusted cash approach is used when there are some difficulties to make reliable estimations for amounts unlikely to be collected or when there are no reliable assessments available.²⁷ Under the time-adjusted cash method prepayment of taxes are recognized when the cash is received by the tax authorities.

4.4 Further difficulties and problems identified for the accounting of taxes under IPSAS 23

The following difficulties and problems related to the revenue recognition and measurement of taxes under IPSAS 23 were identified by EY:²⁸

- ▶ IPSAS 23 does not provide guidance as to how the principles should be applied in practice.²⁹ Feedback by the Member States indicated that the guidance provided in IPSAS 23 is not detailed enough for a practical application of the standard. For example, the guidance provided by IPSAS 23 does not contain any parameters for developing and implementing such models. Also the application guidance of IPSAS 23 only mentions that econometricians should be involved when developing the model and that it should afterwards be validated by an external auditor.
- ▶ It was reported by Member States that for some categories of taxes the taxable event approach in IPSAS 23 can hardly be applied in practice. Especially entities

²⁵ See Eurostat, Manual on Government Deficit and Debt, Implementation of ESA 2010, 2016 edition, p. 87.

²⁶ See ESA 2010, para. 20.174.

²⁷ See Eurostat, Manual on Government Deficit and Debt, Implementation of ESA 2010, 2016 edition, p. 87.

²⁸ Different sources were used to compile the various difficulties and problems. Inter alia the results of the interviews conducted with IPSASB's constituents regarding the specific issues that need to be addressed in IPSASB's project on non-exchange revenues and expenses were used (see Agenda Item 8 on 'Revenue and Non-exchange Expenses' of IPSASB's December 2015 Meeting). But also work done by Eurostat was used.

²⁹ See PwC, Collection of information [...], p. 130.

using cash-based methods reported problems with applying the taxable event approach based on statistical models.³⁰ Many Member States currently apply the time-adjusted or just the cash method for the recognition of tax revenue (see Chapter 2). Especially for taxes where the time lag between the taxable event and the collection of taxes is large, cash-based methods are not able to fulfil the taxable event requirement of IPSAS 23.

- ▶ Given the fact that IPSAS 23 recommends the use of statistical models for revenue recognition purposes, in some cases, making a reliable estimate based on statistical models might not be possible. Next to the volatility of the tax base caused by the economic cycle also other factors (than the economic cycle) might impact the tax base (e.g. the taxation or non-taxation of specific economic transactions, like capital gains or stock-options). Also issues caused by the tax burden of corporates that are in the position to reduce their taxes significantly or even change their place of business for tax purposes which means a complete shortfall of tax revenues can affect the tax base and make statistical models less robust. These factors can have an effect on the tax base independent from the economic development. A further issue that needs to be considered is the quality and reliability of data used for the statistical models. There might be cases where the data necessary for the statistical models is not available in the necessary quality and/or granularity.³¹ A practical issue with the use of statistical models that EY sees is the determination of the collectability of taxes, i.e. the probability of completely collecting what is due. This issue occurs at initial measurement of the tax receivables, but also in subsequent periods when it comes to the possible impairment of tax receivables. The probability of tax collection might differ from Member State to Member State.³² Furthermore, there can be differences between different types of taxes. The characteristics of the various taxpayers (private persons, companies) need to be considered in respect of the different applicable tax regimes (corporate tax, death duties, personal income tax, property taxes, VAT, etc.) in order to determine the taxable event and corresponding tax revenue in accordance with IPSAS.³³ Given the size of the different groups of taxpayers, this requires the gathering of an extensive set of data for feeding into the statistical models.
- ▶ Preparers have raised the issue that revenue recognition according to IPSAS 23 is difficult to understand because the criteria for recognition of tax revenue are defined based on elements of the statement of financial position and only indirectly for the statement of financial performance.³⁴ Member States that currently apply different recognition approaches (e.g. recognizing tax revenue based on revenue criteria) would have to change their approach if the recognition principles of IPSAS 23 would apply. In the context of the European budgetary surveillance government deficit – a flow variable – is used as the central indicator.
- ▶ IPSAS 23.60 requires for the recognition of a tax receivable that “resources arising from taxes satisfy the definition of an asset when the entity controls the resources as a result of a past event...”. Standard-setters therefore question whether for certain categories of taxes (e.g. income taxes) the taxable event is the appropriate point in time when an entity controls the resources.

³⁰ See Commission Staff Working Document, Brussels, 6 March 2013, p. 114.

³¹ See *ibid*, p. 130.

³² See also Agenda Item 8.1 Issues Paper, Revenue and Non-exchange Expenses, Interviews of preparers, IPSASB December 2015 Meeting, p. 4.

³³ See PwC, Collection of information [...], p. 34.

³⁴ See Commission Staff Working Document, Brussels, 6 March 2013, p. 114.

- ▶ With regards to the presentation of tax receivables, EY experienced that in practice it is discussed whether tax receivables should be presented gross or net.
- ▶ Depending on the applicable tax regime, a high degree of complexity (e.g. caused by tax exemptions) may be involved in the calculation/estimation of tax revenue.³⁵ In the Commission Staff Working Document from 2013 it was reported that producing reliable estimates of total tax due and sometimes also of the likely level of bad debts are considered as areas where many governments face significant practical difficulties.³⁶ Given that for some taxes there is a significant time gap between the occurrence of the taxable event and the assessment of the taxes declared, year-end estimates based on statistical modelling are necessary to calculate the year-end tax revenue accrual.³⁷ It was also reported that there are difficulties to assess impairments on receivables reliably.³⁸ Given these measurement difficulties it was stated that in some cases tax revenue may need to be recognised when cash is received.³⁹
- ▶ Difficulties were also identified by an IPSASB assessment of IPSAS 23. According to the IPSASB's assessment there might be conflicts between regulations under national tax legislation on one side and accounting requirements under IPSAS on the other side (e.g. when the taxable event has taken place but the tax law permits taxpayers to defer payment then the question arises whether government controls the assets and revenues could be recognized).⁴⁰
- ▶ For the recognition of revenue from taxes, data from various government IT systems will need to be received on a different basis.⁴¹ What also can be observed in practice is an insufficient information flow from the tax administration to the entity in charge for financial reporting. This is considered to be problematic for a centralized approach of reporting for tax revenues. In this context, IT implementation issues are perceived as relevant due to the greater complexity of record keeping.⁴²
- ▶ The IPSASB's assessment of IPSAS 23 also showed that the accounting treatment of tax incentives is considered to be problematic.⁴³
- ▶ Finally, tax specific issues such as amnesties, tax rebates, unrecoverable tax credits, related fines and penalties are also considered as problematic in terms of revenue recognition of taxes and how to consider them in the different approaches for revenue recognition.

³⁵ See *ibid*, p. 34.

³⁶ See *ibid*, p. 109.

³⁷ See *ibid*, p. 110.

³⁸ See *ibid*, p. 130.

³⁹ See *ibid*, p. 130.

⁴⁰ See Agenda Item 8.1 Issues Paper, Revenue and Non-exchange Expenses, [...], p. 4.

⁴¹ See *ibid*, p. 10.

⁴² See Commission Staff Working Document, Brussels, 6 March 2013, p. 114.

⁴³ See Agenda Item 8.1 Issues Paper, Revenue and Non-exchange Expenses, [...], p. 4.

5. Description of accounting guidance available

5.1 International accounting frameworks

The following sections analyse the guidance on taxes that is contained in the international accounting frameworks and, in particular, how these frameworks treat the difficulties identified under section 4.

5.1.1 International Public Sector Accounting Standards (IPSAS)

IPSAS 23, Revenue from non-exchange transactions (taxes and transfers) prescribes the accounting treatment of revenue from non-exchange transactions⁴⁴, such as taxes and transfers. The appropriate accounting treatment of taxes under IPSAS depends on the applicable tax legislation (see IPSAS 23.65). This section focuses on the accounting treatment of revenue from taxes.

5.1.1.1 Recognition

IPSAS 23 refers for the revenue recognition of taxes to the recognition of the related asset, i.e. the tax receivable. IPSAS 23.59 requires that an asset should be recognized in respect of taxes when (a) the taxable event occurs and (b) when the asset recognition criteria are met.

IPSAS 23.65 outlines that the reporting entity has to analyse the respective taxation laws to determine the taxable event. Unless otherwise specified in laws or regulations, IPSAS 23.65 (a) considers for income taxes “the earning of assessable income during the taxation period by the taxpayer” as the taxable event. For value-added tax “the undertaking of taxable activity during the taxation period by the taxpayer” is considered to be the taxable event (IPSAS 23.65 (b)).

IPSAS 23.60 clarifies that resources arising from taxes satisfy the definition of an asset when the entity controls the resources as a result of a past event (the taxable event) and expects to receive future economic benefits or service potential from those resources. The requirement of a “past event” for the revenue recognition of taxes relates to the taxable event. As a consequence, tax revenue cannot be recognized according to IPSAS 23 until the taxable event has taken place. The identification of the taxable event for a certain category of taxes is therefore one crucial part for the recognition of tax revenue.

Given the fact that next to statistical models there are other methods for recognizing tax revenue based on the taxable event approach the following table illustrates the relationship between the taxable event requirement and the different methods for recognizing tax revenue:

⁴⁴ IPSAS 23.7 defines non-exchange transaction as transactions in which an entity either receives value from another entity without directly giving approximately equal value in exchange, or gives value to another entity without directly receiving approximately equal value in exchange. According to IPSAS 23.63, taxes satisfy the definition of “non-exchange transaction” because the taxpayer transfers resources to the government, without receiving approximately equal value directly in exchange.

Requirement	Recognition of tax revenue based on the taxable event (“taxable event approach”)		
Methods (approaches/models)	Statistical model (IPSAS 23)	Tax declaration/ tax assessment approach	Time-adjusted cash method

IPSAS 23.60 also makes clear that tax revenue can only be recognized when an entity controls the respective resources. According to para. 5.11 of the IPSASB’s Conceptual Framework “control of the resource entails the ability of the entity to use the resource [...] so as to derive the benefit of the service potential or economic benefits embodied in the resource in the achievement of its service delivery or other objectives.” Par. 5.12 states that in the assessment whether an entity presently controls a resource, the following indicators of control are taken into account: a) Legal ownership; b) Access to the resource; c) The means to ensure that the resource is used to achieve its objectives; and d) The existence of an enforceable right to service potential or the ability to generate economic benefits arising from a resource. Despite the fact that para. 5.12 of IPSASB’s Conceptual Framework outlines that these indicators are not conclusive determinants of whether control exists” it can be questioned in the context of a tax receivable whether an entity controls these resources. It can for example be argued that control of the tax resources cannot be realized until the taxes are assessed and the tax assessment is sent to the taxpayer. Only in that point in time the tax receivable would become enforceable. Therefore, from a control perspective also the point in time when the tax authorities receive the tax declaration from the tax payer might be too early to recognize tax revenue.⁴⁵ At the latest when the taxpayer pays the taxes and the tax authority receives cash, tax revenue needs to be recognized. Also when a tax payer pays PAYE tax, such cash flows needs to be recognized as tax revenue in the period when they are paid.

IPSAS 23.60 then outlines that “resources arising from taxes satisfy the criteria for recognition as an asset when it is probable that the inflow of resources will occur and their fair value can be reliably measured.” According to IPSAS 23.60 the degree of probability attached to the inflow of resources is determined on the basis of evidence available at the time of initial recognition. This includes, but is not limited to, disclosure of the taxable event by the taxpayer. In addition to the probability requirements the recognition of tax revenue is dependent on a reliable measurement of the inflow of resources.

In some cases, the assets arising from taxation transactions and the related revenue cannot be reliably measured until some time after the taxable event occurs. This may for example be when a tax base is volatile and reliable estimation therefore not possible. Hence, the recognition criteria are not met at the moment the taxable event occurs and therefore no tax receivable and revenue can be recognized. IPSAS 23.70 indicates that in such cases, the assets and the related revenue may be recognized in periods subsequent to the occurrence of the taxable event. In the case of personal income tax for example, PAYE-taxes would therefore be recognized in the period when they are provided to the tax authorities, however the difference between the taxes paid based on the PAYE-taxes and the final tax amount would only be recognized in the period when the final tax amount could be reliably measured.

⁴⁵ As outlined in Chapter 4.3 only when the differences of the tax results between what has been declared by taxpayer and what has been assessed by the tax authority are low, the tax assessment approach and the tax declaration approach can lead to similar results. If this is the case control can probably already be assumed when tax declarations are received.

5.1.1.2 Measurement

IPSAS 23.67 requires assets arising from taxation to be measured at the best estimate of the inflow of resources to government. In this regard, IPSAS 23.68 states that where there is a separation between the timing of the taxable event and collection of taxes, government may reliably measure assets arising from taxation transactions by using statistical models based on the history of collecting the particular tax in prior periods. These models should take into account the timing of cash receipts from taxpayers, declarations made by taxpayers and the relationship between taxation receivable and other events in the economy. In addition, such a model should take into consideration factors such as:

- ▶ The tax law allowing taxpayers a longer period to file returns than the government is permitted for publishing general purpose financial statements;
- ▶ Taxpayers failing to file returns on a timely basis;
- ▶ Valuing non-monetary assets for tax assessment purposes;
- ▶ Complexities in tax law requiring extended periods for assessing taxes due from certain taxpayers;
- ▶ The potential that the financial and political costs of rigorously enforcing the tax laws and collecting all the taxes legally due to the government may outweigh the benefits received;
- ▶ The tax law permitting taxpayers to defer payment of some taxes; and
- ▶ A variety of circumstances particular to individual taxes and jurisdictions.

One consequence of recording tax receivables and revenue based on a statistical model is that estimations will usually differ from the actual amounts determined in subsequent periods when government makes its tax assessment. Depending on the type of tax and circumstances these differences can be significant and systematic. As outlined earlier this could be the case when the forecast of the economic development is difficult. Also inspections by tax authorities in subsequent periods can lead to considerable changes between the estimations and the tax amount after the inspection (e.g. in the area of VAT). According to IPSAS 23.60, such differences should be recognized in surplus or deficit in the period of change, meaning in the reporting period in which they are identified. This is usually the period following the one in which the taxable event occurred. These changes are considered as changes in accounting estimates according to IPSAS 3 and therefore are reflected prospectively in the financial statements.

Where tax payments have already been received during the period of the taxable event (e.g. by prepayments), for accrual accounting purposes only the difference between those amounts and the amounts determined by using statistical models need to be identified. Depending on the difference this can either be an asset (a tax receivable) or a liability (a tax payable). For taxes where prepayments need to be made by the taxpayers (e.g. in the case of income taxes) or where taxes are received within a short time period after the taxable event takes place (e.g. VAT), a considerable portion of the tax revenue of an accounting period is actually determined before the closing of the books in an accounting period. Statistical models used for the determination of tax revenue for an accounting period can therefore be informed and improved by the amount of taxes already received by the tax authorities. In some cases statistical models might not even be needed, as the uncertain remaining portion is quite insignificant. The quality of the outcomes of such statistical models is therefore better than the statistical models used for forecasting tax revenues.

Also the economic development during an accounting period is already known by year-end (or soon after) and can therefore also further inform the statistical models.

For the accounting of tax expenditures or expenses paid through the tax system under IPSAS 23 please see Chapter 4.2.1.

5.1.2 European Union Accounting Rules (EAR)

Revenue from non-exchange transactions is treated under *EAR 17 - Revenue from non-exchange transactions (taxes and transfers)* which is based on IPSAS 23. Similarly to IPSAS 23, the approach prescribed by EAR 17 is based on the taxable event. However, in line with IPSAS 23, EAR 17 does not provide additional practical guidance on how to deal with the difficulties that arise when applying the taxable event approach as prescribed by IPSAS 23.

5.1.3 International Financial Reporting Standards (IFRS)

Under IFRS, two standards are dealing with taxes: IAS 12 - *Income taxes* and IFRIC 21 - *Levies*. However, they deal with taxes from the point of view of the taxpayer and therefore do not provide any additional information with regard to how governments should account for taxes from a tax collector point of view. As regards the IFRS standard on revenue, IAS 18 - *Revenue*, it covers the accounting treatment of revenue arising from the sale of goods, sale of services and the use by others of entity assets yielding interest, royalties and dividends. It does not apply to revenue from non-exchange transactions and is therefore of limited use for the purposes of this analysis.

5.1.4 ESA 2010

The ESA 2010 prescribes rules for the recording of tax revenue in the national accounts. Taxes are defined as “compulsory unrequited payments, in cash or in kind, made by institutional units to general government or supranational bodies exercising their sovereign or other powers”.⁴⁶ Taxes are described as unrequited because the government provides nothing commensurate with the payment in exchange to the individual unit making the payment.

In principle, the ESA 2010 requires taxes to be recognised on an accrual basis.⁴⁷ In fact, ESA 2010 para. 20.174 states that taxes should be recorded when the taxable events occur (usually when income is earned or when a transaction generating a tax liability occurs, and not when the taxes are collected). However, the ESA 2010 requires taxes to be recorded only to the extent that the tax liability can be reliably measured. This is a consequence of the “symmetry approach” in the macroeconomic statistical system. A tax receivable can only be recognized, if there is a corresponding tax liability by another party. Therefore, in practice, the ESA does not recognise tax amounts due unless they are documented in a tax assessment, a tax return or some other proof that establishes the taxpayer’s indisputable obligation to pay the tax.

⁴⁶ See ESA 2010, para. 20.165.

⁴⁷ See ESA 2010, para. 20.171.

In order to take account of the practical difficulties for governments to make reliable estimates of their tax revenues, the ESA provides in principle two methods to be used, the first one based on tax assessments and the other one based on cash receipts. The MGDD indicates that the national statistical authorities may choose either of the two methods, provided that it is the best way for recording revenue according to the accrual principle.⁴⁸

Tax assessment method	Time-adjusted cash method
<p><u>Recognition</u> Under this method, taxes are recorded when evidenced by assessments and declarations. This approach means that tax revenue is only recognized at the moment the tax returns are obtained by government.</p> <p><u>Measurement</u> Under this method, taxes are measured based on the amounts stated on the tax assessments and declarations. These amounts need to be adjusted by a coefficient reflecting assessed and declared amounts never collected. Therefore, other than IPSAS, a net presentation of tax revenue is preferred. The coefficients shall be estimated on the basis of past experience and current expectations in respect of assessed and declared amounts never collected. They shall be specific to different types of taxes</p>	<p><u>Recognition</u> Under this method, taxes are recorded when evidenced by cash receipts. This approach means that tax revenue is only recognized when there are actual tax payments. Where appropriate, these amounts should then be adjusted so that the cash is attributed when the activity took place to generate the tax liability. This adjustment is based on the average time difference between the activity and cash tax receipt.⁴⁹</p> <p><u>Measurement</u> Under this method, taxes are measured based on the amounts of cash receipts.</p>

ESA 20.169 requires that only amounts likely to be actually collected by government be recorded. Therefore, when recording tax amounts evidenced by tax assessments and declarations, ESA requires governments to estimate the proportion of amounts deemed uncollectible. For practical reasons, the use of the time-adjusted cash method may be preferable when there are difficulties to make reliable estimations for amounts unlikely to be collected or when there are no reliable assessments available.⁵⁰ In such cases, the MGDD states, the time-adjusted cash method is considered an acceptable proxy for accruals.⁵¹

⁴⁸ See Eurostat, Manual on Government Deficit and Debt, Implementation of ESA 2010, 2016 Edition, Luxembourg 2016, p. 85 f.

⁴⁹ For instance, if there is a 1-2 months lag between VAT being accrued and it being paid by corporations to the tax authorities, then the cash received in the first 1-2 months of the year will be allocated to the previous year.

⁵⁰ See Eurostat, Manual on Government Deficit and Debt, Implementation of ESA 2010, 2016 Edition, Luxembourg 2016, p. 87.

⁵¹ See *ibid*, page 87.

5.2 National public sector accounting frameworks

The following table analyses the existing public sector accounting guidance of five Member States (France, Latvia, Lithuania, Malta and the United Kingdom) assessed as having high accounting maturity.

Accounting for taxes	France	Latvia	Lithuania	Malta	UK
1. General principles	<p>The French manual of “Central Government Accounting Standards” contains the accounting standards that apply to the French Central Government.</p> <p>Central Government Accounting Standard (CGAS) 3, <i>Sovereign revenues</i>, establishes accounting treatment rules for sovereign revenues, including taxes, that comply with accrual accounting principles.⁵²</p>	<p>Accounting principles for public sector entities in Latvia are set by the following legislation:</p> <ol style="list-style-type: none"> (1) Accounting law; (2) Rules that set general principles for accounting; (3) Rules that set accounting principles and requirements for annual financial statements of public sector entities (excluding controlled corporations). <p>Projects are currently ongoing to achieve full transition to accrual accounting based on IPSAS. One of those projects focuses on the accounting treatment of taxes and levies. Currently an accounting manual is being developed on the basis of guidelines for revenue from non-exchange transactions (taxes).</p>	<p>Lithuania has developed its own set of accounting standards, the National Public Sector Accounting Standards (NPSAS), based on the IPSAS standards. The NPSAS were established by the accounting public sector accountability law of 2007 and came into force 1 January 2010.</p> <p>The Lithuanian NPSAS are accruals-based. However, as regards taxes, the taxable event approach based on statistical modelling has been assessed as being too complex to be implemented in practice. As a result, Lithuania accounts for taxes based on the timing of tax returns.</p>	<p>The Maltese IPSAS Adoption and Implementation Project started in mid-2012. A five-year IPSAS implementation plan including the strategic approach, success factors, possible risks and milestones was finalized and approved in 2014. As part of its IPSAS implementation plan, the Maltese government has developed guidelines that foresees a phased implementation of accrual accounting based on IPSAS. The guideline ‘IPSAS 23 Revenue from Non-Exchange Transactions (Taxes and Transfers) as adopted by the Maltese government’ outlines accrual-based approaches to recognition of revenues from non-exchange transactions based on IPSAS 23.⁵³ It has to be noted that the guideline is work-in-progress.</p> <p>Based on the current version of the guideline it is intended to follow the taxable event approach by applying statistical models as recommended by IPSAS 23.⁵⁴</p>	<p>HM Revenue & Customs (HMRC) is the agency responsible for collecting tax revenue in the UK. Its accounts are prepared on an accruals basis. HMRC complies with all relevant accounting and disclosure requirements given in “Managing Public Money” and other guidance issued by HM Treasury. This includes the Financial Reporting Manual (FRoM) and the principles underlying it as well as International Financial Reporting Standards (IFRS) as adapted or interpreted for the public sector.⁵⁵</p> <p>The UK government accounts for taxes on an accrual basis based on the taxable event approach.</p>

⁵² See Ministère des Finances et des Comptes Publics, Central Government Accounting Standards, January 2016, p. 52.

⁵³ See CIPFA, Assistance in the Implementation of Accrual Accounting (Accounting for Taxation), Eurostat Project for the Treasury Department of Malta, March 2016, p. 3 ff.

⁵⁴ See CIPFA, Assistance in the Implementation of Accrual Accounting (Accounting for Taxation), Eurostat Project for the Treasury Department of Malta, March 2016, p. 5 ff.

Accounting for taxes	France	Latvia	Lithuania	Malta	UK
1.1. Recognition	<p>According to CGAS 3, tax revenue is to be recognized in the period in which it accrues to Central Government, as long as the revenues for the period can be reliably measured.⁵⁶</p> <p>The accrual criterion for determining the timing of recognition is the occurrence of the taxable event. The reliable measurement criterion implies that the recognition of revenues may in some cases be delayed (the recognition criteria may for example only be fulfilled at the time of the filing of a tax return or the issue of a tax notice (tax assessment) by government. Therefore, depending on when tax returns are filed, tax revenues of year N may be recorded in the financial statements of either:</p> <ul style="list-style-type: none"> ▶ The year in which the taxable event occurred (Year N). This is 	<p>The government of Latvia has decided to adopt accrual principle for the accounting of taxes.</p> <p>Where tax returns are obtained on a regular basis (e.g. personal income taxes), Latvia will recognize tax revenue based on the information contained in the tax returns. Where this is not the case (e.g. corporate income tax), Latvia intends to apply a statistical model to estimate the accrued tax revenue at the end of the reporting period.</p>	<p>Lithuania recognizes tax revenue based on the timing of the tax declaration:</p> <ul style="list-style-type: none"> ▶ Where tax declarations are obtained in time (i.e. before the FS are authorized for issue), tax revenue is allocated to the accounting period in which the taxable event occurred. ▶ Where tax returns cannot be obtained in time, revenue recognition is postponed until the tax declaration is obtained. 	<p>Revenue from taxes should be recognized when a taxable event has occurred, the revenue can be measured reliably, and it is probable that the economic benefits from the taxable event will flow to the government.⁵⁸</p>	<p>Taxes are accounted for on an accruals basis. Revenue from taxes is recognized when a taxable event has occurred, the revenue can be measured reliably, and it is probable⁵⁹ that the economic benefits from the taxable event will flow to the government. Tax revenues are deemed to accrue evenly over the period for which they are due and no revenue is recognized if there are significant uncertainties regarding recovery of the taxes due.⁶⁰</p>

⁵⁵ See HM Revenue & Customs, Annual Report and Accounts 2014-2015, p. 96.

⁵⁶ See Ministère des Finances et des Comptes Publics, Central Government Accounting Standards, January 2016, p. 58.

⁵⁸ See Government of Malta, IPSAS 23 Revenue from Non-Exchange Transactions (Taxes and Transfers) - as adopted by the Maltese Government, p. 9.

⁵⁹ "Probable" means that the flow of revenue should be more likely than not to occur.

⁶⁰ See HM Treasury, The Financial Reporting Manual 2015-16, para. 8.2.5.

Accounting for taxes	France	Latvia	Lithuania	Malta	UK
	<p>the case when tax returns are filed before the authorization date of the financial statements; or</p> <p>► The year when the taxable event is reported in a tax return (typically Year N+1). This is the case when tax returns are filed after the authorization date of the financial statements.⁵⁷</p>				
1.2. Measurement	<p>As regards measurement, CGAS 3 distinguishes between gross and net sovereign revenues. <i>Net tax revenues</i> are gross tax revenues adjusted for Central Government tax liabilities and clearance decisions that cancel the validity of previously recorded tax receivables.⁶¹</p> <p>According to CGAS 9, <i>Current receivables</i>, tax receivables shall initially be measured at the amount owed to government. In case the recoverable amount of the receivable is subsequently assessed as being lower than the amount initially recognized, an impairment provision and loss must be recorded.⁶²</p> <p>With regard to the calculation of the impairment provision, CGAS 9 indicates that statistical estimates should be used in cases where</p>	<p>Taxes will be measured based on information contained in tax returns and/or on a statistical model.</p> <p>Impairments of tax receivables will be accounted for in accordance with IPSAS 29 and will be recognised in the surplus or deficit of the period in which the impairment is identified. Impairments will be based on an analysis of the aging of receivables and other factors.</p>	<p>Taxes are measured based on the amounts stated in tax returns. No statistical model is used to estimate these amounts where tax declarations are received after the authorization date of the financial statements.</p> <p>Lithuania recognizes impairments of tax receivables in the surplus or deficit (statement of financial performance) of the period in which the impairment is identified. This is usually the period following the one in which the taxable event occurred. No adjustments for uncollectible amounts (bad debt allowance) are recorded upon initial recognition (as is required by ESA 2010). Bad debt allowances are recognized only when the payment deadlines are missed with the percentages of allowance depending on the</p>	<p>Taxes should be measured in line with the requirements of IPSAS 23. This implies making estimates based on statistical modelling where appropriate.</p> <p>The current version of the guideline distinguishes between tax expenditures and expenses paid through the tax system, as required by IPSAS 23 (see Government of Malta, IPSAS 23 Revenue from Non-Exchange Transactions (Taxes and Transfers) - as adopted by the Maltese Government, p. 3).</p>	<p>Taxes and duties are measured at the fair value of the consideration received or receivable net of prepayments.⁶⁴ Receivables represent all taxpayer liabilities that have been established, irrespective of whether due or overdue, for which payments have not been received at the Statement of Financial Position date. Accrued revenue receivable represents amounts of taxes and duties relating to the financial year that are not yet due or received from taxpayers, where these have not been included in receivables and collection is reasonably certain. A proportion of these amounts is based on estimates.⁶⁵</p> <p>Estimates are made to support the accrued tax revenue where tax returns reporting taxpayer</p>

⁵⁷ See Ministère des Finances et des Comptes Publics, Central Government Accounting Standards, January 2016, p. 54.

⁶¹ See Ministère des Finances et des Comptes Publics, Central Government Accounting Standards, January 2016, p. 58.

⁶² See Ministère des Finances et des Comptes Publics, Central Government Accounting Standards, January 2016, p. 144.

⁶⁴ See HM Revenue & Customs, Annual Report and Accounts 2014-2015, p. 104.

⁶⁵ See HM Revenue & Customs, Annual Report and Accounts 2014-2015, p. 113.

Accounting for taxes	France	Latvia	Lithuania	Malta	UK
	<p>there are too many receivables in a category to be examined individually (which is the case for taxes in particular). These estimates shall be based upon the outstanding tax receivables on the reporting date estimates and should result in a different write-down rate for each category of tax, based on internal historical data and on the differences in collection rates.⁶³</p> <p>The impairment provisions shall distinguish between:</p> <ol style="list-style-type: none"> (1) Doubtful and disputed receivables where there is a clear risk of non-payment; and (2) Receivables that do not yet present a clear risk of non-payment. It applies mainly to receivables falling due after the financial year-end (31/12). The reason for recording these impairment provisions is that tax claims are never fully collected. <p>(See Ministère des Finances et des Comptes Publics, Central Government Accounting Standards, January 2016, p. 143)</p>		<p>number of overdue days. Hence, bad debt allowances for the same accounts receivables might be recognized in several reporting periods. For example, if the amounts receivables are overdue for 90 days, the impairment amounted to 30% would be recognized. If in the next reporting period, the amounts are still not collected and are overdue for more than 180 days, the impairment amount would be 50% of accounts receivables, therefore additional 20% would be recognized in the statement of financial performance.</p> <p>When the allowance is calculated, it is recognized as an expense in surplus or deficit and as a reduction of the tax receivable in the financial position statement. For information purposes, a separate account for bad debt allowance is foreseen in the chart of accounts so that the allowance is booked separately from accounts receivable.</p> <p>Tax prepayments not yet declared in tax returns by taxpayers are recorded as overpayments with "other liabilities", similarly to advance receipts. Only when evidenced by a tax return, the related revenue is recognized in surplus or deficit.</p>		<p>liabilities or associated tax payments are not filed until after the financial statements have been published.</p> <p>Statistical models are used to produce the estimates and these are based on a combination of projections building on the most recent revenue flows and forecasts of economic variables on which future revenue flows depend.</p> <p>Revenue should be accrued net of amounts not expected to be collected, which might be determined by reference to past trends in write-offs and remissions, the emerging position in-year, historical debt collection performance or by other appropriate means. According to the HM Treasury Financial Reporting Manual, where the carrying amount of an asset exceeds its recoverable amount, an impairment loss will be recognised. The impairment of receivables is calculated to provide a fair value of receivables, in effect reducing them to a value that is likely to be collected and providing for non-collectable debt.</p> <p>Finally, income taxes are not netted for tax credits. Tax credits are included within expenses of</p>

⁶³ See Ministère des Finances et des Comptes Publics, Central Government Accounting Standards, January 2016, p. 143.

Accounting for taxes	France	Latvia	Lithuania	Malta	UK
					government and not as a reduction of tax revenue. ⁶⁶ The Whole-of-Government Accounts for the year ended 31 March 2015 report that “the maximum overall uncertainty regarding estimating taxation revenue is expected to be around £4 billion, which does not significantly affect the reported position. This figure is equivalent to less than 1% of the £566.7 billion tax revenue reported in the Statement of Revenue and Expenditure.”
2. Taxes on income:					
2.1. Approach followed	Approach 2: Tax return approach	Approach 2: Tax return approach and Approach 1: Taxable event approach (depending on type of tax)	Approach 2: Tax return approach	Approach 1: Taxable event approach (currently foreseen)	Approach 1: Taxable event approach
2.2. Accounting treatment	According to CGAS 3, revenue from both personal and corporate income taxes is recognized in the period in which the taxable event (i.e. earning of taxable income) is reported in a tax return. Since income tax returns in France are filed in year N+1, this means that the related tax revenue is recognized in the year following that in which the taxable event occurred. ⁶⁷ The reason advanced by CGAS 3 is that the income tax assessment lag makes it impossible to record	Revenue from personal income tax will be recognized during the reporting period congruently with the filing of the tax returns. Since tax returns are filed on a monthly basis they will be obtained before the closing of the financial statements for the reporting period. It is therefore expected that under such tax return model it will be possible to recognize revenue from personal income tax in the period in which the related taxable event has occurred. In accordance with IPSAS 23,	In Lithuania, tax returns for personal income taxes are filed on a monthly basis (in principle on the 15 th day of the following month). Since all tax returns relating to the reporting period are filed before the government financial statements are authorized for issue (15 th of March of the following year), this means that revenue from personal income taxes is recognised in the reporting period in which the taxable event occurs. The opposite holds true for	With regard to personal income taxes, the current version of the guideline distinguishes between ‘income tax from employment’ and ‘income tax from self-employed persons’. In the case of income tax from employment, monthly returns are submitted to the tax authority by the employer. Payments also occur on a monthly basis. Hence, income tax from employment should be recognized in the month in which the income was earned. The underlying measurement source is the central database of	Where personal tax returns are missing or are filed late, some estimations are required. Estimates are also required to recognise underpayments as receivables or overpayments as payables identified during the end of year final reconciliations of individual taxpayer accounts. HMRC estimates these amounts based on previous experience of the levels of underpayments and overpayments from previous settlements as there are no alternative sources of data to draw from. ⁷³

⁶⁶ See HM Treasury, The Financial Reporting Manual 2015-16, para. 8.3.6.

⁶⁷ See Ministère des Finances et des Comptes Publics, Central Government Accounting Standards, January 2016, p. 55.

Accounting for taxes	France	Latvia	Lithuania	Malta	UK
	<p>the tax revenues in the financial statements for the year in which the taxable income was earned.⁶⁸</p> <p>Tax prepayments (instalments) received for personal and corporate income tax are recognised on the balance sheet only until the final assessment of the tax owed is made in the subsequent year.⁶⁹</p>	<p>revenue which refers to future periods will be treated as advance receipts.</p> <p>The question of corporate income taxes is still open in search of the most appropriate treatment, considering that tax returns for year N are only filed in the following year when companies submit their financial statements.⁷⁰ Latvia currently works on finding the best solution for corrections of tax liabilities and receivables using a statistical model that could be based on historical experience and estimates for the reporting period. It is expected that corporate income taxes will be recognized based on the cash inflows from taxes collected during the reporting period together with an</p>	<p>corporate income taxes: since corporate tax returns for year N are only received on 1 June of year N+1 (which is after the financial statements for year N are authorized for issue), the related tax revenue is only recognized in year N+1.</p>	<p>information which centralizes the monthly returns.</p> <p>In the case of income tax from self-employed persons, self-assessment tax prepayments should be made by the taxpayers during the taxation period. Income tax from self-employed persons should be recognized in the financial year in which the economic activity took place. The amount recognised will be based on the prepayments paid during the year with a statistical estimation of any remaining settlement, which is due in June of the subsequent year.⁷¹</p> <p>With regard to corporate income taxes, companies pay tax prepayments during the taxation period based on their 'Year-2 profits'. Corporate income tax</p>	<p>Instalments for corporate income taxes are received three to four times throughout the year. Based on these prepayments as well as on prior year outturns (historical trends), statistical estimates are made for total corporate tax revenue for the year, together with adjustments for underpayments (tax receivable) or overpayments (tax payable).⁷⁴</p>

⁷³ See HM Revenue & Customs, Annual Report and Accounts 2014-2015, p. 112.

⁶⁸ For example, in the case of corporate income tax, the Central Government cannot know how much revenue the tax will produce until corporations file their annual returns four months after the end of their financial year. This means that, in most cases, the Central Government does not receive corporate income tax returns for the year N until after it has drawn up its own financial statements for the year N.

⁶⁹ See Ministère des Finances et des Comptes Publics, Central Government Accounting Standards, January 2016, p. 62 f.

⁷⁰ In Latvia annual corporate income tax returns are usually filed in April of the following year (or June for large enterprises).

⁷¹ See Government of Malta, IPSAS 23 Revenue from Non-Exchange Transactions (Taxes and Transfers) - as adopted by the Maltese Government, p. 6.

⁷⁴ See HM Revenue & Customs, Annual Report and Accounts 2014-2015, p. 113.

Accounting for taxes	France	Latvia	Lithuania	Malta	UK
		adjustment for accruals at the end of the reporting period based on a statistical model.		should be recognised in the financial year in which the economic activity took place. The amount recognized as revenue for the period will be based on the prepayments paid during the year with a statistical estimation of any remaining settlement. This final settlement is due in the subsequent year, when companies submit their tax return, either within nine months of the end of their financial year (which may not concur with the calendar year) or by 31 March, whichever is earlier. Late payments or repayments will be recognised when they can be reliably measured. ⁷²	
3. VAT:					
3.1. Approach followed	Approach 2: Tax return approach	Approach 2: Tax return approach	Approach 2: Tax return approach	Approach 1: Taxable event approach	Approach 1: Taxable event approach
3.2. Accounting treatment	<p>According to CGAS 3, revenue from VAT is recognized in the period in which the taxable event occurs (i.e. the year in which the VAT becomes due), except where the tax returns are filed after the government financial statements are drawn up.⁷⁵</p> <p>The usual procedure for reporting VAT involves monthly returns, meaning that the bulk of the Central Government's receivables for the year are known in time to draw up the financial statements. It can however happen that VAT</p>	<p>Revenue from VAT is expected to be recognized based on the amounts stated in the monthly VAT declarations.</p> <p>Since VAT returns are generally submitted and the related taxes paid within 20 days after the end of the taxation month, most VAT returns and payments will have been received before the closing of the financial statements. This suggests that revenue from VAT will be allocated to the accounting period in which the taxable event occurred.</p>	Revenue from VAT is recorded based on the amounts stated in monthly VAT returns. Returns are obtained on the 25th day of the following month. Hence, all declarations are obtained in time (i.e. before the financial statements are authorized for issue) to record the related tax revenue in the financial statements of the reporting period in which the taxable transactions occurred.	VAT should be recognized on the final day of the tax period based on amounts declared and deemed to have arisen evenly over the period to which they relate. The underlying measurement source is the VAT database. Statistical estimation of accruals for amounts due for the financial year and not yet formally declared is only required for those returns that are filed after the authorization date of the financial statements.	<p>A large amount of the VAT accrued revenue receivable and payable is based on actual data and is therefore not subject to estimation uncertainty.</p> <p>It is however necessary to estimate a small percentage as some returns relating to the current financial year are not available prior to publication of these accounts. An estimate is produced by calculating the value of these returns last year as a proportion of the total value of the returns in the preceding period</p>

⁷² See Government of Malta, IPSAS 23 Revenue from Non-Exchange Transactions (Taxes and Transfers) - as adopted by the Maltese Government, p. 7 f.

⁷⁵ See Ministère des Finances et des Comptes Publics, Central Government Accounting Standards, January 2016, p. 54 f.

Accounting for taxes	France	Latvia	Lithuania	Malta	UK
	<p>returns for year N are only received after the financial statements for year N have been drawn up. The tax receivables corresponding to these returns, are not recognised in the financial statements for year N unless they can be reliably measured. Otherwise, they are recognized in the financial statements for year N+1.</p>				<p>last year. Those proportions are then applied to the value of returns for the corresponding period of the current year.⁷⁶</p>

⁷⁶ See HM Revenue & Customs, Annual Report and Accounts 2014-2015, p. 116.

6. Discussion of matters relevant for a European harmonization

Eurostat raised the following matters for the Issue Paper:

6.1 Consequences for a possible convergence between IPSAS and ESA

ESA 2010 follows the principle that taxes should be recorded when the activities, transactions or other events occur which create the liability to pay tax, i.e. when the taxable events occur.⁷⁷ Therefore, also ESA follows a taxable event approach. Whereas IPSAS 23 recommends the use of statistical models based on the history of collecting the particular tax in prior periods (see IPSAS 23.68) for determining the tax accruals, ESA argues that “different institutional arrangements for taxation (existence or not of assessments) may lead in practice to using different recording methods, according to the characteristic of the tax”. According to the ESA 2010 either an approach based on assessments and declarations corrected for reliable estimates of the amounts unlikely to be collected or the time-adjusted cash approach shall be used.⁷⁸ According to ESA, as long as there are no reliable assessments available or if there are amounts unlikely to be collected, tax revenues cannot be reliably estimated. In such cases ESA considers the time-adjusted cash method as an acceptable proxy for accruals.⁷⁹ ESA 2010 does not explicitly foresee the use of statistical models like in IPSAS 23. However, for recognition purposes, IPSAS 23 only requires a reliable measurement of assets arising from taxation transactions. As IPSAS 23.68 provides that “government may reliably measure assets arising from taxation transactions by using statistical models” the use of statistical models is therefore only one option for such a reliable measurement. Therefore, it can be concluded that when the time-adjusted cash method or the tax declaration/tax assessment approach are able to reliably measure tax revenue, it can be argued that they can be in line with the requirements of IPSAS 23. Whether the time-adjusted cash method or the tax declaration/tax assessment approach are able to provide the necessary reliable information required for the taxable event approach of IPSAS 23 depends very much on the nature of the tax. Where the distance between the timing of the taxable event and the collection of taxes is large the time-adjusted cash method and/or the tax declaration/tax assessment approach are less suitable than a statistical model to comply with the taxable event approach.

There are categories of taxes (e.g. VAT) where the time-adjusted cash method leads to results that are very near to what is required according to the taxable event approach. In this context it needs to be considered that digitalization in the tax administration processes leads to the fact that taxation takes place closer to the taxable event. On the other side, there might be types of taxes (e.g. personal income tax or death tax) where some of the described methods might not be suitable to reliably determine tax revenue based on the taxable event (e.g. the time-adjusted cash method).

Under a tax assessment approach tax revenues are recognized when the tax authorities have made their tax assessment and have issued a tax assessment to the taxpayer. Considering the fact that under the tax assessment approach

⁷⁷ See ESA 2010, para. 20.174.

⁷⁸ See Eurostat, Manual on Government Deficit and Debt, Implementation of ESA 2010, 2016 Edition, Luxembourg 2016, p. 86.

⁷⁹ Ibid.

- a) prepayments could be considered as tax revenue of the current period and therefore matching to the taxable event,
- b) tax payments within an appropriate timeframe after the end of an entity's reporting period could be considered as tax revenue of the current period (i.e. similar to the time-adjusted cash method) and therefore matching to the taxable event,
- c) tax declarations referring to the period of the taxable event received from taxpayers within an appropriate timeframe after the end of an entity's reporting period could be considered as tax revenue of the current period (i.e. in analogy to the time-adjusted cash method) and therefore matching to the taxable event,

the results achieved by using a time-adjusted tax assessment approach could - depending on the type of tax and the arrangements made within the tax system - be close to what would be achieved by the taxable event approach using statistical models. The main advantage of the tax assessment approach would be that the reliability and the verifiability of the results would likely be better than using statistical models.

To summarize it can be said that both IPSAS and ESA 2010 follow the taxable event approach. Therefore, on a conceptual level, convergence between ESA 2010 and IPSAS seems to be achievable. In terms of the detailed approaches to determine tax revenue of an accounting period, IPSAS refer primarily to statistical models whereas ESA 2010 recommend using either the time-adjusted cash method or the tax declaration/tax assessment approach. Depending on the category of tax and the individual Member States' tax regimes/laws all three approaches to determine tax revenue of an accounting period are in principle capable to determine tax revenue according to the taxable event. For example, for the revenue recognition of VAT the time-adjusted cash method might be sufficient to capture a significant portion of VAT tax revenue of a period, whereas with regard to income taxes the time-adjusted cash method is not able to capture income tax revenue on a sufficiently comprehensive basis. In the latter case, other methods like the tax declaration/assessment approach or statistical models might be better suited.

Despite the fact that ESA 2010 does only foresee the time-adjusted cash method and the tax declaration/tax assessment approach, this does not necessarily mean that ESA 2010 is not consistent with IPSAS. IPSAS 23 outlines that statistical models are only one possibility to comply with the taxable event approach according to IPSAS 23. As both the time-adjusted cash method and the tax declaration/tax assessment approach are able to comply with the taxable event approach, those approaches can also be in accordance with IPSAS 23. Depending on the type of tax and the individual country's tax regime/laws, the different approaches for the recognition of tax revenue in reality do not necessarily lead to different results. Therefore, consistency of ESA 2010 with IPSAS 23 depends on the type of tax and the tax arrangements within a country.

6.2 Advantages and disadvantages of the existing widely used approaches to recognize and measure tax revenue

The following table summarizes the advantages and disadvantages of the existing widely used approaches for the recognition and measurement of tax revenue. For this assessment the following criteria are used:

- ▶ Fulfilment of accrual principle (i.e. recognition of taxes when taxable event takes place)
- ▶ Models and efforts needed for the measurement of taxes
- ▶ Faithful representation⁸⁰
- ▶ Verifiability⁸¹
- ▶ Informational value of the approach.

For the tax assessment/declaration approach it is assumed that prepayments of taxes (e.g. PAYE tax) are recognized in the period when the taxable event takes place.

	(1) Statistical models in accordance with IPSAS 23	(2) Tax assessment/declaration approach	(3) Time-adjusted cash method
Advantages	<ul style="list-style-type: none"> + Tax revenues can be recognized in accordance with the taxable event approach. + Faithful representation of tax revenues can be achieved. + Informational value can be high provided that parameters and assumptions of the applied statistical models are reflecting economic reality and provided that they are disclosed. + Consideration of impairment of tax receivables and presentation in financial statements allows for deeper analysis (e.g. government's performance in collecting taxes being due and payable). + IPSAS 23 does not require the use of statistical models. Also other approaches (e.g. the tax assessment approach) are 	<ul style="list-style-type: none"> + Where the time lag between when the taxable event occurs and the point in time when the tax payer hands in the tax declaration or when the final tax amount due is determined is short faithful representation of tax revenues are improved compared to the time-adjusted cash-method. + When the amounts of actual payments by taxpayers are close to the final tax assessment/declaration then deviations from the taxable event approach are limited. + Consideration of impairment of tax receivables is possible and allows for deeper analysis (e.g. government's ability to collect taxes). + Time-adjustments (i.e. to consider also tax declarations/assessments in the subsequent accounting period before closing of the 	<ul style="list-style-type: none"> + Reliability and verifiability of revenue recognition is high as revenue will only be recognized when cash is received. + When the amounts of prepayments are close to the final taxes due and payable or when taxes are paid soon after the taxable event takes place, then deviations from the taxable event approach are limited. + Time-adjustments can bring the results closer to the results of the taxable event approach.

⁸⁰ Faithful representation is attained "when the depiction of the phenomenon is complete, neutral, and free from material error". (See IPSASB, Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities, October 2014, para. 3.10). The terms "reliable" and "reliability" are used in this paper in the meaning of "faithful representation" as outlined in IPSASB's Conceptual Framework.

⁸¹ Verifiability is the "quality of information that helps assure users that information in GPFs faithfully represents the economic and other phenomena that it purports to represent". (See IPSASB, Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities, October 2014, Para. 3.26).

	<p>possible.</p> <ul style="list-style-type: none"> + Flexibility of IPSAS 23 approach: In cases where the assets arising from taxation transactions and the related revenue cannot be reliably measured until some time after the taxable event occurs, the standard allows that assets and the related revenue may be recognized in periods subsequent to the occurrence of the taxable event. 	<p>books) can bring the results of the tax assessment/ declaration approach closer to the results of the taxable event approach.</p>	
Disadvantages	<ul style="list-style-type: none"> - Reliability and objectivity of the results achieved by using statistical models could be reduced as they involve judgement by preparers for the estimates. - Due to judgement there is an even larger risk of over- or underrecording the tax revenue. - Efforts for (a) setting up the statistical models, (b) data collection and calculations in subsequent periods and (c) corrections in subsequent periods can be high. - Time might be needed for a proper adjustment of statistical models. - Due to the complexity of statistical models also verifiability might be difficult to achieve. 	<ul style="list-style-type: none"> - Part of the tax revenues will be not recognized in accordance with the taxable event approach => especially when the time lag between the taxable event and the tax assessments/ declarations is large, i.e. when the results of the tax assessments cannot be considered in the financial statements of the year when the taxable event took place. - For some taxes there is a risk of over-recording the tax revenue, given the fact that not all taxes can be collected in the end.⁸² Impairment consideration of tax receivables can mitigate that disadvantage. - Verifiability of tax revenue is reduced compared to the time-adjusted cash method. - Time adjustments require additional efforts. 	<ul style="list-style-type: none"> - Recognizing only collected taxes does not provide information on the performance and capability of the tax collection system. - Depending on the type of tax and the Member State's tax regime tax revenues might partly not be recognized in accordance with the accrual principle => especially when the time lag between the taxable event and the tax payments are large, e.g. in case of taxes where there are no prepayments, no tax revenue would be recognized. Also in cases where tax payments are deferred no revenue would be shown in an entity's financial statements. As a result, presentation of tax revenue is not complete. In such cases, faithful representation can therefore not be achieved. - The incompleteness of data does not allow for deeper analysis of tax revenue. - Time adjustments require additional efforts.

⁸² ESA 210, para. 20.172.

6.3 Categories of taxes to be treated by future EPSAS standards or guidance taking into account materiality and comparability

Based on materiality and the assessment made in Chapter 3 EPSAS should focus on income taxes (personal income tax and corporate income tax) and VAT as they cover almost 50% of tax revenue in Member States. Against the background of the different tax systems in Member States and the fact that the application of the different approaches for the recognition of tax revenues are dependent on the type of tax and the individual Member States' tax regime/laws an EPSAS on revenue recognition of taxes would need to be principles-based. In EY's view the principles for tax accounting of IPSAS 23 should be taken as a point of reference.

Given the complexity and variety of the multiple taxes and tax systems is such that it is probably not realistic to try developing detailed guidance in a standard which covers all circumstances and arrangements in Member States additional guidance is likely needed to operationalize the principles of IPSAS 23. The EPSAS objective of comparability implies that the development of further detailed application guidance compared to what is currently provided by IPSAS 23 is needed.⁸³

The analysis has also shown that depending on the category of tax and the individual Member State's tax system/tax laws, the tax assessment/tax declaration approach and the time-adjusted cash method under certain circumstances lead to the same result in terms of revenue recognition compared to statistical models. Detailed application guidance on accounting for taxes would therefore be needed to provide the linkages between the categories of taxes and the different approaches as well as how these approaches should be applied. For the design and the practical application of those approaches tax-specific application guidance would be needed.

Given that VAT has a common legal framework between Member States, development of application guidance for the revenue recognition of VAT should be possible. Furthermore, as for VAT the time lag between the taxable event and the tax payments is limited, the level of complexity for such guidance seems to be manageable. However, it has to be seen that the EU's common system of value added tax (VAT) offers options. Therefore, it has to be considered how Member States use these options and what effect that has on determining tax revenue from VAT.

For income taxes (personal income tax and corporate income tax) it has to be considered that tax systems differ between Member States. Therefore, statistical models and/or a time-adjusted tax declaration/tax assessment approach are possibly the best approaches to reliably determine tax revenue of an accounting period for income taxes. However, there is currently no guidance under IPSAS available how those approaches should be designed and applied in practice.

Even though the approach for levying income taxes is similar throughout the Member States, significant differences can appear at the level of the individual tax. In fact, when comparing the main features of the tax systems for the different Member States, it becomes clear that attributes like for example the definition of the tax base, the tax rates

⁸³ In this context it needs to be considered that IPSAS 23 is meant for global application and therefore needs to be more general and less detailed/prescriptive.

applied, the different types of incomes included in capital income or the different types of tax credits and tax deductions that governments provide to their taxpayers differ between the Member States. This is consistent with the fact that, to this day, no EU-wide directive or regulation on income taxes has been implemented. Also a differentiation between 1) taxes from stable employment that are characterized by regular predictable incomes and therefore tax revenue, 2) other types of employment with less stable incomes and taxes and 3) corporate taxes (that are also likely to be less stable) is helpful in determining the best approach for a reliable measurement of tax revenue of an accounting period for income taxes.

For the accounting for other categories of taxes than VAT and income taxes (like death tax (duty) or property tax) a principle-based approach covered in an EPSAS on accounting for taxes seems appropriate. At a later stage in the EPSAS process it should be considered whether specific application guidance for the determination of tax revenue based on the taxable event for these categories of taxes should be developed or whether a principles-based approach is sufficient (also taking into account the experiences made with the guidance on accounting for VAT and income taxes).

6.4 Need for supplementary guidance to what is currently foreseen under IPSAS and format of that guidance

As outlined above EY is of the view that application guidance on accounting for taxes that is directed to preparers needs to concretize the principles of IPSAS 23 on accounting for taxes and outline how the principles shall be applied in practice. This application guidance could be provided as a separate part of the EPSAS (similar to application and implementation guidance provided under IPSAS) or as a separate (sub-standard) interpretations document.

Our analysis has shown that for the application of the taxable event approach in practice more detailed application guidance is needed for the design and operations of statistical models or other suitable approaches like the tax declaration/tax assessment approach or the time-adjusted cash method for the determination of tax revenues in accordance with the taxable event approach. For the question which of these approaches should be applied under what circumstances a differentiation of income taxes between 1) taxes from stable employment that are characterized by regular predictable incomes, 2) other types of employment with less stable incomes and 3) corporate taxes is expected to be useful. It also needs to be considered that due to the different tax systems in Europe the applicable models and approaches might differ between Member States. The different characteristics of the tax systems would need to be reflected in the EPSAS application guidance.

As outlined above application guidance should be developed with a focus on VAT and income tax. With regard to the format of such guidance, for each category of taxes guidance on recognition (especially the application of statistical models, tax declarations/tax assessment approach as well as the time-adjusted cash method), measurement, presentation and disclosure issues should be provided.

For the determination of tax revenue based on statistical models it would be required to specify on how the statistical model would need to be set up and for which categories of taxes it could be applied. Especially the relevant variables, types of parameters and necessary assumptions for the model should be identified. Also guidance needs to be

provided for subsequent application of the statistical model as well as on how to determine and handle corrections in subsequent periods. Also detailed tax-specific application guidance would be needed for the design and application of those statistical models.

For the application of the tax assessment/declaration approach it would need to be specified for each category of the relevant taxes at what point in time an entity would be allowed to recognize a tax receivable. Also recommendations with regards to time adjustments should be given (e.g. until what point in time tax assessments/declarations should be considered). Also with regards to measurement further guidance should be provided on impairment of tax receivables.

In summary, EY would recommend that future EPSAS guidance on accounting for taxes should be designed as follows:

Type of guidance:	Standard (EPSAS)	Interpretations and application guidance (either as part of the EPSAS or as separate)
Purpose of guidance:	Principles for accounting of tax revenues by Member States	Providing interpretations and application guidance for accounting for tax revenues by preparers in Member States
Point of reference:	Principles on accounting for taxes under IPSAS 23	Individual tax systems of Member States
Issues to be covered:	<ul style="list-style-type: none"> • Recognition principles for tax revenues (i.a. the taxable event approach, advance receipts of taxes) • Measurement of assets arising from taxation transactions (i.a. reliable measurement through statistical models, the tax declaration/tax assessment approach or the time-adjusted cash method, factors determining the measurement, impairment of tax receivables) • Presentation and disclosures issues, like accounting treatment of differences between tax amounts determined by the different measurement methods and the amounts determined in subsequent reporting periods or treatment of expenses paid through the tax system and tax expenditures 	<ul style="list-style-type: none"> • Concretion of the recognition principles for tax revenues taking into account the individual tax systems of Member States • Concretion of the measurement principles for tax revenues taking into account the individual tax systems of Member States (i.a. application of what measurement approach under what circumstances) • Detailed application guidance on presentation and disclosure issues taking into account the individual tax systems of Member States

7. Way forward recommended

Based on the analysis above, EY has derived the following recommendations:

1. Given the variety of tax arrangements in Member States there should be a principles-based EPSAS on accounting for taxes. The EPSAS should be based on the principles of IPSAS 23 and should follow the taxable event approach. Given the fact the EPSAS should be principles-based the standard shall apply to all categories of tax revenue.

Rationale:

- ▶ Taxes are the main source of revenue for governments.
- ▶ The complexity and variety of the multiple taxes and tax systems is such that it is probably not realistic trying to develop detailed guidance in a standard.
- ▶ IPSAS 23 shall be taken as a first reference base for EPSAS to ensure comparability across Member States on accounting for tax revenues on a conceptual level.
- ▶ Given the fact that also ESA requires tax revenue recognition based on the taxable event, convergence between IPSAS and ESA would be achieved.

2. Additional application guidance for the accounting of tax revenue should be developed. In our view, this application guidance could be provided as a separate part of the EPSAS (similar to IPSAS) or as a separate (sub-standard) interpretations document. Taking into account materiality and comparability such guidance should in the first instance focus on VAT and income taxes (personal income tax and corporate income tax). Depending on the category of tax and the respective tax system detailed application guidance should be developed for the design and practical application of statistical models, the tax declaration/tax assessment approach and the time-adjusted cash method. This guidance would need to be tax-specific and would have to take into account the individual tax systems of Member States.

Rationale:

- ▶ VAT and income taxes are the main source of tax revenue for governments. They cover almost 50% of tax revenue in Member States.
- ▶ The level of guidance provided by IPSAS 23 and ESA needs to be concretized for the accounting of taxes in accordance with the taxable event approach.
- ▶ Each category of taxes has different characteristics that need to be considered in the development of guidance.
- ▶ Depending on the category of tax and the individual country's tax regime/laws next to statistical models the tax declaration/ assessment approach and the time-adjusted cash method are able to fulfil the taxable event requirement.
- ▶ Tax systems vary in Member States, especially with respect to income taxes.

3. Given the fact that the IPSASB currently has a project on "Revenue" on its agenda, this project should be closely monitored in the context of the development of the EPSAS guidance on accounting for taxes.

Rationale:

- ▶ The aim of IPSASB's project is to develop one or more IPSASs covering revenue transactions (exchange and non-exchange).
- ▶ Based on the current IPSASB's work plan a Consultation Paper is envisaged to be approved for December 2016.

8. Implications to be noted for other non-exchange revenue

For non-exchange revenue transactions like transfers or grants typically no estimation uncertainties occur. Therefore no implications for those other non-exchange revenues were noted based on the lessons learnt from the recognition of tax revenue. However, for revenue recognition of social contributions similar issues can arise as for taxes. Similar to personal income tax, social contributions are based on incomes and can be paid in later reporting periods. For the revenue recognition of social contributions therefore possibly approaches similar than for taxes could be applied.

9. Summary of questions

In the following a summary of the questions raised by Eurostat is provided:

For which main categories of taxes do problematic points/issues with regards to recognition and measurement arise?

The following problematic points/issues with regards to recognition and measurement of tax revenue for the main categories of taxes have been identified:

- (1) For taxes where the time lag between the taxable event and the collection of taxes is large (e.g. more than 6 months) cash-based methods (e.g. the time-adjusted cash method) are not able to fulfil the taxable event requirement of IPSAS 23. This holds true especially for income taxes.
- (2) Also the use of statistical models for reliably measuring tax revenues can be problematic as in some cases making a reliable estimate based on statistical models might not be possible. These problems are caused for example by the volatility of the tax base, the lack of availability, quality and reliability of data used for the statistical models or the differing abilities of Member States to collect taxes. This problem applies to both income taxes as well as to VAT.
- (3) To sum up: Dependent on the type of tax, statistical models, the tax declaration/tax assessment approach as well as cash-based methods might not be able to fulfil the taxable event requirement of IPSAS 23 for revenue recognition of taxes. In case that none of the tax recognition methods is able to fulfil the taxable event approach then tax revenue would have to be recognized when cash is received (or reimbursed) by tax authorities.
- (4) It can be questionable for some types of taxes whether the taxable event is the appropriate point in time when an entity controls those resources and therefore recognizes tax revenue. This is especially the case for income taxes.
- (5) With regards to the measurement of tax receivables, impairments on those receivables can sometimes be hard to be determined, especially when reliable historical data is not available. This can especially be the case for income taxes.
- (6) The guidance provided in IPSAS 23 is not detailed enough for a practical application of the standard. This applies to both income taxes as well as VAT.

Are the problematic points/issues with regards to recognition and measurement of tax satisfactorily treated in IPSAS?

IPSAS 23 suggests the use of statistical models for a reliable measurement of taxes. These statistical models can be helpful in reliably determining tax revenue based on the taxable event approach. However, the guidance provided in IPSAS 23 on the design and the operations of such statistical models is not sufficient for a practical application by Member States. In general, IPSAS 23 allows the use of other models and approaches than statistical models, however, no guidance is provided under what circumstances which approach/model should or could be used. IPSAS 23 acknowledges that the use of statistical models for reliably measuring tax revenues can be problematic in some cases and therefore suggests to recognize such tax revenues only in subsequent periods to the taxable event.

IPSAS 23 does not provide further guidance at what point in time an entity controls the tax resources and whether that can conflict with the taxable event approach or not. Given IPSAS 23's preference for statistical models the guidance on the application of other

approaches/models is limited. As a consequence also further guidance on the subsequent measurement of tax receivables is not included in IPSAS 23.

Which categories of taxes should be treated by future EPSAS standards or guidance taking into account materiality and comparability considerations?

Based on materiality and the assessment made in Chapter 3 EPSAS should focus on income taxes (personal income tax and corporate income tax) and VAT as they cover almost 50% of tax revenue in Member States. Against the background of the different tax systems in Member States and the fact that the application of the different approaches for the recognition of tax revenues are dependent on the type of tax and the individual Member States' tax regime/laws an EPSAS on revenue recognition of taxes would need to be principles-based. In EY's view the principles for tax accounting of IPSAS 23 should be taken as a point of reference.

Would supplementary guidance on some aspects of the treatment of taxes be necessary and what would this look like?

Given the principles-based approach of IPSAS 23 further application guidance on accounting for taxes that is directed to preparers is needed. The principles of IPSAS 23 need to be concretized for a practical application by Member States. In EY's view this application guidance could be provided as a separate part of the EPSAS (similar to IPSAS) or as a separate (sub-standard) interpretations document. It should focus on recognition, measurement and presentation/disclosures of tax revenues/tax receivables and it would need to be tax-specific.

The table on page 38 of the issue paper summarizes how future EPSAS guidance on accounting for taxes could be designed.

What would the consequences be for a possible convergence between EPSAS and ESA?

Both IPSAS and ESA 2010 follow the taxable event approach. Therefore, on a conceptual level, convergence between ESA 2010 and IPSAS seems to be achievable. In terms of the detailed approaches to determine tax revenue of an accounting period, IPSAS refer primarily to statistical models whereas ESA 2010 recommend to use either the time-adjusted cash method or the tax declaration/tax assessment approach. Depending on the category of tax and the individual Member States' tax regimes/laws all three approaches to determine tax revenue of an accounting period are in principle capable to determine tax revenue according to the taxable event. For example, for the revenue recognition of VAT the time-adjusted cash method might be sufficient to capture a significant portion of VAT tax revenue of a period, whereas with regard to income taxes the time-adjusted cash method is not able to capture income tax revenue on a sufficiently comprehensive basis. In the latter case, other methods like the tax declaration/assessment approach or statistical models might be better suited.

Despite the fact that ESA 2010 does only foresee the time-adjusted cash method or the tax declaration/tax assessment approach, this does not necessarily mean that ESA 2010 is not consistent with IPSAS. IPSAS 23 outlines that statistical models are only one possibility to comply with the taxable event approach according to IPSAS 23. As the time-adjusted cash method or the tax declaration/tax assessment approach both are able to comply with the taxable event approach, those approaches can also be in accordance with IPSAS 23. Depending on the type of tax and the individual country's tax regime/laws, the different

approaches for the recognition of tax revenue in reality do not necessarily lead to different results. Therefore, consistency of ESA 2010 with IPSAS 23 depends on the type of tax and the tax arrangements within a country.

Differences between what has been reported under the taxable event approach using statistical models and what has been reported under ESA 2010 using the the time-adjusted cash method or the tax declaration/tax assessment approach could be subject to notes disclosures under EPSAS.

What way forward is recommended on taxes and what would be a good approach for organising future discussions with the EPSAS stakeholders?

For the way forward that EY recommends please refer to chapter 7 of the issue paper.

A good approach for organising future discussions with the EPSAS stakeholders in EY's view would be to (again) present this issue paper at the Working Group meeting in November 2016 and seek Member States' view on the proposals presented in this paper.

Are there any implications that should be noted for other non-exchange revenues from the conclusions on taxes?

For revenue recognition of social contributions similar issues can arise as for taxes. Similar to personal income tax, social contributions are based on incomes and can be paid in later reporting periods. For the revenue recognition of social contributions therefore possibly approaches similar than for taxes could be applied.

10. Annexes

10.1 Annex 1 – EU tax revenues, breakdown by Member State and category of tax (MEUR) in 2014⁸⁴

ESA 2010 code	D2	D21	D211	D212	D214	D29	D5	D51	D59	D6	
Country / Description	Taxes on production and imports	Taxes on products	Value added type taxes (VAT)	Taxes and duties on imports excluding VAT	Taxes on products, except VAT and import taxes	Other taxes on production	Current taxes on income, wealth, etc.	Taxes on income	Other current taxes	Social contributions	Total
Austria	47.964	36.693	25.445	369	10.879	11.271	45.081	42.858	2.223	50.776	143.821
Belgium	53.070	44.219	27.518	2.368	14.333	8.851	67.198	65.263	1.936	67.756	188.024
Bulgaria	6.220	5.985	3.799	74	2.112	235	2.252	2.188	65	3.297	11.770
Croatia	8.103	7.660	5.368	70	2.223	442	2.631	2.458	173	5.065	15.799
Cyprus	2.615	2.254	1.512	36	706	362	1.775	1.599	176	1.557	5.948
Czech Republic	18.793	18.044	11.602	2.226	4.216	749	11.193	11.072	121	22.826	52.813
Denmark	43.304	37.389	24.985	403	12.001	5.916	87.036	83.569	3.466	2.740	133.080
Estonia	2.781	2.622	1.711	881	30	158	1.479	1.479	-	2.222	6.481
Finland	29.695	29.259	18.948	170	10.141	436	33.771	31.540	2.231	26.288	89.754
France	338.907	240.257	148.129	2.548	89.580	98.650	269.968	245.625	24.343	408.548	1.017.423
Germany	318.461	299.230	203.081	22.896	73.253	19.231	345.621	338.234	7.387	481.948	1.146.030
Greece	27.937	22.228	12.676	272	9.280	5.709	17.227	15.033	2.194	23.847	69.011
Hungary	19.438	17.481	9.754	139	7.588	1.956	6.937	6.705	232	13.618	39.993
Ireland	21.379	18.440	11.496	3.599	3.345	2.938	24.938	23.073	1.865	10.898	57.214
Italy	249.439	189.485	96.897	2.081	90.507	59.954	237.567	230.096	7.471	216.404	703.410
Latvia	3.025	2.697	1.787	38	872	328	1.834	1.761	73	2.054	6.913
Lithuania	4.207	3.984	2.764	104	1.116	223	1.844	1.825	19	4.174	10.224
Luxembourg	6.388	5.523	3.586	1.499	439	864	6.813	6.484	330	6.012	19.213
Malta	1.112	1.071	642	14	415	41	1.156	1.077	78	560	2.828
Netherlands	77.445	66.967	42.708	8.942	15.317	10.478	70.982	63.671	7.311	101.761	250.188
Poland	53.043	46.966	29.317	2.258	15.392	6.076	28.543	25.992	2.551	54.381	135.967
Portugal	24.740	22.115	14.672	954	6.489	2.625	18.974	18.247	726	20.371	64.084
Romania	19.363	18.050	11.650	565	5.835	1.313	9.310	8.768	542	12.913	41.585
Slovakia	8.173	7.345	5.021	127	2.196	828	5.120	4.868	252	10.289	23.582
Slovenia	5.636	5.131	3.154	53	1.925	505	2.677	2.421	256	5.464	13.776
Spain	120.823	100.740	64.688	1.644	34.408	20.083	105.393	101.480	3.913	130.063	356.279
Sweden	95.157	51.352	38.846	633	11.874	43.805	77.243	76.102	1.141	16.146	188.547
United Kingdom	291.030	255.022	154.146	3.658	97.218	36.008	307.954	256.616	51.339	171.992	770.976
Total	1.898.243	1.558.208	975.901	58.619	523.688	340.035	1.792.516	1.670.104	122.413	1.873.970	5.564.730

⁸⁴ This overview has been prepared based on the Tax revenue statistics as published on the website of Eurostat (http://ec.europa.eu/eurostat/statistics-explained/index.php/Tax_revenue_statistics).

10.2 Annex 2 – Main features of the tax systems: Personal income tax⁸⁵

Main features of tax system	General		System and Applicable rates						Capital income						Main tax credits & deductions				
	Country	Base and jurisdiction	Taxation of couples and families	Basic allowance	Rate schedule	Surtaxes	Regional and local surcharges	Top statutory PIT rate (including surcharges)	Owner-occupied dwelling	Income from renting movable property	Income from renting immovable property	Capital gains (immovable property)	Capital gains (movable property)	Dividends	Interests on deposits and special savings accounts	Interests on corporate and government bonds	Professional expenses	Pension savings	Others (not exhaustive)
Austria	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation	EUR 11 000 + tax credits: employee, traffic, pensioner, sole earner and single parents	- progressive, rates: 36.5 % 43.21 % and 50 % - top marginal rate: 50 %(> EUR 60 000)	NA	NA	50%	not included	included	included	included	included	25 % (final withholding)	25 % (final withholding)	25 % (final withholding)	lump-sum OR based on real expenses	yes	child care, educational, medical and travel expenses, loan interest, alimony, donations, life insurance contributions, union fees, national regional or local taxes	3-year carry forward (small businesses, specific restrictions)
Belgium	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation (limited) marital quotient	EUR 7 090 (increased for lower income) + allowances for children (increasing with rank, refundable up to EUR 430 per child) and other dependents	- progressive, 5 brackets: 25 % 30 % 40 % 45 % 50 % (*) - top marginal rate: 50 % (> EUR 37 870)	NA	- local additional surtaxes: 7.54 % (on average (max: 9 % Brussels: 7 %)	54%	exempted	included	included in global income (specific rules)	no, except in principle for some short-term capital gains	no, but some exceptions: separate taxation of 0.4 % (on capital gains on shares which are normally totally exempted and which are realised by another company than a SME)	25%	standard saving accounts exempted (15 % when > EUR 1 880 interest income); other deposits: 25 %	25 % (15 % on some specific government bonds)	yes (lump sum proportional OR based on real expenses, capped)	yes	educational travel expenses, alimony, child care expenses, donations, investment in particular eco friendly or energy efficient goods; several refundable tax credits (incl for low income workers)	indefinite carry forward, can be transferred to spouse or partner
Bulgaria	resident: worldwide income (subject to double-tax relief) non-resident: domestic income	- separate taxation	- LEI 200 per child (max. LEI 600)	- flat rate 10 %	NA	NA	10%	not included	included in global income	included in global income	included in global income	included in global income (except if sold on EEA stock exchange)	5 % final withholding tax	8 % final withholding tax	exempted	NA	yes, also to life insurance funds	BGN 7 920 per year (BGN 660 per month) deduction from taxable income for persons with 50 % or more reduced capacity for work	yes (deduction), in certain conditions (income from sale or exchange of stocks, shares, compensatory instruments, investment bonds, etc.)
Croatia	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation	HRK 31 200; child allowance increasing with rank (HRK 15 600 for 1st child)	- progressive, 3 rates: 12 % 25 % 40 % - top rate: 40 % (> HRK 158 400)	NA	- max 18 % surcharge, depending on municipality size	47.2 %	not included	12%	12%	25%	exempt	12%	0.12	not included	in percentage of income or based on real expenses [self-employed]	yes	donations	5-year carry forward
Cyprus	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation	up to EUR 19 500 tax free progressive, brackets: 20 % 25 % 30 % 35 %	- top rate: 35 % (> EUR 60 000)	NA	NA	35%	not included	included in general income	included in general income	20%	NA	17 % (final withholding tax under Special Defence Contribution)	30 % (final withholding tax under Special Defence Contribution)	30 % (final withholding tax under Special Defence Contribution), except for government bonds which are 3 %	based on real expenses	yes	travel expenses, loan interest, donations, life insurance contributions, union fees	5-year carry forward
Czech Republic	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation	CZK 24 840; other credits depending on family and level of income	- flat rate 15 %	7 % solidarity surcharge on high incomes (> 4 times average wage)	NA	22.0 %	not included	included in global income (occasional income from renting movable property is exempted up to the limit of CZK 30 000/year)	included in global income	included in global income, but exempt if property used for permanent housing at least 2 years before sale or owned more than 5 years	exempt	15%	0.15	0.15	NA	yes	childcare and educational expenses, donations for purposes of science, education, culture, medicine, ecology, sports, and religion are deductible up to 15 % of the tax base	5-year carry forward
Denmark	- resident: worldwide income (subject to double-tax relief) (pension tax, local tax), domestic income (state tax, church tax) - non-resident: "limited income" (domestic income)	- separate taxation, joint taxation of net positive capital income and of pension (state tax, church tax) nb: children are also tax liable	DKK 43 400 (DKK 32 600 for <18y); can be transferred between spouses additional employment allowance 8.05 % maximum DKK 28 500	- state tax: progressive: 8.08 % and 15 % (> DKK 459 200 in 2015) - labour market contribution: 8 % (flat) (P); health tax: 4 % (2015)	NA	- local tax: between 22.5 % and 27.8 % avg: 24.904 %	55.8 %	not included	NA	included in global income	taxable as capital income (except owner-occupied dwellings)	progressive: 27 % and 42 % (> DKK 49 899)	progressive: 27 % and 42 % (> DKK 49 899)	included in global income	included in global income	yes, based on real expenses	yes	donations; labour market contributions are deducted	deductible in top tax and dividend tax, rest is passed on to spouse, and then indefinite carry forward
Estonia	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation - possibility of joint declaration	EUR 1 848 additional allowance for children and old age dependants	- flat rate: 20 %	NA	NA	20%	not included	included in global income	included in global income	included in global income	included in global income		included in global income	creditable withholding tax	based on real expenses (for entrepreneur income only)	yes	donations, educational expenses	7-year carry forward
Finland	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation	for national income tax, no tax on earned income below EUR 16 500 for municipal tax, earned income allowance maximum EUR 2 970 per year	- progressive, 5 rates from 6.5 % to 31.75 % - top marginal rate: 31.75 % (> EUR 90 000)	NA	- municipal income tax varying between 16.5 % and 22.5 % (weighted average 19.84 %; church tax of between 1 and 2 % depending on the municipality (average 1.43 %)	51.6 %	not included	included in capital income	included in capital income	included in capital income	included in capital income	creditable withholding tax 7.5 % (non-listed companies), 25.5 % (listed companies), 27 % (dividends exceeding EUR 150 000)	30 % (final withholding)	30 % (final withholding)	standard lump-sum deduction (EUR 620) OR based on real expenses	No	travel expenses, alimony, donations (deductible from earned income); interest from loans (deductible from capital income)	10-year carry forward
France	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- joint taxation (tax unit is the household) - quotient familial (1 share per parent, 1/2 share for the first two children or dependants, 1 additional share for each additional child or dependent)	up to EUR 9 690 tax free	- progressive—5 brackets: 0 % 14 % 30 % 41 % 45 % - top marginal rate on earnings: 45 % (> EUR 151 956) - exceptional contribution on incomes: 3 % (> EUR 250 000/individual) or 4 % (> EUR 500 000/individual)	- general social welfare contribution (CSG) (partially deductible): 7.5 % (earnings) - welfare debt repayment levy (CRDS): 0.5 %	NA	50.3 %	not included	included	included	19 % flat rate (exemptions apply) + 15.5 % social contributions	capital gains on securities subject to progressive income tax, with reduction regime depending on length of time securities held, and whether SME; gains on business assets held < 2 yrs taxed as business income, > 2 yrs 16 % flat rate	subject to progressive income tax for 60 % of amount + 15.5 % social contributions; 24 % withholding tax creditable against final tax liability (possible exemption < EUR 50 000/individual)	subject to progressive income tax + 15.5 % social contributions; 24 % withholding tax creditable against final tax liability (possible exemption < EUR 25 000/individual); certain special savings accounts are exempted	subject to progressive income tax + 15.5 % social contributions; 24 % withholding tax creditable against final tax liability (possible exemption < EUR 25 000/individual)	- income tax: yes, in percentage (10 %) OR based on real expenses; capped (EUR 12 157) - CSG/CRDS: yes, 1.75 % capped (EUR 2 663)	Yes	- refundable tax credits: earned income tax credit (prime pour l'emploi), childcare for young children; tax credit or reduction for home employees - tax reductions: low income households, certain type of investment, charitable or other donations	6-year carry forward (can be transferred to spouse or partner)
Germany	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- joint taxation and full marital quotient - separate taxation possible, but will always yield tax liabilities → joint	EUR 8 472; child credit or allowance, special provisions for lone parents	- marginal rate increasing with income (formula): from 14 % till 42 % (45 % for very high incomes) - top marginal rate 42 % (> EUR 52 882), 45 % (> EUR 250 731)	- 5.5 % (on income tax liability [solidarity surtax] (an exemption limit is applied)	No	47.5 % (50.5 % > EUR 250 731)	not included	included in general taxation	included in general taxation	included in general taxation	included in general taxation	25 % (final withholding) — possibility to opt-out if marginal effective tax rate below 25 %	25 % (final withholding) — possibility to opt-out if marginal effective tax rate below 25 %	25 % (final withholding) — possibility to opt-out if marginal effective tax rate below 25 %	yes, lump sum (employees; EUR 1 000/year) / based on real expenses, capped (business)	Yes	Yes, partly capped	1-year carry backward; unlimited carry forward
Greece	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation - joint tax form but separate assessment	none	- progressive, 3 rates: 22 % (≤ EUR 25 000), 32 % (EUR 25 000–42 000), 42 % (> EUR 42 000) - top rate: 42 % (> 42 000)	- special solidarity contribution: 0.7 % (EUR 12 001–20 000), 1.4 % (EUR 20 001–30 000), 2 % (EUR 30 001–50 000), 4 % (EUR 50 001–100 000), 6 % (EUR 100 001–600 000), 8 % (> EUR 500 000) on annual total net income	NA	48%	included	NA	11 % (up to EUR 12 000), 33 % (> EUR 12 000)	15%	15%	10 % (final withholding)	15 % (final withholding)	15 % (final withholdin	yes, based on real expenses, capped	included	child care, educational and medical expenses, alimony, donations, life insurance contributions, investment in eco-friendly goods	5-year carry forward

⁸⁵ This overview has been prepared based on the Eurostat publication "Taxation trends in the European Union", 2015 edition (http://ec.europa.eu/taxation_customs/taxation/gen_info/economic_analysis/tax_structures/index_en.htm).

Personal income tax systems	General		System and Applicable rates						Capital income						Main tax credits & deductions				
	Country / Main features	Base and jurisdiction	Taxation of couples and families	Basic allowance	Rate schedule	Surtaxes	Regional and local surcharges	Top statutory PIT rate (including surcharges)	Owner-occupied dwelling	Income from renting movable property	Income from renting immovable property	Capital gains (immovable property)	Capital gains (movable property)	Dividends	Interests on deposits and special savings accounts	Interests on corporate and government bonds	Professional expenses	Pension savings	Others (not exhaustive)
Hungary	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation	- children: The basis of income tax can be reduced by HUF 750 000 per year/each dependent for families having one or two children), or HUF 2 475 000 per year/each dependent for families having at least three children) (child allowances can also offset SSC liabilities). - first marriage: The tax base can be reduced by HUF 375 000 per year per marriage, provided at least one of the couple is getting married for the first time. The allowance can be used for maximum 2 years.	- flat rate 16 %	NA	NA	NA	16%	included	16%	16%	16%	16 % creditable withhold	16 % final withholding; interests from LT accounts: 0 % 10 % 16 %	16 % final withholding	10 % of income OR based on real expenses (only for self-employed)	Yes (20 % capped, tax refunds)	union membership fees	(limited) 5-year carry forward, (limited) 2-year carry backward
Ireland	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- joint assessment of married couples	EUR 1 650; additional tax credits for Pay-As-You-Earn (PAYE) employees (EUR 1 650) depending on family situation	- 2 rates: 20 % 40 % - top marginal rate: 40 % (> EUR 33 800 (single), > EUR 42 800 (one income couple))	- universal Social Charge: 1.5 % to 8 % depending on income (11 % - top rate for self-employed)	NA	48 %/51 % for self employed > EUR 100 000	not included	included in general taxation	included in general taxation	33 % ordinary rate (with some exemptions and reliefs)	33 % ordinary rate (with some exemptions and reliefs)	withholding tax 20 %	41 % (Deposit Interest Retention Tax)	included in general taxation	yes, based on real expenses, capped	Yes	medical expenses, donations	3-year carry backward; unlimited carry forward
Italy	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation - possibility of joint declaration	progressive, 5 brackets: 23 % 27 % 38 % 41 % 43 % top rate: 43 % (> EUR 75 000)	- progressive, 5 brackets: 23 % 27 % 38 % 41 % 43 % - top rate: 43 % (> EUR 75 000)	- solidarity contribution: 3 % (> EUR 300 000); deductible	- 3.33 % (regional) + 0.9 % (local) (values given for Roma)	48.9 %	not included (only luxury owner-occupied dwellings are taxed)	included, optionally separate taxation at 21 % for some contracts at 15 % (10 %/or 2014-17)	included, optionally substitute taxation at 20 % exempt if kept more than 5 years	in case of qualified shares partially included in PIT, otherwise 26 %	in case of qualified shares partially included in PIT, otherwise 26 %	in case of qualified shares partially included in PIT, otherwise 26 %	26 % 20 %/or pension funds	26 % governments bonds are taxed at 12.5 %	yes, based on real expenses, capped	Yes	renovation and insulation works, child care, educational, sport, medical expenses, alimonies, donations, (cash registers for merchants)	5-year carry forward (+ losses of the 1st 3 activity years can be carried forward indefinitely)
Latvia	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation	EUR 900 (EUR 2 820 for pensioners) EUR 1 980 per child	- flat rate: 23 % - top marginal rate: 23 %	NA	NA	23.0 %	exempt	10 % 23 % (exempted if not related to business activity)	10 % 23 % (business activity)	15 % 2 % if non resident sells to entrepreneur, and owner-occupied generally exempt	10 % 15 %	10 %	0,1	corporate: 10 % 15 % government bonds: 0 %	yes (royalties 15-40 % of taxable income, income of sale of a standing forest 25 % of taxable income, income of selling timber 50 % of taxable income)	Yes, limited to 10% of taxable income (contributions to private pension funds)	education and medical expenses, alimonies, donations, social contributions and tax on real estate (if used in prof activity)	3-year carry forward
Lithuania	- worldwide income (resident) - domestic income (non-resident)	- separate taxation	EUR 3 480; EUR 720 per child earned income allowance (max. EUR 1 992), decreasing with income	- flat rate: 15 % - top rate: 15 %	NA	NA	15%	not included	NA	NA	exempted	0 % non shares up to EUR 3 000	specific exemptions	NA	NA	yes, in percentage OR based on real expenses	Yes, including to life insurance funds	education expenses	1-year carry forward
Luxembourg	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- joint taxation	EUR 11 264 (1st income bracket taxed at 0 % also child, spouse and extraprofessional allowances	- progressive: 19 brackets from 0 % to 40 % - top marginal rate: 40 % (> EUR 100 000)	- solidarity surcharge: 7 % or 9 % depending on income - Impôt d'équilibre budgétaire temporaire 0.5 %	NA	43.6 %	included	included	included	included	included	15 % (final withholding)	10 % (final withholding)	NA	lump sum OR based on real expenses	Yes	child care, alimony, loan interest, life insurance contributions	999-year carry forward
Malta	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	separate taxation married couple may opt for joint assessment or separate computation	- individual assessment: EUR 8 500; joint assessment: EUR 11 900; - parent: EUR 9 800 for specific provisions and variations pls consult TED8	- progressive: 15 % 25 % and 35 % - top marginal rate: 35 % (> EUR 60 000 (> EUR 7 800 for non-EU/EEA non-residents)	No	No	35%	not included	option of 15 % on gross rental income	included	NA	NA	35 % (creditable); non-residents: no (N.B.: full imputation)	15 % (final); non-residents: no (if no PE)	15 % (final); non-residents: no (if no PE)	yes, where necessarily incurred	No	alimony; child care, education, culture and sport expenses	can be set-off against other sources of income
Netherlands	- worldwide income (resident) - domestic income (non-resident)	separate taxation possibility to allocate income and deductions between fiscal partners	EUR 2 203 (max basic tax credit, decreasing with income) + EUR 1 042 for 60+ age dependent if income is not more than EUR 35 770; EUR 152 if income is more than EUR 35 770	- progressive: 36.5 % 42 % 52 % (I/P) - top rate: 52 % (> EUR 57 585)	NA	NA	52%	Base: standard rate of income (= percentage of the value of the property) minus mortgage interests	included	included	included	included	included; the dividend tax of 15% is creditable against PIT	included	included	No	Yes; contributions up to an income of EUR 100 000. EET-system (contributions are exempt; investment income and capital gains are exempt; benefits are taxed).	educational, medical, travel expenses; alimonies; fixed deduction of EUR 7 280 and 14 % of profits for not incorporated entrepreneurs	3-year carry backward; 9-year carry forward (Box 1) and 1-year carry backward; 9-year carry forward (Box 2), separately
Poland	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation - possibility of joint taxation	basic personal allowance PLN 3 091	- 18 % (PLN 3 091 to PLN 85 528) - 32 % (above PLN 85 528)	NA	NA	32%	not included	included in general taxation	included in general taxation	included in general taxation	included in general taxation	19%	0,19	0,19	yes, a lump-sum amount OR in percentage OR based on real expenses	Yes	obligatory social contributions, internet expenses, donations, expenditure on acquiring new technology	5-year carry forward
Portugal	- worldwide income (resident) - domestic income (non-resident)	- joint taxation, with family quotient (1 for taxpayers and 0.3 for dependants) - possibility to fill in a separate tax form	EUR 4 104 ; personal tax credit linked to min wage and family (I) EUR 325 per child; EUR 300 per old-age dependent (both taks credits)	- progressive: 14.5 % 28.5 % 37 % 45 % 48 % (non-residents: 25 %) - top marginal rate: 48 % (> EUR 80 000) (P)	- extraordinary surtax: 3.5 % (net income > min wage) - additional solidarity surcharge: 2.5 % (> EUR 80 000), 5 % (> EUR 250 000)	NA	56.5 %	not included	not included	included, or taxed separately at 28 %	included (base = 50)	28%	28 % (base reduced if resident) (P)	28 % (base reduced if resident) (P)	28 % (base reduced if resident) (P)	self-employed % OR real expenses; (immovable property) real expenses including tax	Yes	union fees, taxes (5 % VAT) deductible; child care, education, medical expenses, alimonies, donations are tax credits	12-year carry forward (limited to 75 % of profits)
Romania	domestic income (resident and non-resident)	- separate taxation	up to RON 250 (if gross monthly income less than RON 1 000 and no dependants) additional RON 100 for each dependant	- flat rate 16 %	NA	NA	16%	3 % up to RON 200 000; over RON 200 000, RON 6 000 + 2 % calculated at a value exceeding RON 200 000	16%	16%	3 % up to RON 200 000; over RON 200 000, RON 6 000 + 2 % calculated at a value exceeding RON 200 000 (2)	16%	16 % final withholding	16 % final withholding	16 % final withholding	No	Yes	No	annual tax losses can be carried over and offset against income from the same source for the following 5 fiscal years.
Slovakia	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation	EUR 3 803.33 (allowance depends on the minimum subsistence level and taxpayer's taxable income) also allowance for spouse on no or low income	- 19 % up to EUR 35 022.32 - 25 % above EUR 35 022.32	NA	NA	25%	included	included	included	included	included	not included	19 % (final withholding)	19 % (final withholding)	% income OR based on real expenses; cap for deductions in % of income	supplementary pension contributions (maximum EUR 180 per year)	voluntary contributions to the privately managed fully funded pillar are tax-deductible (maximum 2 % x 60 x average wage (t-2) per year)	4-year carry forward
Slovenia	- worldwide income (resident) - domestic income (non-resident)	- separate taxation	EUR 3 302.7 + depending on income (higher for low income) child: EUR 2 436.92 (increasing with rank); old-age dependent: EUR 2 436.92	- progressive: 16 % 27 % 41 % 50 % - top rate: 50 % (> EUR 70 907.2)	NA	NA	50.0 %	not included	not included (flat rate)	25%	from 25 % to 0 % (dep. on holding period)	from 25 % to 0 % (dep. on holding period)	25%	0,25	0	% income OR based on real expenses	Yes	donations, investments in eco-friendly or energy efficient goods special allowances for business income	indefinite carry forward (max. 50 % of the tax base)
Spain	- worldwide income of resident or spanish nationals posted abroad (or in tax havens) - non-resident: special law, mostly domestic income	- separate taxation - possibility of joint family taxation	individual: EUR 5 550; couple: EUR 3 400; children: EUR 2 400 to 4 500	- 5 rates, from 19.50 % to 46 % - top marginal rate: 46 % (> EUR 60 000)	No	- regional governments can implement their own tax schedule	46%	not included	yes	yes	yes	yes	20 % creditable withholding tax; 19.5 % applies since 12 July	20 % creditable withholding tax; 19.5 % applies since 12 July	20 % creditable withholding tax; 19.5 % applies since 12 July	yes, based on real expenses, capped (P)	Yes, also to life insurance funds	alimony; unions; national, regional or local taxes; investment in new companies etc	4-year carry forward
Sweden	- national and local income tax apply to income of residents - non-residents are taxed on domestic income under specific tax (optional)	- separate taxation	SEK 13 100 (up to SEK 34 300, depending on income) (I) + in-work tax credit of max SEK 26 486 / SEK 30 000 (State tax)	- 20 % 25 % - 20 % (SEK 430 200 - SEK 616 100) - 25 % (> SEK 616 100)	NA	- (additional local tax) 31.99 % (average)	57.0 %	not included	imputed rent (government borrowing rate) on assets taxed by 30 % (insurance endowments) or 15 % (pension endowment)	allowance for income up to SEK 40 000 per year for housing	22 % (can be deferred in case of property re-acquisition)	included in individual capital income tax	included in individual capital income tax	included in individual capital income tax	included in individual capital income tax	yes (real expenses)	Yes	travel expenses; household services; renovation works, etc. (50 % tax credit, capped)	indefinite carry forward
United Kingdom	- resident: worldwide income (subject to double-tax relief) - non-resident: domestic income	- separate taxation	basic personal allowance GBP 10 000 (higher for elderly marriage and married couple's allowances, dependent on income/ age; child tax credits, working (low-income) tax credits	- progressive 3 brackets 20 % 40 % 45 % - top rate 45 % (above GBP 150 000)	NA	NA	45%	included	included	included	18 % non net gains where below income tax basic rate threshold; 28 % thereafter	as above	progressive scale 10 % 37.5 % 42.5 %	20 % withholding tax	included	based on real expenses	Yes	child care, educational, medical and travel expenses, alimony, donations, union fees, loan interest	indefinite carry forward; 3-year carry backwards

10.3 Annex 3 – Main features of the tax systems: Corporate income tax⁸⁶

⁸⁶ This overview has been prepared based on the Eurostat publication “Taxation trends in the European Union”, 2015 edition (http://ec.europa.eu/taxation_customs/taxation/gen_info/economic_analysis/tax_structures/index_en.htm).

Corporate income tax systems	Tax rates						Tax base	Anti-avoidance				Allowance for Corporate Equity
	Country / Main features	Nominal corporate income tax rate	Central government surcharge	Regional government surcharge	Local government surcharge	Top CIT statutory rate (incl. surcharges)		Special tax rate for SMEs (all-in rate)	Limits to interest deductions	Transfer pricing rules	Controlled foreign company (CFC)	
Austria	25%	NA	NA	NA	25%	no	worldwide income	yes (financing costs related to acquisitions of participations within a group are not deductible; nor is interest paid to a related entity if taxed at less than 10 %)	yes, arm's length principle	no	no	no
Belgium	33%	3%	NA	NA	34%	24.98 % (income < EUR 25 000); 31.93 % (EUR 25 000 < income < EUR 90 000); 35.54 % (EUR 90 000 < income < EUR 322 500)	worldwide income	yes (thin cap rule of 5:1 debt to equity)	yes, arm's length principle	no	no	yes (notional rate 1.63 % for non-SMEs; 2.13 % for SMEs)
Bulgaria	10%	NA	NA	NA	10%	no	worldwide income	yes (thin cap rule of 3:1 debt to equity)	yes, arm's length principle	no	no	no
Croatia	20%	NA	NA	NA	20%	no	worldwide income	yes (thin cap rule of 4:1 debt to equity)	yes, arm's length principle	no	no	no
Cyprus	13%	NA	NA	NA	13%	no	worldwide income	yes (no interest deduction up to 7 years for the purchase of private vehicles and assets not used in business, except purchase of shares as from 2012 of directly or indirectly wholly owned subsidiary; no thin cap rules)	yes, arm's length principle	no	no	no
Czech Republic	19%	NA	NA	NA	19%	no	worldwide income	yes (arm's length test and thin cap rule of 4:1 debt to equity)	yes, arm's length principle	no	no	no
Danmark	23.5 %	NA	NA	NA	23.5 %	no	domestic income	yes (arm's length test and thin cap rule of 4:1 debt to equity)	yes, arm's length principle	yes	yes	no
Estonia	20%	NA	NA	NA	20%	no	worldwide income	no	yes, arm's length principle	no	no	no
Finland	20%	NA	NA	NA	20%	no	Worldwide income	yes (deductibility of interest on intra-group loans restricted to 25 % of earnings before interest, taxes, depreciation, and amortisation subject to certain safe harbours from 2014 onwards; no thin cap rules)	yes, arm's length principle	yes	no	no
France	33.33 % (standard rate)	NA	NA	NA	33.33%	15%	domestic income	yes (75 % of net interest charges for companies generating more than EUR 3 million of net interest expenses; thin cap rules, ratio and arm's length test)	yes, arm's length principle	yes	na	no
Germany	15%	0.825 %	NA	NA	15.825%	no	worldwide income	yes (deduction of interest up to a value of 30 % of earnings before interest, taxes, depreciation and amortisation)	yes, arm's length principle	yes	yes	no
Greece	29%	NA	NA	NA	29%	no	worldwide income (subject to double-tax relief)	yes (deduction of interest up to a value of 50 % of earnings before interest, taxes, depreciation and amortization (40 % from 1.1.2016 and 30 % from 1.1.2017))	yes, arm's length principle	yes	yes	no
Hungary	19 % (over HUF 500 M of the positive tax base) / 10 % (below this amount)	NA	NA	NA	21%	small business tax 16 % (special conditions e.g. 25 employees or less and revenue & BS below HUF 500 million)	worldwide income	yes (thin cap rule of 3:1 debt to equity)	yes, arm's length principle	yes	no	no
Ireland	12.5 % (on trading income) (25 % on non-trading income)	NA	NA	NA	12.5 %	no	worldwide income	yes (deductions wholly and exclusively for business purposes; some restrictions on related party payments and borrowing; no thin cap rules)	yes, arm's length principle	no	no	no
Italy	27.5 % (standard rate)	NA	NA	NA	27.5 %	no	worldwide income	yes (net interest expenditure is deductible up to a value of 30 % of earnings before interest, taxes, depreciation and amortization; no thin cap rules)	yes, arm's length principle	yes	no	yes (notional rate 4.5 % for tax year 2015)
Latvia	15%	NA	NA	NA	15%	9%	worldwide income	yes (no deductions for interest exceeding the lower of: 1.57 times the average short term credit rate; or thin cap rule of 4:1 debt to equity ratio)	yes, arm's length principle	no	no	no
Lithuania	15%	NA	NA	NA	15%	5%	worldwide income	yes (thin cap rule for loans from controlling parties: 4:1 debt to equity)	yes, arm's length principle	yes	no	no
Luxembourg	21%	7%		6.75 %	29.22 %	no	worldwide income	yes (no specific thin cap rules, but tend to use 85:15 debt equity ratio)	yes, arm's length principle	no	no	no
Malta	35%	NA	NA	NA	35%	no	worldwide income	no	no	no	no	no
Netherlands	first bracket: 20 % second bracket 25 % (above EUR 200 000)	NA	NA	NA	25%	no	worldwide income	from 2013 thin cap rules have been replaced by rules on interest paid on loans considered to finance participations. If these payments exceed EUR 750 000, they cannot be deducted from taxable profits. The Netherlands also have anti-base erosion provisions limiting deductibility of interest on loans relating to 'tainted' transactions. Deductibility of interest on 'acquisition debt' and hybrid loans is also restricted.	yes, arm's length principle	no	no	no
Poland	19%	NA	NA	NA	19%	no	worldwide income	yes (interest on loans is deductible up to the tax value of assets multiplied by the repo rate of the National Bank of Poland increased by 1.25 % Total tax deductible interest may not exceed 50 % of operational profit . Alternatively, taxpayer may opt for thin cap rule of 1:1 debt to equity)	yes, arm's length principle	yes	no	no
Portugal	21%	7 % (for profit before deduction of losses of over EUR 35M)	NA	1.5 %	29.5 %	17 % (for taxable profit up to EUR 15 000)	worldwide income	yes (maximum of 30 % of EBIT or EUR 1 million; no thin cap rules)	yes, arm's length principle	yes	no	yes (notional rate 5 %)
Romania	16%	NA	NA	NA	16%	no	worldwide income	yes (thin cap rule of 3:1 debt to equity)	yes, arm's length principle	no	no	no
Slovakia	22%	NA	NA	NA	22%	no	worldwide income	yes (deduction of interest up to 25 % of earnings before interest, taxes, depreciation and amortisation)	no	yes	no	no
Slovenia	17%	NA	NA	NA	17%	no	worldwide income	yes (thin cap rule of 4:1 debt to equity)	yes, arm's length principle	no	no	no
Spain	28%	NA	NA	NA	28%	25%	worldwide income	yes (net financial expenses deductible up to 30 % of operating profit, subject to maximum of EUR 1 million)	yes, arm's length principle	yes	yes	no
Sweden	22%	NA	NA	NA	22%	no	worldwide income	yes (Main rule limits deductibility for all loans between related parties. Exception if interest income related to expenses is taxable at rate of 10 % in the hands of the beneficial owner. Also 'business reasons exemption'. No thin cap rules.)	yes, arm's length principle	yes	no	no
United Kingdom	20%				20%	20 % ('Small Profits Rate')	worldwide income	yes (thin cap rules incorporated within transfer pricing rules; apply arm's length principle; worldwide debt cap restricts the deduction for financing expenses of large groups based on gross financing expenses of the worldwide group)	yes, arm's length principle	yes	no	no

10.4 Annex 4 – Main features of the tax systems: VAT rates⁸⁷

Country / VAT rates	Standard rate	Reduced rate(s)
Austria	20%	10%
Belgium	21%	6%and 12%
Bulgaria	20%	9%
Croatia	25%	5%and 13%
Cyprus	19%	5%and 9%
Czech Republic	21%	10 %and 15 %
Danmark	25%	NA
Estonia	20%	9%
Finland	24%	10%and 14%
France	20%	2.1 %(super-reduced rate), 5.5 % and 10 %
Germany	19%	7%
Greece	23%	6.5 %and 13 %
Hungary	27%	5 %and 18 %
Ireland	23%	4.8 %(super-reduced rate), 9 %and 13.5 %
Italy	22%	4 %(super-reduced rate) and 10 %
Latvia	21%	12%
Lithuania	21%	5 %and 9 %
Luxembourg	17%	3 %(super-reduced rate), 8 %and 14 %
Malta	18%	5 %and 7 %
Netherlands	21%	6%
Poland	23%	5 %and 8 %
Portugal	23%	6 %and 13 %
Romania	24%	5 %and 9 %
Slovakia	20%	10%
Slovenia	22%	9,50%
Spain	21%	4 %(super-reduced rate) and 10 %
Sweden	25%	6 %and 12 %
United Kingdom	20%	5%

⁸⁷ This overview has been prepared based on the Eurostat publication "Taxation trends in the European Union", 2015 edition (http://ec.europa.eu/taxation_customs/taxation/gen_info/economic_analysis/tax_structures/index_en.htm).

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