Report
on
Review of the *Guidelines for Accounting and Recognition of Tax and Customs Revenue*

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Summary

A review of the Ministry of Economy and Finance draft *Guidelines for Accounting and Recognition of Tax and Customs Revenue* was conducted to achieve compliance with IPSAS. The text of the guidelines states that the guidelines are based on IPSAS ED 71, and it was found that the guidelines broadly follow the requirements of both the current IPSAS 23 and IPSAS ED 71. However, changes are recommended to fully comply with both IPSAS 23 and IPSAS ED 71. A main recommendation is to expand the scope of the guidelines to cover tax and customs related transfers, such as fines and penalties that are related to tax. A number of minor revisions are recommended to bring the guidelines into better compliance with IPSAS.

Scope of Work

This review was a desk review of the draft *Guidelines for Accounting and Recognition of Tax and Customs Revenue* to achieve compliance with IPSAS currently in effect, including IPSAS 23. Stakeholders were not interviewed and there was no review of policies or practices currently in place. As a result, this review gives no comment on whether the examples in the text of the guidelines sufficiently reflect the transactions to be recorded.

IPSAS 23 vs. ED 71

A single set of guidelines may be used to comply with both IPSAS 23 and IPSAS ED 71. In the guidelines, there are no adjustments required to reconcile accounting for revenue between IPSAS 23 and ED 71, except to remove references to ED 71. However, there are recommended revisions to bring the guidelines into better compliance with both IPSAS 23 and ED 71 as discussed below.

Recommended Revisions to the Guidelines

Major Revisions

1. Expand Section 1 and Section 2 to cover tax and customs related transfers and explicitly state in Section 1.3 Scope that the guidelines do not cover transfers not related to tax and customs; delete Section 3

It is not practical to include accounting for all transfers in these guidelines since the scope of transfers is quite broad, including grants, donations and gain on concessionary loans. Therefore, there is no need to include "Section 3: Transfers" which currently does not include sufficient guidelines for recognition or measurement.

Instead, in Chapter 1, Section 1.3, the scope should limit these guidelines to cover only transfers related to penalties and fines related to tax and customs. Following this, the recognition and measurement criteria in Section 1 and Section 2 should be expanded to cover fines and penalties related to taxes and customs.

2. Explicitly state that income tax revenue is not recognized in the period of the taxable event because the amounts cannot be reliably measured and revise recognition timing in 2.1.3

There is a problem in that according to IPSAS 23 and ED 71, tax revenue must be recognized in the period of the taxable event. In the case of corporate income tax, the taxable event in a given year (e.g. 2022) is the profit earned in that year. However, the corporate income tax is paid the following year, with a deadline by March of the following year (e.g. March 2023). Therefore, strictly following IPSAS, the revenue must be recognized in the year of the taxable event (2022). New Zealand, for example, uses forecasting methods to make an estimate of the corporate income tax owed to the government. Any resulting differences are recorded as a change in estimates. Another approach is to initially book an estimate and make an adjustment when the corporate income taxes are declared and paid (adjusting event).

However, an easier solution used by Australia and Canada is to delay the recognition of the revenue with the explanation “the corporate income tax is not yet reliably measured”. Therefore, for these two countries, they do not recognize the corporate income tax in the year of the taxable event because they do not know clearly the amount of the revenue until they receive the corporate income tax declarations and payments.

Therefore, following the Australian and Canadian approach, it is recommended to revise the timing for recognition in 2.1.3 to be “Recognized on or after the taxable event at the earliest the amount of tax due may be reliably measured, the earlier of (a) submission of a tax declaration, or (b) point of receipt”.

3. Remove reference to modified cash accounting

If the intention is to achieve compliance with IPSAS, the introduction should not make any references to modified cash accounting (in paragraph 2, of section 1.1).

4. Delete 2.1.2(c)

2.1.2(c) does not represent recognition criteria and is misleading to list as a criteria. It is only a general suggestion and should be deleted.

5. Allow for an annual allowance for bad debts as a solution to resolve the write-off for bad debts which may take up to 10 years

The government appears concerned about prematurely writing off bad debt, presumably with the concern that the debtor may avoid his/her responsibility. However, there is an easy solution to avoid writing off the debt until later:

Recognize a general allowance for bad debts without specifying any individual debtor (the allowance is a contra-receivables account), and then write-off bad debts only after 10 years or whatever strict policy the government may have. In this way, the debtors' names are kept in the books and are responsible for their debts, but the creation of a

general allowance allows the government to show the true value of receivables that may truly be collected for use by the government.

In relation to this, all references to bad debts will need to be revised, especially Chapter 5.

6. Delete sections 3.3

It is unnecessary to include discussion of compliance obligations in these guidelines since they are not relevant to tax and customs revenues. A short definition may be included in section 1.4 Definitions, but there is no need to have an entire section 3.3 on this topic.

7. Limit the score of 3.4 to Tax and Customs and Tax and Customs related transfers

As these guidelines do not cover most transfers (e.g. grants, donations, subsidies), section *3.4 Deferred revenue or advance receipt of transfers* should only cover discussion of transfers related to tax and customs, such as fine and penalties.

8. Use the Functional Currency in all Examples

Throughout the examples, it is recommended to use only Cambodian riel currency and not United States dollars. The functional currency of Cambodian government entities will be Cambodian riel and all accounting must be in the functional currency. Therefore, it may be misleading to users if there are example journal entries in USD.

9. Delete 3.6 and recognize prepayment of tax on income in the period collected

When the government collects the prepayment of tax on income there is no liability from the point of view of the government because the the definition of a liability is “a present obligation arising from past events” however, if the company does not earn a profit, there is no present obligation. Moreover, the earning of profit by the company is a future event that may or may not occur in future periods. The event of earning profit in the future is not a “past event”. There is no present obligation because: (a) if the

company has a loss in the current period, that prepayment becomes a minimum tax which the government has the right to retain; and (b) if the company has a profit in the current period, that prepayment is a payment of tax arising from a taxable event in the current period and should be recognized in the current period which is the period that the prepayment was made.

Although the explanation above may be rebutted, the explanation above provides an easy way to account for prepayment of income tax by recording revenue when the payments are received. In the event that a company has losses and the company recognizes a deferred tax asset, from the point of view of the government, at most this would be a contingent liability because the government has no way to reliably measure possible future profits of a company; contingent liabilities only require a disclosure in the notes and do not require accounting entries.

Minor Revisions

1. Minimize sections 1.1 and 1.2

To make the guidelines more user friendly and practical, it is best to keep the guidelines concise. Therefore, sections 1.1 (introduction) and 1.2 (purpose) should be kept to 1-2 short sentences each.

2. Revise the definition of tax

The definition of tax seems to be copied from IPSAS, however, for a Cambodian specific set of guidelines, there should not be any mention of “country to country”. Also, income tax is not only collected from large enterprises, so the example given in the definition may be misleading.