



Financial Reporting Advisory Board Paper

Imputed Tax and Spend

Issue:	Certain obligation based levy funded schemes, especially in the energy sector, are recognised by the ONS as imputed tax and spend in the National Accounts. These schemes often do not meet the recognition criteria for inclusion in departmental accounts. The Board has asked for an update on this issue and a further issue that was considered by a FRAB working group in respect of the accounting treatment for Contracts for Difference.
Impact on guidance:	No impact on the FReM
IAS/IFRS adaptation?	No
Impact on WGA?	None
IPSAS compliant?	Yes
Interpretation for the public sector context?	No
Impact on budgetary regime?	Budgets will continue to follow national accounts.
Alignment with National Accounts	In the case of imputed tax and spend schemes where the IFRS recognition criteria are not met (and hence the schemes are excluded from accounts), the resource accounts treatment will not align with National Accounts.
Impact on Estimates?	In the case imputed tax and spend schemes where the IFRS recognition criteria are not met (and hence the schemes are excluded from accounts), the schemes will also be excluded from Estimates.
Recommendation:	That the FRAB note developments and that there is no intention to amend the FReM in regard to these two issues.
Timing:	Revised Estimate treatment for the effected imputed tax and spend schemes will apply from 2014-15. Alternative reporting to Parliament will commence from 2013-14.

Background

1. The Board received a verbal update in October 2013 on 'imputed' tax and spend schemes. These are obligation based levy funded schemes (almost entirely energy related) which the ONS has, or the Treasury anticipates will, classify as equal and offsetting taxation and public spending which in National Accounts will be imputed to flow through central government. In accordance with the Treasury's responsibilities to control and ensure accountability to Parliament for taxation and public spending the Treasury required these schemes be included in departmental budgets, Estimates and resources accounts. However, each year at the Supplementary Estimates the Chief Secretary of the Treasury gave a derogation to the effected departments to remove the schemes, pending a resolution of the accounting treatment.
2. In April 2012 the C&AG wrote to the DECC Accounting Officer outlining his concerns about the inclusion of these schemes within the DECC's resource accounts principally because the imputed tax did not meet the income recognition criteria under IFRS. He further expressed concerns about the inclusion of these schemes in the Statement of Parliamentary of Supply and indicated that this would result either in an ongoing qualification of DECC's accounts or a significant delay in the laying of accounts before Parliament.
3. Separately, in early 2013 a technical working group of the FRAB considered the potential accounting treatment for another energy sector related scheme which was being developed under the Government's proposals for Electricity Market Reform (outlined in the Energy Bill introduced to Parliament in 2012) called Contracts for Difference. This is not a potential 'imputed' tax and spend scheme as the economic (and cash) flows of the subsidy and levy funding mechanism will flow through a central government body. The contracts require a counterparty body (expected to be classified by the ONS to the central government sector) to pay or receive the difference between the strike price in the contract and a reference energy price for each unit of metered output generated by the contract holder.
4. The technical working group considered the accounting treatment for Contract for Difference under IFRS and the FReM and concluded that the contracts fell within the scope of IAS 39. Contracts for Difference will be funded through the Supplier Obligation which the ONS provisionally concluded will be a tax. DECC had expressed some concern that reporting the liability created under IAS 39 for Contracts for Difference, but not recognising a matching asset under the Supplier Obligation, would misrepresent the overall financial position. Government financial statements do not typically recognise assets derived from a right to fund expenditure through future taxation and consistent with this approach the Treasury are not planning to amend the FReM to accommodate the recognition of a matching asset.

Update on Imputed Tax and Spend

5. In accordance with the Treasury's policy intentions outlined in the verbal update of October 2013 the Treasury further considered how to best resolve the imputed tax and spend issue to meet Treasury's objectives of controlling and maintaining accountability for public spending and taxation.
6. In November 2013, in accordance with the protocol agreed under Clear Line of the Sight, the Chief Secretary to the Treasury wrote to the relevant committees in Parliament requesting approval to create the first misalignment between departmental budgets and Estimates since the beginning of Clear Line of Sight. Under this proposal a further derogation would be given to these schemes in 2013-14, but from 2014-15 they will be included in departmental budgets, but not Estimates or accounts unless they meet the recognition criteria in accordance with the FReM.
7. Departments will be required to report annually to Parliament on such 'imputed' tax and spend schemes, as recognised by the Office for National Statistics. These report(s) will be subject to audit and be implemented for the 2013-14 financial year onwards. These reports will focus the needs of the Parliamentary and general user and will be laid before Parliament at the same time as the Office of Gas and Electricity Market's existing annual publication on the Renewables Obligation (expected March 2015).
8. The Chief Secretary to the Treasury received responses from the relevant committees who were supportive of the approach but had a number of suggestions in respect of the form and contents of these reports. Treasury officials are currently engaging with the effected departments (primarily DECC) to consider the practicalities of the different options and will be advising the Chief Secretary of the Treasury in due course on his response to Parliament and begin the process of planning and consultation with the relevant stakeholders to facilitate production and audit of the new reports.
9. The Treasury does not intend to make any amendment to the FReM in respect of these schemes.

Update on Contract for Difference

10. The Energy Act 2013, which forms the legislative basis for Contracts for Difference and the Supplier Obligation, received Royal Assent in December 2013. The final terms of the Supplier Obligation will be determined in regulations. The first Contracts for Difference (or precursor instruments called Final Investment Determinations) are expected to be signed in 2014-15 and we expect DECC to account for them in accordance with the FReM.
11. The Treasury does not intend to make any amendment to the FReM in respect of Contracts for Difference.

Summary and recommendation

12. The Board requested an update on two issues in respect of energy schemes that have previously been discussed by the Board; 'imputed' tax and spend and Contracts for Difference.

13. A new reporting framework is being developed for 'imputed' tax and spend schemes, thus removing the need to consider an amendment to the FReM that might lead to a departure from IFRS.
14. The legislative framework that facilitates Contracts for Difference and the funding mechanism called the Supplier Obligation is reaching its final stages. The Treasury has no intention to amend the FReM for Contract for Difference.

HM Treasury
3 April 2014