

In brief

A look at current financial reporting issues

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Investigations into 'state aid'

Issue

The European Commission (EC) has announced an investigation into whether certain income tax legislation and rulings of European Union (EU) member states constitute unlawful 'state aid'. State aid is an EC term that refers to forms of public assistance given to entities on a selective basis that has the potential to distort competition and affect trade. These developments and similar investigations of other jurisdictions might require consideration in the context of uncertain income tax positions.

Impact

Management should assess the accounting impact of new developments at each reporting date, including the impact of local and international court decisions. The accounting consequences of such investigations, based on available information, are likely to be in the scope of IAS 12, '*Income taxes*'.

Management should assess the potential effect on existing uncertain income tax positions, as well as amounts owed for previously closed periods and possible refund claims or positions to be taken in the future. IAS 12 measurement principles should be applied to uncertain tax positions, with current tax liabilities (assets) measured at the amount expected to be paid to (recovered from) the taxation authorities.

Management should also consider additional disclosures. IAS 12 (by reference to IAS 37, '*Provisions*') requires disclosure of tax-related contingencies for which no provision has been made but where the likelihood of an obligation arising is more than remote. IAS 1 requires disclosure of sources of uncertainty which apply to estimates made in the measurement of current tax liabilities.

Insight

These developments result from the interpretation of competition and antitrust laws by the EC and Court of Justice of the European Union, in conjunction with the application of income tax laws or the taxing authority administration. Judicial decisions that find existing arrangements to represent unlawful state aid could result in tax liabilities for prior years including those closed for tax purposes, unless the aid is qualified as 'existing aid' or previous Commission actions or communication have given rise to legitimate expectations that the aid was lawful. The authority for such a review and final EC decisions might support repayment of tax benefits going back ten years. For more information, see [EU Fiscal State aid – a briefing document](#).

It might be challenging to evaluate the potential financial reporting implications of these developments. Management will need to identify developments that might affect the entity, assess the technical merits of any potential claims, quantify the exposure, and consider accounting and disclosure consequences. Management might need outside assistance to support its assessments.



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