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What if IAS/IFRS were a Tax Base? New Empirical Evidence from an Austrian Perspective.

Working Paper

Institut für Revisions-, Treuhand- und
Rechnungswesen

WIRTSCHAFTS
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Working Paper Nr. 1

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Abstract

In particular in Germany and Austria, but also in other countries, extensive theoretical and analytical research has been published on the potential tax effects in case IAS/IFRS were used as the basis for corporate taxation. Very few quantitative papers exist. This motivated us to conduct a study that quantifies the actual effects of a potential decisiveness of IAS/IFRS for the national tax base - without further questioning the usefulness of an IAS/IFRS relevance. Our paper extends existing research substantially. The research question of our paper deals with the measurement of differences in discounted tax burden in different scenarios, by simulation. Our sample comprises original data of 61 Austrian companies. The median of the difference between book values of IAS/IFRS single accounts and tax accounts for specific balance sheet items is determined. We then apply the result on the items of a typical corporate account derived from an Austrian database. As a result, depending on the term of items, we can calculate the discounted tax effects for different scenarios. It must be underlined that such highly confidential and detailed tax data is usually not available to researchers. The main preliminary finding of our empirical survey is that only in few cases we find essential differences between IAS/IFRS and tax accounts. Our evidence suggests that no dramatic change in the tax base has to be expected. Our study provides not only new empirical evidence but also a basis for further research on a possible common consolidated corporate tax base from an academic perspective.

Contents

1 Introduction

In many countries, there is a strong 'tax link' between commercial accounting and tax accounting, e.g. in Sweden, France, Spain and also Switzerland (Arbeitskreis "Steuern und Revision" im BWA 2004). The strongest tax link can be found in Austria and in Germany (given the common roots in tax history). Changes in commercial accounting such as its internationalization therefore have immediate effect on the tax burden.

Recently, an increasing degree of attentiveness can be observed in European countries towards the question of what would happen to the discounted tax burden if IAS/IFRS were the authoritative basis for taxation. Two reasons can be identified:

- The 'internationalization'[2] of financial reporting proceeds continuously. For a number of years, the group financial statements of multinational firms in Europe have frequently followed either the US Generally Accepted Accounting Principles (US GAAP) or the International Accounting Standards/International Financial Reporting Standards (IAS/IFRS) (Zorn 2003). The EC regulation[3] provides for the mandatory use of the IAS/IFRS in group accounts of listed companies in the European Union. In addition, it offers the option for the Member States to provide for the use of IAS/IFRS in the group accounts of non-listed companies and in individual accounts. So far, Germany and Austria have implemented the use of IAS/IFRS only for the group accounts of listed companies, but it can easily be imagined that sooner or later the international standards for financial reporting will dominate individual accounts - either as a consequence of national or European legislation or as a matter of fact (Arbeitskreis Externe Unternehmensrechnung der Schmalenbachgesellschaft für Betriebswirtschaft 2001; Gassner 2003; Zorn 2003).[4] Unless the tax law were changed, this results in an effect on the tax base in countires with a tax link.
- Recently, the EC Commission has given additional impetus on the discussion by identifying IAS/IFRS as a starting point for the determination of taxable group profits (European Commission 2003).[5] Given that European groups have to present IAS/IFRS consolidated annual statements, the thought was near to use them as a basis for a possible future common consolidated corporate tax base.

The academic discussion on the link between IAS/IFRS and income taxation has been extensive during the last years, in particular in Austria and Germany (Schreiber 1997, 2000; Thiele 1997;

[2]This article refers to the 'internationalization' of financial reporting, international financial reporting and international annual accounts. These terms are an imprecise appellation that was chosen to refer to the principles of the IAS/IFRS and the US GAAP (see text). These principles tend to provide for methods of valuation that can be compared to the principles of the Austrian and German financial reporting standards.

[3]Regulation (EC) No. 1606/2002 (OJ L No. 243, 11 September 2002) (IFRS Regulation).

[4]The Schmalenbachgesellschaft für Betriebswirtschaft (Institute for Business Research) proposed the use of IAS/IFRS for individual accounts.

[5]Meanwhile, the plan has been abandoned.

Herzig and Dautzenberg 1998; Rahlf 1999; Eberhartinger 2000; Ditz 2001; Buchholz and Weis 2002; Drescher 2002; Bertl 2003). Some authors also tried to quantify the possible effect for enterprises (Oestreicher and Spengel 1999a; Eberhartinger 2003; Spengel 2006).

The present study is dedicated to the financial consequences of an IAS/IFRS tax link for an enterprise. In this context, the following issues are of importance:

- The study is limited to Austria. This is due to two facts:
  - On the one hand, it is related to income tax law which by nature (still) is within national sovereignty.
  - On the other hand, the data used is singular and it is available for Austria only.
- The study is based on two sets of data:
  - Empirical data on the typical balance sheet structure of Austrian enterprises of different sectors.
  - Data from a survey carried out by the authors on the differences in the measurement of assets and liabilities between IAS/IFRS, commercial law and income tax law, for individual enterprises. This data is - to our knowledge - unique in research, not only in Austria, but also from an international perspective. The data is highly confidential and usually not available for scholars. Therefore, the study focuses on the *actually observed* (not the supposed) differences in measurement.

The result will show the relative gain or loss in interest due to timing differences in tax payments.

As a consequence of 'less prudent' accounting principles under IAS/IFRS, the general assumption in practice is that profit will arise at an earlier stage, not only compared to Austrian commercial accounts, but also compared to tax accounts. Therefore a loss in interest, resulting from the requirement to pay taxes earlier, is generally expected (Mayer-Wegelin 1999; Glaum 1998). In particular enterprises and their lobbying industry stress that perceived disadvantage. However, other studies show that the effect might be low (Spengel 2006; Eberhartinger 2000). This paper shall shed some more light on the actual effect to be expected.

It must be underlined that analyzing the consequences of IAS/IFRS being the basis for taxation does not coincide with supporting that idea. In contrast, as will be shown in section 3 below, the authors share the predominant view that IAS/IFRS are not suitable for taxation.

2 Determination of Taxable Profit in Austria

The relationship between financial accounting and taxation is characterized by the German term 'Maßgeblichkeitsprinzip', a word which has been translated into the English language as 'authoritative principle' (Seckler 1995; Pfaff and Schroer 1996; other translations: 'congruence principle', Walton 1995, Haller 1992; also: 'principle of decisiveness', McCourt and Radcliffe 1995). It indicates a very strong link, indeed the strongest within the EC, between the financial and the tax report.

The Maßgeblichkeitsprinzip is enacted in § 5 (1) of the Austrian Income Tax Act. It determines the taxable income of traders that draw up annual accounts (including companies) according to the required accounting principles (Grundsätze ordnungsmäßiger Buchführung). In practice, this means that commercial measurement is authoritative for taxation. Thus, the prudence principle which is predominant in accounting, finds its way into the determination of taxable profit.

Only in cases where tax law prescribes mandatory rules which deviate from accounting practices applied in the financial report, the accounting practices chosen for financial reporting must be adapted in order to meet the tax requirements. Austrian tax law differs from commercial accounting only in a few specific cases. Such examples for mandatory tax law provisions are:

- Capitalization of overhead cost as part of production cost,
- Mandatory capitalization of acquired goodwill[6],
- Straight line depreciation,
- Useful life of acquired goodwill is 15 years, useful life of cars is 8 years, stipulated useful lives for buildings (depending on their use, refutable),
- Amount deductible for pension plans, for future severance payments and for future anniversary payments is restricted,
- Measurement of (other) provisions is restricted (no flat calculation; undiscounted long term provisions at 80%); however, provisions for onerous losses are admitted.

The fact that financial reporting is relevant for taxation, leads as a direct and logical consequence to the 'umgekehrte Maßgeblichkeit', the reversal of the authoritative nature of financial statements for tax accounts. The 'umgekehrte' (reverse) Maßgeblichkeit describes the retroactive effect of tax computation on financial statements. Where the accounting treatment in the financial statements directly affects the tax position of the company, it leads to a subordination of accounting policy to tax considerations (also named 'financial conformity'). As a result,

[6]In financial reporting as well as in taxation the capitalization of internally generated intangible assests (incl. internally generated goodwill) is prohibited.

the above listed mandatory tax rules are also used in the commercial accounts. Furthermore, certain tax incentives for investment have to be accounted for in the commercial accounts.[7] Consequently, the majority of Austrian enterprises draw up one set of accounts that serves for both purposes ('Einheitsbilanz') (Bertl/Greimel/Kostermann 2004). In the few cases where this is not possible, an arithmetical off balance sheet reconciliation is made.

The purpose of the authoritative principle can be seen primarily in simplifications. As financial accounting fulfils the requirements of tax law to a great extent, a separate tax accounting independent of financial accounting is dispensable in the view of the historical legislation (Gassner/Hofians/Karner 1987). Uniform accounting leads to cost savings for entrepreneurs; moreover, a detailed codification of tax law is not necessary (Pokorny 1987). The arguments against the relevance of financial reporting for taxation are numerous (Eberhartinger 2000). Most of them are based on the fact that the purpose of both determinations is completely different, which must lead to different principles and rules. Furthermore, the aforementioned reverse effect of tax considerations on the financial accounts is frequently mentioned. These arguments gain weight when considering IAS/IFRS, as will be shown.

[7] In Austria, however, the number of cases where this is necessary has been consequently reduced to the " 'roll-over-relief' only (§ 12 ICTA).

3 IAS/IFRS as a Tax Base

The discussion on whether IAS/IFRS are appropriate as a basis for taxation, has been very intense in the past, in particular in German and Austrian literature - obviously because those two countries are mostly involved.

The one strong argument in favour of using IAS/IFRS for taxation is - again - simplification. For reporting as well as for taxation, an economic profit has to be determined. Why not use one common profit that might be adapted to each purpose and thus save compliance costs. At present, enterprises being part of a group which draws up its accounts according to IAS/IFRS, cannot benefit from such cost savings. IAS/IFRS as a basis for taxation would render such cost savings possible. However, the arguments against taxation according to IAS/IFRS are numerous.

The pros and cons have been considered in-depth in numerous articles and books (apart from the literature mentioned in the introduction above, the following can be named: Wagner 1998, 2000; Hennrichs 1999, 2005; Treptow 1999; Euler 2000, 2002; Herzig 2000; Heyd 2001; Kirchhof 2000; Sigloch 2000, 2004; Kahle 2001, 2003, 2006; Kußmaul and Klein 2001; Freedman 2004; Herzig and Hausen 2004; Schön 2005a; Eberhartinger 2005; Jensen-Nissen and Lochmann 2006; Spengel 2006). Many of them are of German or Austrian origin, which is not surprising, considering the close tax link in those countries. The purpose of this paper is not a comprehensive discussion of all the pros and cons. Only the main arguments against using IAS/IFRS for taxation shall be named.

First of all, a difference in objectives can be identified. The objective of financial statements according to the IASB Framework and according to IAS 1[8] is to provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users in making economic decisions. Therefore, the Framework does not necessarily apply to special purpose financial reports such as, among others, reports to tax authorities. Tax accounts, in contrary, are meant to serve the need for fair and equal income taxation. The fisc, which is able to gather information about the enterprise by the comprehensive right to audit any detail, is not in need of financial statements as a means of information. From this difference in objectives, several differences in recognition and measurement arise.

One of the most striking arguments is the increasing importance of fair values under IAS/IFRS (Wagenhofer 2006). Their possible definition as 'the price that *would be* received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in the market in which the reporting entity transacts'[9] shows that the data underlying the measurement is rather vague in many cases. Apart from doubts on the appropriateness of fair values in financial

[8] Also in the suggestions according to Exposure Draft of Proposed Amendments to IAS 1 Presentation of Financial Statements: A Revised Presentation (March 2006).

[9] See SFAS No. 157 Fair Value Measurements and IASB Meeting March 2006 on the Fair Value Measurements Project (convergence project with the FASB); emphasis added.

reporting, it is obvious that they are not appropriate for taxation, for two reasons:

1. On the one hand, the objectivity of fair values is not always sufficient for taxation in order to guarantee equality,
2. On the other hand, the possible measurement of assets at fair values above historical cost, provided the difference in values is included in the profit and loss account, would lead to the taxation of unrealised profits.

Both issues constitute a breach of major principles of income taxation.

Furthermore, legal and political arguments against IAS/IFRS as a tax base exist. On the one hand the constitutionality of using standards set by a multinational, democratically not legitimated body for taxation is more than doubtful (Hennrichs 2005; Van Hulle 2004; Weber-Grellet 2003).[10] On the other hand, one can assume that the political will to surrender parts of fiscal sovereignty to the IASB is limited. Additionally, one must say that IAS/IFRS in their present state, notwithstanding efforts to establish IAS/IFRS for enterprises that are of no public interest, are not suitable for SME´s (Ballwieser 2006; Kußmaul and Henkes 2006; Niehus 2006; Ochs and Leibfried 2006).

To sum up: also to the authors' conviction, the use of IAS/IFRS as a basis for taxation is not appropriate. Nevertheless, the question of the monetary consequences for an enterprise in case the authoritativeness would still be implemented arises.

[10]Even if considering the Comitology Procedure.

4 Design of the Study

The objective of the following analysis is to discuss the change in discounted tax burden if IAS/IFRS were relevant for taxation. The discounted tax burden under present Austrian income tax rules is compared to the discounted tax burden that would arise under IAS/IFRS relevance.

1. Starting point is the **typical Austrian balance sheet structure** for three sectors. It gives a picture of the weight of each balance sheet position in the financial report (cp. chapter 4.1).

2. Each balance sheet position is multiplied by an '**IFRS-factor**' and a '**tax-factor**', which converts the commercial balance sheet to an IAS/IFRS statement and an income tax statement respectively. The factors reflect the changes in measurement in the different settings. They are derived from a survey, which includes the individual commercial accounts, the individual tax accounts and the individual IAS/IFRS accounts of 61 Austian enterprises (cp. chapter 4.2). As such, it is possible to compare the statements.

3. In our study we assume that a change in measurement leads to a change in profit and - if relevant - to a change in tax burden. If, for example, the value of provisions under IAS is lower than the value according to income tax law, profit and tax will be higher in the respective year. The **tax effects of each change in measurement**, however, depend on the specific case under review and on the scenario chosen.

4. Furthermore we assume that each change in measurement is revoked as soon as the respective item is taken from the balance sheet (use, sale, etc.). This assumption is justified by the fact that at the end of the day, irrespective of earlier measurement, cash flows remain unchanged. The discounted tax burden therefore depends on the **term** of the item (cp. chapter 4.3). For this reason the net present value of the tax advantage/disadvantage is calculated.

5. In how far each change in measurement and its revocation actually lead to tax consequences depends on the **scenario** chosen (cp. chapter 4.4).

4.1 Typical Austrian Balance Sheet Structure

The typical statement is derived from the data made available by the Austrian Institute for SME Research together with the Austrian National Bank.[11] This data is presented in form of the median, the upper and the lower quartile of balance sheet ratios of 73.141 enterprises in total. The data includes 15.364 enterprises of the sector 'D. Manufacturing', 222 enterprises of the sector 'E. Utility'[12], and 23.163 enterprises of the sector 'G. Wholesale and Retail Trade; Repair

[11] http://www2.oenb.at/tridion/jakz/jahresabschlusskennzahlen_auswahl.php?contenturl=/de/stat_melders/datenangebot/realwirtschaft/jahresabschlusskennzahlen/jahresabschlusskennzahlen_navigation.jsp.

[12] Electricity, Gas and Water Supply.

of Motor Vehicles, Motorcycles and Personal and Household Goods' in 2001.[13] The sectors (Manufacturing; Wholesale and Retail Trade; Utility) are selected according to the sectors that were well represented in our sample.

The data cover all sizes and all legal forms.

- The differentiation according to the size of enterprises is included in the data available and will also be included in the simulation below.[14]
- A differentiation according to legal form (in particular partnerships vs. corporations) is in contrast not available and therefore not included in the simulation below. However, it can reasonably be assumed that it is not relevant for the results of the study since according to Austrian law differences in measurement apply to all legal forms equally.

From the balance sheet ratios the typical balance sheet structure in %

$$\left(e = \sum_{k=1}^{12} b_k\right)$$

can be deduced (see Table 1).

Specific attention shall be given to financial assets, given their potential for fair value accounting. The data above shows: little relative importance of financial fixed assets (around 1% of the total) and some relative importance of other current assets, including financial current assets (between 13 and 25%). The data above gives no information on derivatives off balance sheet.

[13] Classification according to ÖNACE.

[14] Micro: sales $\leq$ 1 mio €; small: 1 mio € $\prec$ sales $\geq$ 7 mio €; medium: 7 mio € $\prec$ sales $\geq$ 40 mio €; large: 40 mio € $\prec$ sales $\geq$ 100 mio €; very large: sales $\succ$ 100 mio €.

		Enterprises, all Sizes, Median, in %		
		Utility 2001	Manufacturing 2001	Wholesale and retail trade 2001
ASSETS				
b_1	**Intangible Fixed Assets**[a]	6,79	2,56	2,49
b_2	**Tangible Fixed Assets**	59,16	35,58	18,51
b_3	**Financial Fixed Assets**	1,48	1,76	0,8
	Current Assets	25,79	57,55	75,71
b_4	Inventories	2,18	17,27	33,05
b_5	Receivables	7,4	16,81	12,66
b_6	Cash	3,2	3,25	4,38
b_7	Other Current Assets	13,01	20,22	25,62
b_8	**Accrued Expenses**	6,78	2,55	2,49
LIABILITIES				
	Provisions	-7,58	-7,68	-5,1
b_9	Pension Liability and Other Long Term[b]	-4,19	-5,43	-2,75
b_{10}	Short Term	-3,39	-2,25	-2,35
b_{11}	**Liabilities**	-28,14	-56,25	-65,23
	Bank Liabilities	-23,7	-46,47	-46,38
	Accounts Payable	-4,44	-9,78	-18,85
b_{11}	**Other Liabilities and Accrued Income, Other Liabilities**	-31,72	-25,04	-24,39
b_{12}	Revaluation Reserve	-0,00	-0,00	-0,00
e	**Equity incl. Reserves**	32,56	11,03	5,28
	TOTAL	100	100	100

[a]'Other assets' in the ratios provided by the OeNB includes not only accrued expenses, but also intangibles. Since differences in the capitalization rules for intangibles might be material, we decided to split the 'other assets' between its two constituents at a ratio of 1:1. As it turns out in the simulation, this simplification does not bias the result.

[b]For Austria, this includes liabilities for severance payments mandated by law. Their importance is declining due to a recent change in law.

Table 1: Typical Austrian Balance Sheet Structure

Variable	Description
e	Equity
b_k	Balance Sheet Item, $k \in \{1, ..., 12\}$

Table 2: Descriptive Statistics of Key Variables

4.2 IFRS-Factor, Tax-Factor

Each of the above shown balance sheet items is multiplied by an IFRS-factor f_{ik} and a tax-factor f_{tk}. The respective factor converts the item (according to commercial accounting) to an item according to IFRS-measurement or tax-measurement respectively. The example of tangible fixed assets shows:

	b_k	f_{ik}	$b_k f_{ik}$	f_{tk}	$b_k f_{tk}$
Tangible Fixed Assets	59,16	1	59,16	1,05	62,12

The factors have been derived from a sample survey. The sample includes 61 Austrian enterprises (some of them are part of a group) of different sizes. For each enterprise, the anonymized

- individual commercial accounts,
- individual IAS/IFRS-accounts (as available for consolidation) and
- individual tax accounts (usually derived from deferred tax calculations and from tax reconciliations)

were made available by several offices of one large auditing and consultancy firm in Austria. The relative differences in the measurement of the balance sheet items as shown above have been collected. The median for each balance sheet item is defined as the relevant f_{ik}/f_{tk}. The median has been chosen because of non-normality of the data:

$$f_{ik} = \begin{cases} \left(\frac{b_{k,ias}}{b_{k,hgb}}\right)_{\frac{(n+1)}{2}} & for\ n\ odd \\ \frac{1}{2}\left(\left(\frac{b_{k,ias}}{b_{k,hgb}}\right)_{\frac{n}{2}} + \left(\frac{b_{k,ias}}{b_{k,hgb}}\right)_{\frac{n}{2}+1}\right) & for\ n\ even \end{cases}$$

$$f_{tk} = \begin{cases} \left(\frac{b_{k,tax}}{b_{k,hgb}}\right)_{\frac{(n+1)}{2}} & for\ n\ odd \\ \frac{1}{2}\left(\left(\frac{b_{k,tax}}{b_{k,hgb}}\right)_{\frac{n}{2}} + \left(\frac{b_{k,tax}}{b_{k,hgb}}\right)_{\frac{n}{2}+1}\right) & for\ n\ even \end{cases}$$

with

$b_{k,ias}$ ... value of balance sheet item k according to IAS/IFRS
$b_{k,tax}$ ... value of balance sheet item k according to Austrian Income Tax Act
$b_{k,hgb}$ ... value of balance sheet item k according to Austrian Commercial Code (HGB)
$k \in \{1, ..., 12\}$, covering the balance sheet items
n ... sample size per balance sheet item

It shall be underlined that the data is unique. Such detailed data on commercial, international *and* tax accounts of individual enterprises is usually not available. Data bases usually cover only one of the three frameworks. Furthermore, disaggregated (tax) data is highly sensitive and usually not available to researchers. The data therefore allows observing *actual* changes in measurement, as opposed to assumptions. To our knowledge, such a study has not been conducted yet.

Panel A: Economic Activities represented in the Sample

Sector	Representation
Manufacturing	62,30%
Utility	4,92%
Construction	1,64%
Wholesale and Retail Trade	9,84%
Real estate, Renting and Business Activities	6,56%
Other Public and Personal Services	14,75%

Panel B: Distribution of the Size of Enterprises in the Sample

Size of Enterprise[a]	Representation
Medium	14,75%
Small	45,90%
Large	39,34%

Panel C: Distribution of Legal Forms in the Sample

Legal Form	Representation
GmbH	67,21%
AG	11,48%
KG	21,31%

[a]acc. to § 221 Austrian Commercial Law

Table 3: Description of Sample Data

Even though the number of enterprises included in the sample is not very large, due to the difficult access to the data, we consider the results of our study to be valid. In particular the little variance in the factors f_{ik}/f_{tk} (1^{st} and 3^{rd} quartiles) justifies that consideration.

The statements were taken from the latest year available for each enterprise. Per enterprise, all three statements relate to the same year, of course.

When determining the factors f_{ik}/f_{tk}, no distinction between sizes, sectors or legal forms has been made. The sample size does not allow for a distinction between sizes or sectors.

- A distinction between legal forms is not relevant, because the adoption of IAS/IFRS as well as the determination of taxable profit (if double bookkeeping exists) do not differ according to the legal form.
- A differentiation of the factor f_{ik} according to size might be relevant, since it can be

reasonably assumed that accounting choices (commercial code vs. IAS/IFRS) depend on the size of the enterprise. A differentiation of the factor f_{tk} according to size might also be relevant. It has been shown empirically that smaller enterprises tend to have very little differences between tax accounts and commercial accounts (Einheitsbilanz) (Bertl/Greimel/Kostermann 2004).

- A differentiation according to sector might be relevant for certain balance sheet items, in particular for inventories or receivables.

Insurance companies, banks, other financial institutions, as well as charitable institutions are not included in the sample.

The difference between the factors f_{ik} and f_{tk} for each item can be seen in Table 4.

		$f_{ik} - f_{tk}$		
Balance Sheet Item	n	Lower Quartile	**Median**	Upper Quartile
Intangible Fixed Assets	43	0%	**0%**	0%
Tangible Fixed Assets	52	0%	**0%**	3%
Financial Fixed Assets	44	0%	**0%**	2%
Inventories	39	0%	**0%**	0%
Receivables	58	0%	**0%**	1%
Other Current Assets	2	0%	**0%**	0%
Cash	58	0%	**0%**	0%
Accrued Expenses	42	0%	**0%**	0%
Pension Liability and Other Long Term[a]	47	86%	**32%**	30%
Short Term Provisions	61	-51%	**-11%**	0%
Other Liabilities, Accrued Income	60	0%	**0%**	5%
Revaluation Reserve (and similar)	7	3%	**5%**	10%

[a]For Austria, this includes liabilities for severance payments mandated by law, see above.

Table 4: Median Values for each Balance Sheet Item

The table gives rise to several remarks:

- Obviously, n differs and hardly ever reaches the number of 61. This is due to the fact that not all enterprises show all balance sheet items.

- The table clearly shows the tendency towards avoiding differences between commercial/tax statements and IAS/IFRS statements, as far as assets are concerned. The differences in measurement are small in most cases, the variance reflected in the upper and lower quartile is very low. The result of zero has the highest frequency for most assets. Only in singular cases, outliers can be observed, e.g. within intangible and tangible fixed assets because of changed useful lives. Here the differences range between -250,02% and +267,71%. Extreme differences (e.g. -246,51%) in the value of financial fixed assets between commercial/tax statements and IAS/IFRS statements can be traced back to the measurement above cost via reserve. The few outliers that have been detected amongst inventories and receivables (e.g. -73,28%; +61,11%) are due to the use of the percentage of completion method.

- Differences in measurement such as higher measurement of production cost, longer useful lives of fixed assets, higher measurement using the percentage of completion method, additional capitalization of intangibles, or similar, are irrelevant in practice.

- Neither are differences in the useful lives of ppe of relevance. This is due to the fact that Austrian income tax law usually does not mandate useful lives[15], enterprises therefore have some discretion to bring the useful lives for tax purposes and for reporting purposes in line. This notion is underlined by little or no variance, as represented by the upper and lower quartiles.

- For pension liabilities and for other provisions, material differences in measurement cannot be avoided.

  - Very restrictive tax rules for pension liabilities meet rather liberal IAS rules.

  - Rather liberal tax rules for other long term and short term provisions (based on conservative commercial accounts) meet the restrictive IAS rules.
    The prevalent *Einheitsbilanz* (tax accounts equal commercial accounts) that has been mentioned before cannot be maintained for liabilities, as soon as IAS/IFRS are introduced.

- It can be observed that only in two cases other current assets (in particular securities held for trading) are shown in the balance sheet. It seems that though the implications of measurement at fair value of securities held for trading might be large, the weight of such assets is rather small. Nevertheless, since $n = 2$ is far too small for a sample, it must be assumed that no change in measurement takes place.

- In certain cases, according to IAS/IFRS, measurement at fair value is admissible only if the amount above cost is shown in a revaluation reserve. In Table 4 the reserve is expressed as a percentage of fixed assets according to IAS/IFRS. Since such measurement is not allowed under Austrian accounting and tax law, the factors cannot be appropriately calculated. Also here, $n = 7$ is too small.

- Our sample therefore shows negligible importance of fair value measurement above cost of financial instruments. This is consistent with recent empirical evidence from Germany (Küting 2007). According to this analysis, fair values do not play a major role in financial

[15]This might constitute a major difference to Germany, where the useful lives are fixed by the tax authorities as a rebuttable presumption.

accounts of German listed companies. It is reasonable to assume similar accounting behaviour for non listed companies in Austria. The simulation might lead to different results if enterprises with substantial financial current assets were included.

4.3 Term

In our study we assume that each change in measurement is revoked at a certain time in the future. As a consequence the maturity of each balance sheet item is especially important. Differences in maturity can be dealt with in a net present value calculation. The following distinction has been made:

- Long term: fixed assets, revaluation reserve, pension liabilities, and other provisions;[16]
- Short term: current assets, other liabilities and accrued income.

The classification is in line with the observations in the survey. The simulation assumes long term to be 10 years and short term to be 1 year.

The assumption of 10 years for long term assets and liabilities is the result of a major simplification. The term of fixed assets can vary between approx. 2 and 50 or more years, depending on the type of fixed assets (e.g. more IT-equipment or more real estate) and on their remaining useful life (old or new). The term of long term liabilities, in particular of pension liabilities can vary between very short term and 30 or more years, depending on the age of the employees, the duration of their contracts, and the fluctuation. The data available did not allow for a detailed analysis of the term of assets and liabilities. To our knowledge, empirical data on the question does not exist. We therefore chose 10 years as a matter of simplification.

4.4 Tax Effects of Each Change in Measurement

The survey we conducted also includes an analysis of the legal reasoning behind every change in measurement. This is important for the determination of the tax effects of the different scenarios (see Table5).

[16] The survey showed that the 'other provisions' are predominantly long term.

Reason	Description
A	Changed Useful Life of Fixed Assets
B	Recognition; additional / dropped out Recognition of Assets or Liabilities (e.g. Intangibles, Interest)
C	Measurement (e.g. Percentage of Completion, Construction Cost, Provisions)
C1	Measurement above Cost, via Reserve (e.g. most Financial Fixed Assets)
C2	Measurement above Cost, via Profit and Loss (e.g. certain Immovable Property)
Reclassification	

Table 5: Legal Reasoning behind Changes in Measurement

Furthermore, the Austrian concept of 'Maßgeblichkeit' has been categorized according to the different possible deviations/non-deviations of the measurement of balance sheet items between commercial law and tax law (see Table 6). Such categorization is needed in order to define the different scenarios below.

Category	Description
1	Reverse Maßgeblichkeit: Tax deductibility of certain investment allowances is only admitted when the item is provided for in commercial accounts as well (untaxed reserves)
2	No Maßgeblichkeit: Imperative deviation of tax values from commercial values due to mandatory tax law (e.g. non-deductibility of certain expenses, of certain provisions); bringing commercial values in line with tax values *is not* possible due to restrictive commercial law
3	No Maßgeblichkeit: Imperative deviation of tax values from commercial values due to mandatory tax law (e.g. non-deductibility of certain expenses, of certain provisions); bringing commercial values in line with tax values *is* possible due to liberal commercial law (e.g. most provisions, certain useful life), de facto Reverse Maßgeblichkeit
4	Unrestricted Maßgeblichkeit: Tax values follow commercial values (e.g. measurement of assets in most cases)

Table 6: Different Types of Measurement

The survey shows that category 3 and 4 dominate for all balance sheet items, except of course for untaxed reserves (category 1).

Scenarios

The simulation is carried out for three different scenarios:

- Scenario 1:
  $taxable\ profit = IAS/IFRS\ profit$
  IAS/IFRS are fully and without any restriction relevant for taxation. This includes all above mentioned reasons A, B, C, C1, C2[17] and the above mentioned categories 3 and 4. Scenario 1 therefore is rather hypothetical, given the broad consensus that unrealised gains shall not be taxed.

- Scenario 2:
  $$\begin{aligned} taxable\ profit &= IAS/IFRS\ profit \\ &\quad - unrealised\ gains\ included\ in\ profit \end{aligned}$$
  IAS/IFRS are relevant for taxation except for all cases where measurement above historical cost is involved, since taxation of unrealised profits constitutes a breach of core tax principles. Reasons A, B, C and categories 3 and 4 are covered.

- Scenario 3:
  $$\begin{aligned} taxable\ profit &= IAS/IFRS\ profit \\ &\quad - unrealised\ gains\ included\ in\ profit \\ &\quad \pm other\ adjustments\ according\ to\ tax\ law\ currently\ in\ effect \end{aligned}$$
  IAS/IFRS are relevant for taxation under the assumption that the present mandatory tax rules are maintained. Reasons A, B, C and only category 4 are included. If IAS/IFRS were considered for taxation at all, the 3^{rd} scenario seems to be the most realistic scenario. It seems unreasonable to assume that the fisc will give up all existing tax rules for the benefit of IAS/IFRS (rather in the contrary).

Those three scenarios are simulated by applying the IAS/IFRS-/tax-factor (median) to the balance sheet items.

In all scenarios, untaxed reserves are maintained. Untaxed reserves in Austria reflect tax allowances for certain investments, they are the result of fiscal policy. It is assumed that fiscal policy is not affected by the way in which taxable profit is determined. On- or off-balance sheet, fiscal policy will not cease to exist and it is not influenced by a possible relevance of IAS/IFRS statements. Therefore, category 1 will not be considered further.

Additionally, the three scenarios are simulated a second time under worst-case assumptions.[18] The assumption is that for the enterprise, measurement under income tax rules is to its advantage (lower quartile for assets, upper quartile for liabilities) and that the measurement under IAS/IFRS rules turns to its disadvantage (upper quartile for assets, lower quartile for liabilities).

[17] Reason C2 has actually never been observed in the sample.
[18] Worst case seen from the perspective of the taxpayer.

5 Simulation

For each balance sheet item, 6 scenarios for enterprises in total and by size and sector have been simulated. The simulation is carried out under the assumption that tax effects arise immediately, it is therefore assumed that the enterprise shows a taxable profit. The indexes u, $u \in \{1, 2, 3\}$, for each scenario, and v, $v \in \{1, 2\}$, for each simulation according to size/sector will not be included in the following formulation for reasons of simplification.

The difference between the present and the discounted future tax burden for each balance sheet item is given by:

$$T_k = (f_{ik} - f_{tk}) \cdot \tau \cdot (1 - q^{-n}), k \in \{1, ..., 12\}, n \in \{1, 10\} \tag{1}$$

$$q = 1 + p \cdot (1 - \tau) \tag{2}$$

The respective differences per balance sheet item are weighted and added up. As a result, I is the relative tax advantage ($I \succ 0$) or disadvantage ($I \prec 0$) related to the balance sheet total, that an enterprise would face if IAS/IFRS were relevant for taxation in the given scenario:

$$I^{bt} = \sum_{k=1}^{12} T_k \cdot b_k \tag{3}$$

The relative tax advantage/disadvantage equals the gain/loss in interest. For additional information it seems to be appropriate to relate the tax advantage/disadvantage also to

- the equity incl. reserves according to commercial statements (I^e) and to
- the return on equity[19] (I^{op}) according to commercial statements.

$$I^e = \frac{I^{bt}}{e} \tag{4}$$

$$I^{op} = \frac{I^{bt}}{roe} \tag{5}$$

$p = 3\%$
$\tau = 25\%$ (Austrian corporate tax rate)
$q_s = 1,0225$

[19] Operating profit (Ergebnis der gewöhnlichen Geschäftstätigkeit) related to equity incl. reserves; taken from the data provided by OeNB/SME Research.

Parameter	Description
n	Term
T_k	Difference between present and discounted future tax burden for each balance sheet item
f_{ik}	IAS/IFRS factor
f_{tk}	Tax factor
τ	Corporate income tax rate
p	Discount rate
b_k	Weighted balance sheet item
I^{bt}	Discounted tax dis-/advantage related to the balance sheet total
I^{e}	Discounted tax dis-/advantage related to equity
I^{op}	Discounted tax dis-/advantage related to return on equity
roe	Return on equity

Table 7: Parameters of the executed Simulations

6 Results

6.1 By Sector

The overall result of the simulation is shown in Figure 1, 2 and 3. They show the additional or reduced tax burden - which in fact is a loss or gain in interest, resulting from earlier or later tax payments as a percentage of the balance sheet total. Since this figure might be misleading, also the percentage of equity[20] and the percentage of the return on equity[21] are given. The results show broadly the same picture (Figures 1, 2 and 3):

- Low percentage in all relations, in all scenarios;
- Scenarios 1 and 2 show no difference;
- Scenarios 1 and 2 are to the benefit of the enterprise;
- Scenario 3 is to its disadvantage.

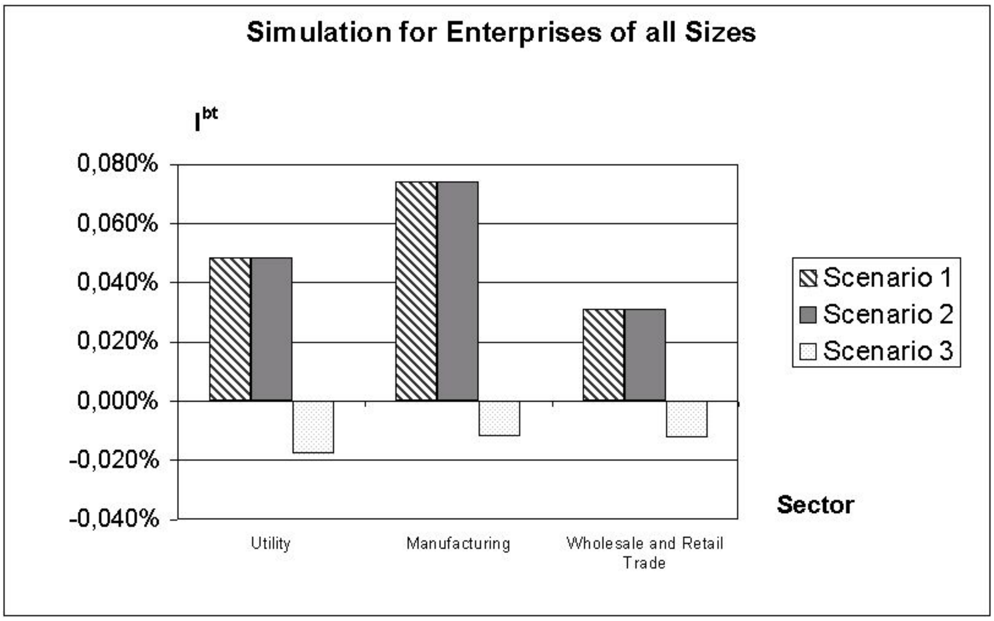

Figure 1: Gain/Loss in Interest related to Balance Sheet Total sorted by Sectors

[20] Equity according to the data provided by OeNB/SME Research, aggregated in Table 1, URL quoted above.
[21] Return on equity according to the data provided by OeNB/SME Research, URL quoted above.

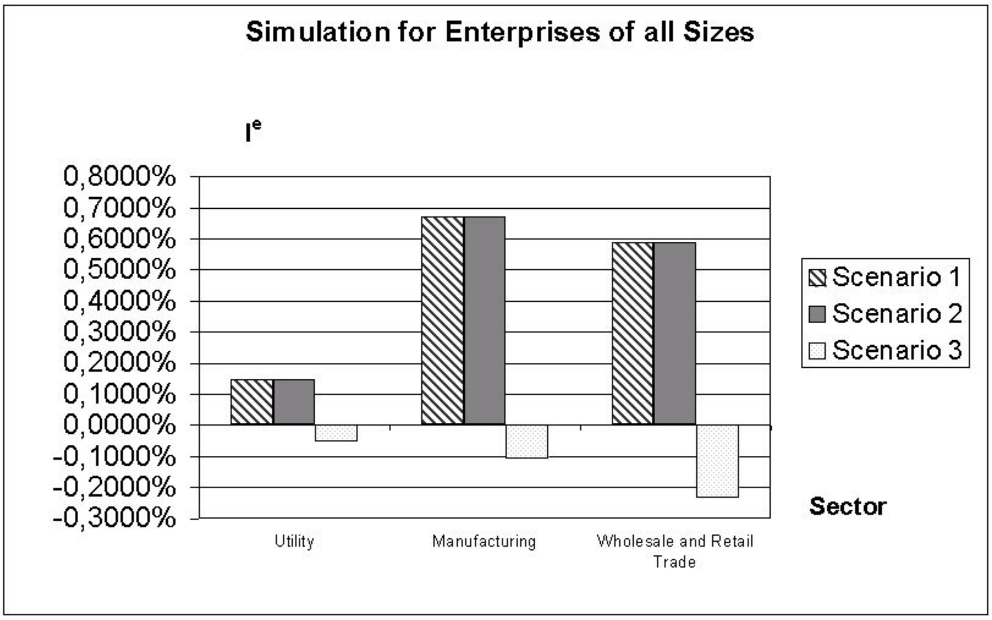

Figure 2: Gain/Loss in Interest related to Equity sorted by Sectors

The results of this study show that:

- There is no difference between scenario 1 (full relevance of IAS/IFRS) and scenario 2 (full relevance of IAS/IFRS with no measurement above historical cost), in other words: measurement above historical cost is of no practical importance. Given the recent developments in international accounting and the strong commitment to fair value accounting, this might change in the future.

- Surprisingly and against all fears expressed by enterprises, scenarios 1 and 2 lead to a relative tax benefit (discounted tax advantage) for the enterprise. The reason for that can be seen in the fact that - according to the scenarios - the restrictive tax rules for the measurement of pension liabilities (and similar) are abandoned, instead the IAS rules, which lead to much higher liabilities, are relevant. This leads to a long-term postponement of the tax payment.

- Scenario 3, which is calculated according to the assumption that the existing mandatory tax rules for the determination of taxable profit remain unchanged, leads to a discounted tax disadvantage. In this setting, the existing restrictive tax rules for the measurement of pension liabilities (and similar) are maintained. What remains is the effect of other provisions being measured at a lower value according to IAS, thus leading to a discounted tax disadvantage.

- The discounted tax dis-/advantage is relatively small, both when related to the balance sheet total and when related to the equity of the typical enterprise. The gain in interest does not even reach 1% of the equity; the loss in interest amounts to 0,23% of the equity. The increase or reduction of the return on equity, caused by the gain or loss in interest is

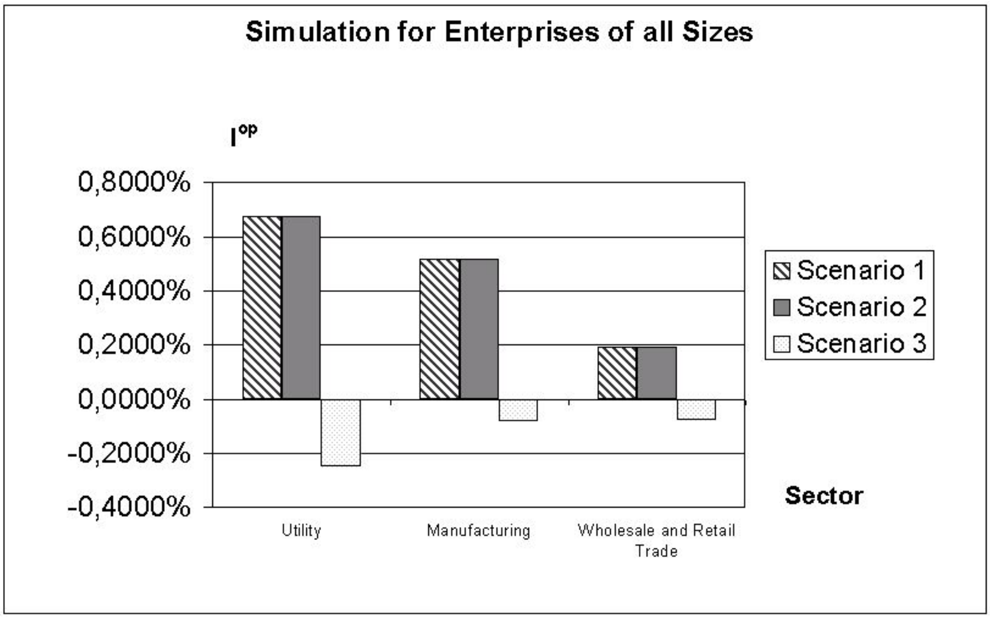

Figure 3: Gain/Loss in Interest related to the ROE sorted by Sectors

also very low. It amounts to +0,67% (scenarios 1 and 2) and -0,25% (scenario 3), and is negligible when the gain/loss in interest is spread over the supposed period of 10 years.

6.2 By Sector and Size

In addition to an analysis by sector, an analysis by size is of interest. The question is whether large enterprises would be affected more or less than small enterprises.

The additional element of size is included by using b_k by size as included in the set of data provided by the Austrian National Bank[22]. The data differs between micro/small/medium/large/ very large. As our set of data does not include micro sized enterprises, the category micro is excluded from the analysis below. This seems reasonable also when assuming that taxation according to IAS/IFRS will not be relevant for micro-enterprises.
The factors f_{ik} and f_{tk}, as explained above, cannot be distinguished by sector or by size.

The factors over all sizes are applied to size-specific weights of balance sheet items. The results therefore give information on how the different weight of balance sheet items influences the expected tax effect. For example, the significant proportion of pension liabilities in large utility enterprises (17% of the balance sheet total) versus only 3% in medium-sized utility enterprises influences the tax benefit in scenarios 1 and 2. Differing use of accounting choices according to size are not represented in the results.

Analyzing the discounted tax benefit related to equity (I^e) according to size and sector, one can see:

[22]URL quoted above.

- For scenarios 1 and 2 (equal results, see above) the relative advantage decreases with size (see Figure 4). The reason lies in equity ratios increasing with size.
- Utility makes an exception: unlike in other sectors, the equity ratio is not positively correlated to the size of the business. Instead it is negatively correlated to the weight of pension liabilities, which are of crucial importance for our analysis. Larger utility enterprises have larger pension liabilities which results in lower equity. Thus, the relation of tax advantage to equity increases.
- No clear tendency can be seen for scenario 3 (see Figure 5).

When regarding the discounted tax dis-/advantage related to the return on equity ROE (I^{op}), similar observations can be made (see Figures 6 and 7):

- The effect is very low: it is at maximum +2,3%, at minimum -0,5% of the ROE;
- For manufacturing, the positive or negative effect correlates to the size of the business: the larger the enterprise, the bigger the effect on the relative dis-/advantage is.
- For trade, the relative effect is rather unimpressed by size.
- For utility, no clear tendency can be observed.[23]

[23] ROE for large utility businesses is not available.

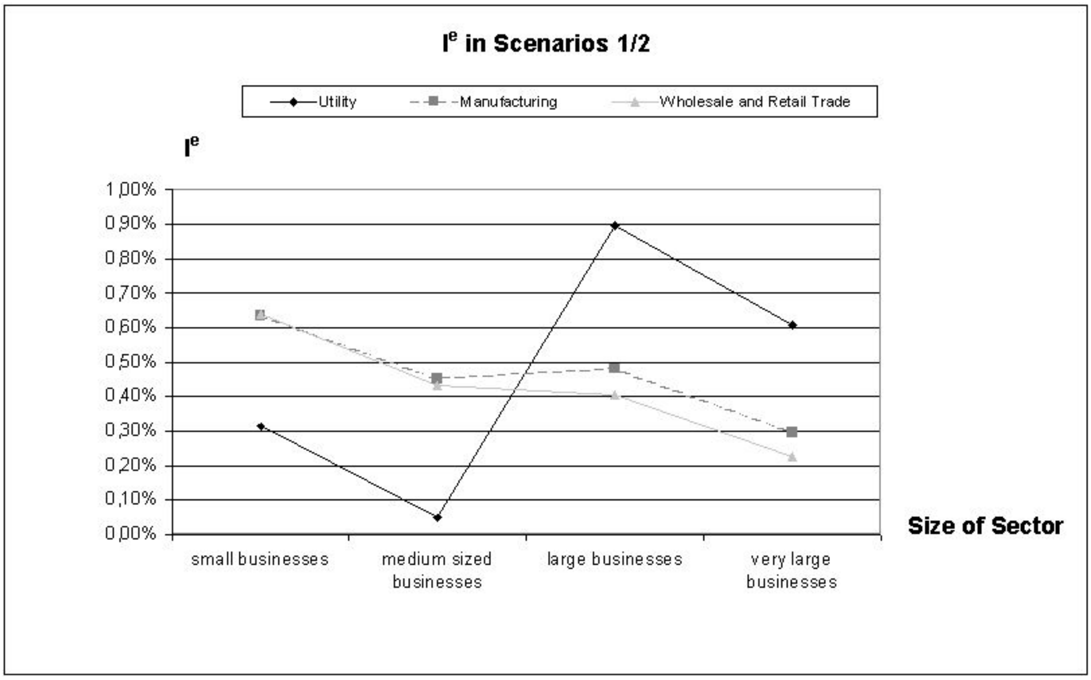

Figure 4: Gain in Interest related to Equity sorted by Sectors and Size

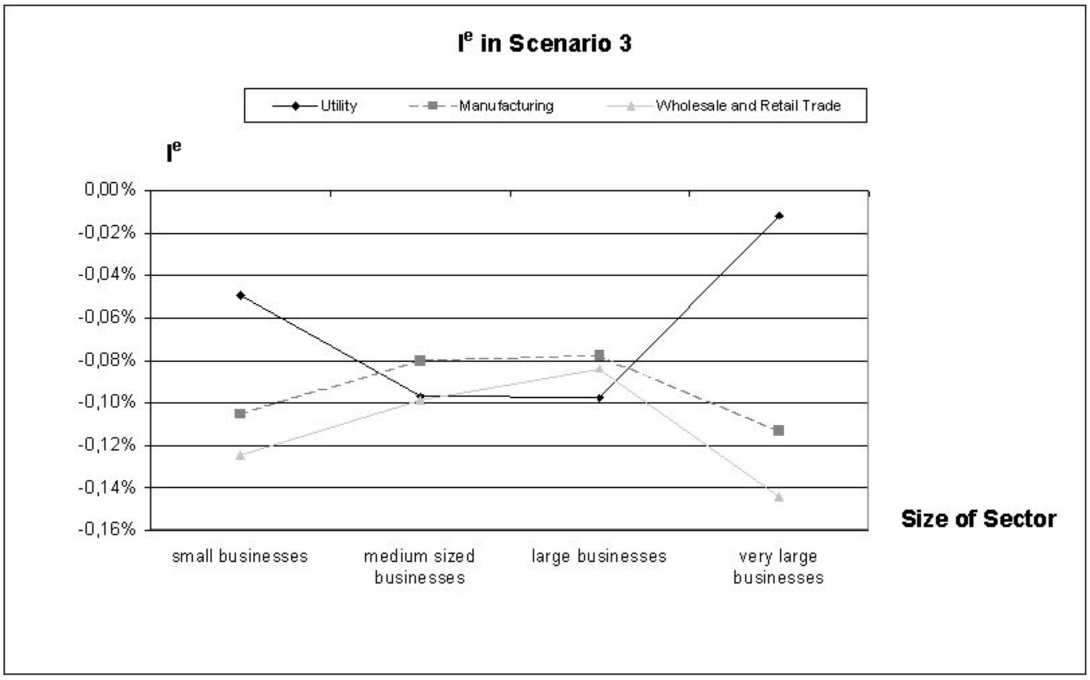

Figure 5: Loss in Interest related to Equity sorted by Sectors and Size

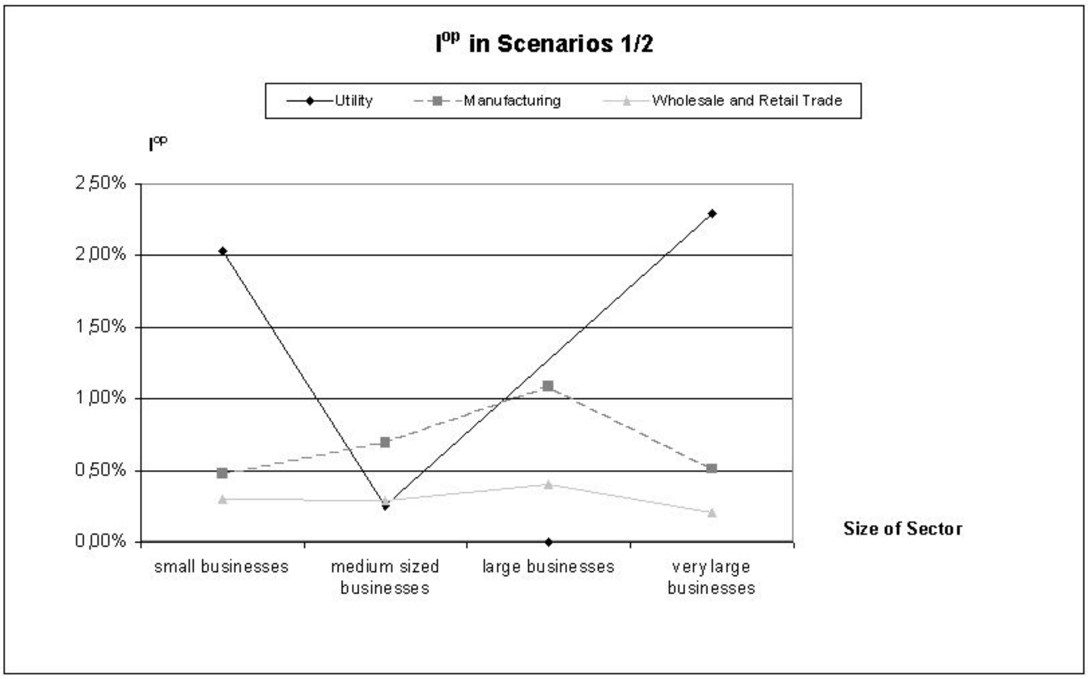

Figure 6: Gain in Interest related to the ROE sorted by Sectors and Size

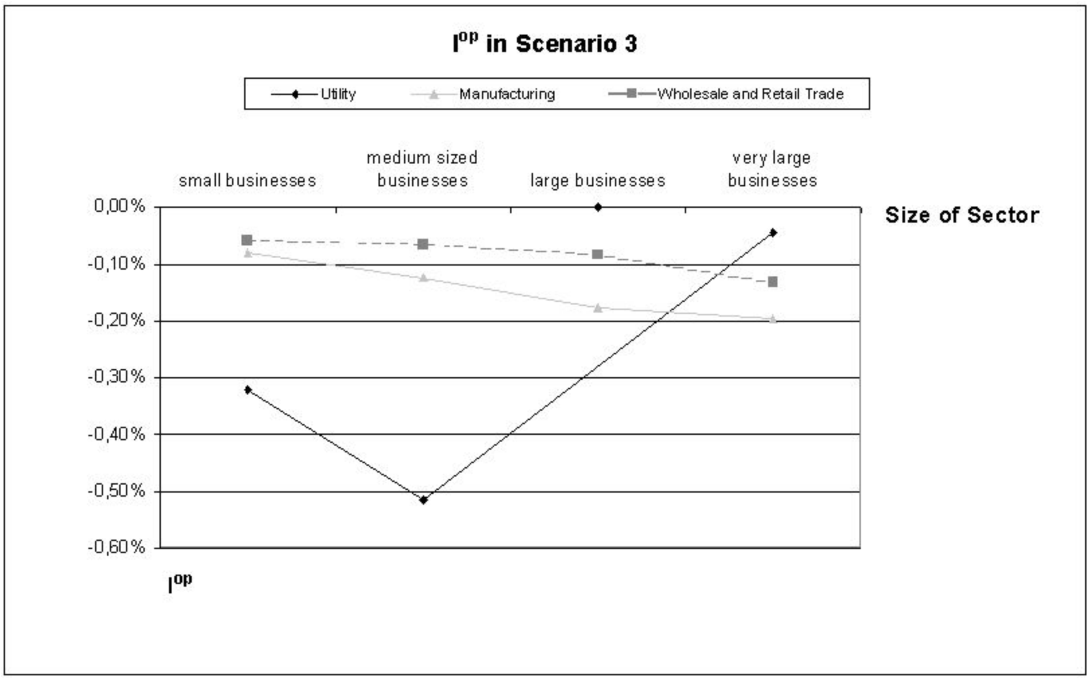

Figure 7: Loss in Interest related to the ROE sorted by Sectors and Size

6.3 Summary

The results so far imply that in scenarios 1 and 2 the relative importance of pension liabilities b_9 is relevant for the tax benefit in case of IAS/IFRS relevance. This can easily be seen in Table 4 and is confirmed by a correlation of 0,99 between pension liabilities and I^{bt} (Pearson's correlation coefficient).

In scenario 3, no tax consequences arise from the different measurement of pension liabilities under IAS, since according to that scenario, the existing restrictive tax rules on pension liabilities (among other) are maintained. The extent of the discounted tax disadvantage is fully correlated to the weight of the other provisions b_{10} that are considered, since only those differences in measurement have an influence in scenario 3 (see Table 4; consequently Pearson's correlation coefficient $r = -1$). The fact, that the measurement of provisions according to IAS is 'less prudent' and allows for less hidden reserves, would lead to a loss in interest from earlier tax payments, if IAS-provisions were relevant for taxation.

In scenarios 2 and 3, measurement above cost is eliminated. In scenario 1 however, the effect of fair value measurement of financial instruments according to IAS 39 deserves further attention. The effect of IAS on the discounted tax burden depends on the one hand on the weight of the specific item in the balance sheet according to the data base, on the other hand on the relative differences in measurement according to our sample.

- For financial fixed assets, the weight is negligible (b_3 0,8 - 1,48%; see Table 1). Additionally, no difference in measurement was observed ($f_{ik} - f_{tk}$ 0 / 0 / 2%, $n = 44$; see Table 4).
- Financial current assets (included in other current assets) have some weight (b_7 13,01 - 25,62%; see Table 1), but our sample includes only two cases where financial current assets were included. In those two cases, no difference in measurement was observed (see Table 4), however this allows no generalization. A discrepancy between the weight of the balance sheet item and the low frequency in our sample is observable. It seems that large amounts of financial current assets are held by only few enterprises. For the majority of enterprises, financial current assets play no large role in practice. For those enterprises that do hold financial current assets, for example banks, the effect of IAS 39 could not be established by our simulation.
- Table 1 gives no information on derivatives. The same conclusions as for financial current assets can be drawn: For the majority of enterprises, derivatives play no large role in practice. In all other cases, the simulation does not give information on the effect of IAS 39.

7 Limitations of the study

The results of the study face certain limitations.

- The sample size for analysing the differences in measurement is limited. As already mentioned, this is due to the difficult access to the data, which is usually not available to researchers. A larger number of enterprises would increase the validity of the study - however we are confident that the results as presented here are valid. Given the very low variance for differences in measurement for assets and for most liabilities, additional data will probably not change the results of the study.

- The data of our sample was made available by offices of one large auditing and consultancy firm only, no other consultancy firm participated. This might lead to a bias in so far as, according to the firm's policy, certain accounting methods might be preferred.

- Some sectors are not represented in the sample, e.g. banks and insurance companies. Other sectors are represented insufficiently. The selection of the companies for analysis reflects not only the difficulty to get confidential data but also our focus on the most detailed financial statements available. Sector-factors could not be derived. The calculation of the factors f_{ik} and f_{tk} is dominated by manufacturing industry.

- Scenario 1 of our study is constrained by the fact that the sample selection was done at a time when measurement at fair value was of minor interest. In the meantime, fair values became more important in IFRS. The importance of measurement above cost in German (and Austrian) IFRS-statements, however, is still low (Küting 2007). Scenarios 2 and 3 are not affected.

- According to our study, the effect of fair value measurement for financial instruments is relevant to a minority of enterprises only. It therefore could not be established. It is reasonable to assume that scenario 1 - in breach of core tax principles - could lead to large effects for enterprises with substantial measurement above cost.

- The fact that only little difference in measurement was found in our sample might be the result of previous alignment between tax measurement, IAS/IFRS measurement and commercial measurement. It is reasonable to assume that after having introduced IAS/IFRS, enterprises would have tried to minimize the cost of keeping three sets of accounts. The differences in measurement might be larger when referring to would-be figures of enterprises not yet presenting international statements. Regrettably, such data is not available.

- The findings cannot be transferred to other countries. Obviously, the effect on tax depends largely on the current rules for the determination of taxable profit, which differ considerably among countries. Furthermore, the tendency to aggregate commercial and taxable results is typical for Austrian (and German) enterprises.

Future research could address these limitations.

The financial statements in our sample come from different years among enterprises. The statements cover the years 2002 - 2005. During that time IAS 41, IFRS 1 and IFRS 3 entered into force. The fact that these provisions might not have been taken into account in the statements prior to their coming into force, however, does not bias our results. Our sample does not include enterprises of the agricultural sector, therefore the later introduction of IAS 41 can be neglected. The provisions of IFRS 1, being effective of January 2004, are already incorporated in the statements of the year 2004 and 2005 which account for approximately 64% of our sample. The remaining 36% of the statements may not incorporate IFRS 1 explicitly, however the main provisions have already been part of SIC 8. The introduction of IFRS 3 can be neglected as our sample only includes single accounts.

Contrary to what can be assumed, the fact that several of the 61 enterprises pertain to groups does not limit the validity of our results either. Apart from nine enterprises that do not form part of a group in our sample, the sample covers seven groups. The group size in our sample varies from five to twelve members. Usually, all group members follow the same accounting methods and policies, as mandated by the parent. Thus, it can be assumed that the deviance to tax accounts will also be alike. However, the data does not confirm that supposition. Within groups, the factors f_{ik} and f_{tk} differ significantly.

As has been stated in the description of the design of the study, the term in which differences in measurement will reverse has been chosen to be 10 years for long term assets and liabilities (nl). Since this was a rough simplification, the sensitivity of nl is of interest. A sensitivity analysis shows that the relation between nl and I^{op}, I^{e}, I^{bt} is almost linear 1:1. Doubling nl from 10 to 20 years almost doubles the relative discounted tax dis-/advantage. Reducing nl from 10 to 5 years nearly halves the effect. The result obviously depends very much on the term. Nevertheless, the relations of the simulations and the overall picture do not change. The effects are still small and the results and conclusions remain valid.

8 Conclusion

The question of what would happen to the discounted tax burden of an Austrian enterprise if IAS/IFRS were used as the relevant basis for taxation has been tested in three scenarios. The data used reflect the typical Austrian balance sheet structure and the empirically observed changes in measurement when drawing up IAS/IFRS-accounts and tax accounts respectively. Contrary to other studies, not only empirically observed financial statements but additionally the empirically observed differences in measurement are the basis for the simulation. This constitutes a novelty in research.

The overall result (for all scenarios, for all sectors included, and for all sizes) is that the discounted tax dis-/advantage is very small. This is true when measured in absolute terms and when related to the balance sheet total, to the equity and to the return on equity. Notwithstanding considerable legal and economic reservations against the relevance of IAS/IFRS for taxation, enterprises would not have to fear large financial effects.

Scenario 1 assumes that all IAS/IFRS are relevant for taxation, irrespective of their compliance with the basic principles of income taxation (in particular when the taxation of unrealised profit due to measurement above historical cost is concerned). In spite of concerns to be found in practice, enterprises would face a discounted tax advantage. This is (almost exclusively) due to the fact that under this assumption, the existing restrictive rules of sec. 14 Austrian Income Tax Act for pension liabilities would accordingly no longer apply, the tax deductible liability would be of a considerably higher amount. In other words: differences in measurement such as for example measurement at fair value above historical cost, higher historical cost due to the capitalization of interest, higher intangible assets due to different capitalization rules, higher inventory/receivables due to the percentage of completion method, or lower measurement of provisions (just to name a few), that all would give rise to a discounted tax disadvantage, are of no practical relevance. Too little weight of the balance sheet item and too little differences in measurement are the reasons.

Since taxation of unrealised gains is unacceptable from a systematic point of view, scenario 2 assumes that even though all IAS/IFRS are relevant for taxation, measurement above historical cost is not admitted. The results do not differ from scenario 1; it is thus shown that measurement above cost does not play a role yet.

In scenario 3, all existing mandatory tax rules are assumed to be maintained. The only effect on the discounted tax burden results from provisions that would have to be measured at a more realistic value, not allowing for hidden reserves. This leads to a discounted tax disadvantage.

Since the effects on discounted tax burden are small, one could argue that IAS/IFRS prove to be a suitable basis for taxation. The authors do not support this view. The fact that Austrian enterprises need not fear substantial additional tax burdens, in case IAS/IFRS were relevant for taxation, does not invalidate all the other (more legal) arguments against such relevance from chapter 3.

The question remains, in how far these results from Austria can be generalised for other (European) countries. On the one hand, the results apply only to Austria. By nature any research referring to national tax law is relevant to the respective state only. On the other hand, it seems reasonable to draw conclusions for other states. Austria is a country of continental-European accounting tradition with a dominant position of the prudence principle. Via *Maßgeblichkeit* and in spite of several mandatory tax law provisions, this conservatism is reflected in the taxable profit. Still, the effect of IAS/IFRS is small. It can therefore be assumed that the effect would be small in other countries as well. This remains to be verified.

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