Taxation of Provisions and Accruals
(income tax and corporation tax)

Part 04-05-06

This document should be read in conjunction with sections 76A, 76B and 81 of the Taxes Consolidation Act, 1997

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Revenue
Cáin agus Custaim na hÉireann
Irish Tax and Customs

The information in this document is provided as a guide only and is not professional advice, including legal advice. It should not be assumed that the guidance is comprehensive or that it provides a definitive answer in every case.

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Note: The accounting standards referred to within this document are listed below. Any accounting analysis herein is included for information purposes only and does not replace the detailed requirements of the individual accounting standards.

- FRS 101 Reduced Disclosure Framework (September 2024);
- FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland (September 2024);
- FRS 105 The Financial Reporting Standard applicable to the Micro-entities Regime (September 2024);
- FRS 12[1]/IAS 37 Provisions, Contingent Liabilities and Contingent Assets (September 1998);
- SSAP 9 Stocks and Long-term Contracts (September 1988)[2];
- IAS 11 Construction Contracts (December 1993);
- IFRS 15 Revenue from Contracts with Customers (May 2014);
- IAS 19 Employee Benefits (June 2011).

[1] FRS 12 was effective for accounting periods ending on or after 23 March 1999. It was withdrawn for accounting periods beginning on or after 1 January 2015, when FRS 102 became effective.

[2] SSAP 9 was effective for accounting periods starting on or after 1 July 1988. It was withdrawn for accounting periods beginning on or after 1 January 2015, when FRS 102 became effective.

1 Introduction

A suite of accounting standards, referred to as current Irish GAAP (FRS 100 to FRS 105), was introduced in 2015 to replace former Irish GAAP (FRSs, SSAPs, etc.). This means that former Irish GAAP standards, including FRS 12 Provisions, Contingent Liabilities and Contingent Assets, can no longer be used. As a result, this guidance was updated to confirm that the position regarding the taxation of provisions and accruals remains unchanged under current Irish GAAP.

2 Executive summary

A provision is a liability of uncertain timing or amount while an accrual is a liability to pay for goods or services which have been received without formal confirmation of the amount payable. For tax purposes, provisions and accruals are regarded as substantially the same and are treated identically (albeit greater measurement uncertainty will usually be the distinguishing feature of a provision). The relevant Irish statute law concerning provisions and accruals is as follows:

- Section 76A(1) of the Taxes Consolidation Act, 1997 (TCA 1997) Computation of profits or gains of a company – accounting standards; and
- Section 81 TCA 1997 General rule as to deductions.

Section 76A(1) TCA 1997 legislates for a long-established case law principle[3] and provides that Case I or Case II profits or gains of a trade or profession carried on by a company are required to be "computed in accordance with generally accepted accounting practice subject to any adjustment required or authorised by law in computing such profits or gains for those purposes"[4]. "Law" for these purposes is not defined but it would include statute law, case law, statutory instruments and any directly applicable EU law. The case law principle embodied in section 76A(1) TCA 1997 applies equally to income tax.

[3] Odeon Associated Theatres Ltd v Jones (HM Inspector of Taxes) [1971] 48 TC 257.

[4] By virtue of section 76B(1)(b) TCA 1997, Case I or Case II losses of a trade or profession carried on by a company are computed in the same way as profits or gains.

Section 81 TCA 1997 applies to both income tax and corporation tax charged under Case I or II of Schedule D and provides that tax is to be charged "without any deduction other than is allowed by the Tax Acts". Section 81(2) TCA 1997 is concerned with prohibiting various claims for deduction from Case I or II profits rather than being directly concerned with the computation of Case I or II profits or gains or losses, the latter question being determined by section 76A(1) TCA 1997/case law principles. Section 81(2)(a) TCA 1997 provides that one of the critical tests of deductibility is whether the expense is "money wholly and exclusively laid out or expended for the purposes of the trade or profession". The terms "laid out" and "expended" are not defined in statute and are interpreted in accordance with case law principles.

As the Tax Acts are otherwise silent concerning provisions[5] and accruals, it is necessary to look to case law principles when considering if a provision or accrual is allowed for tax purposes. Irish courts and the courts of the United Kingdom (UK) have clearly identified the fundamental rule: a taxpayer is to be taxed on his profits, that is, on what remains after deducting expenses properly incurred to earn those profits. The object is to determine, as accurately as possible, the full profits or losses of the taxpayer's business for the accounting period in question (which case law[6] defines as "the difference between the receipts from the trade or business during such year or accounting period and the expenditure laid out to earn those receipts").

The specific question of the taxation of provisions has not come before the Irish courts but has been considered by the UK courts. Following some important UK court decisions concerning the taxation of provisions, and the introduction of accounting standards dealing specifically with provisions, Revenue issued *Tax* Briefing 41 in September 2000. Tax Briefing 41 applied to provisions which were included in the accounts ('recognised') in full compliance with FRS 12 Provisions, Contingent Liabilities and Contingent Assets/IAS 37 Provisions, Contingent Liabilities and Contingent Assets.

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[5] Section 81(2)(i) TCA 1997 deals with allowances for bad or doubtful debts. Although the word 'provision' is sometimes used in this context, strictly speaking these are adjustments of the carrying amount of an asset (debtors/amounts receivable) rather than recognition of a liability. Therefore allowances for bad and doubtful debts are not provisions and are not covered by FRS 12/IAS 37/FRS 101/section 21 of FRS 102/section 16 of FRS 105.

[6] Cronin v Cork and County Property Co Ltd III ITR 198; Carroll Industries Plc (formerly P J Carroll and Co Ltd) and P J Carroll & Co Ltd v S O'Culachain (Inspector of Taxes) IV ITR 135.

This Tax and Duty Manual (TDM) confirms that the position remains unchanged under current Irish GAAP: a provision or accrual recognised in accordance with IFRS [IAS 1.27, IAS 11, IAS 19.13 and IAS 37] or Irish GAAP [FRS 101; sections 2.48, 21 and 28.6 of FRS 102; sections 2.24, 16 and 23.5 of FRS 105] is acceptable for tax purposes subject to normal tax rules (for example, the expenditure in respect of which the provision or accrual is made would be an allowable deduction in computing profits for tax purposes and the provision or accrual is sufficiently reliable, as discussed at 6.2 below).

3 Background

Financial statements or 'accounts' of Irish incorporated companies are subject to both the financial reporting standards ('accounting standards') of the applicable 'financial reporting framework' and the requirements of Irish company law. The main financial reporting frameworks in use in Ireland are: (i) European Union-endorsed International Financial Reporting Standards (known as IFRS), which are issued by the International Accounting Standards Board; and (ii) the Financial Reporting Council's suite of financial reporting standards, which are known as UK and Irish generally accepted accounting practice (GAAP).

4 Provisions and accruals

4.1 Provisions

4.1.1 Definition

A provision is a liability of uncertain timing or amount. Under both IFRS [IAS 37.14 and IAS 37.23] and Irish GAAP [FRS 101/sections 21.4, 21.6 and Appendix I of FRS 102/sections 16.5, 16.7 and Appendix I of FRS 105] a provision must be included in the accounts ('recognised') as an expense in the profit and loss account/income statement and a liability on the balance sheet/statement of financial position when, and only when:

- there is a present obligation (legal or constructive) as at the balance sheet date;
- as a result of a past event (the 'obligating event'); and
- payment ('an outflow of resources embodying economic benefits' or a 'transfer of economic benefits') is probable ('more likely than not'); and
- the amount to be so paid can be estimated reliably.

The word 'provision' is often used in another context (for example, a provision for bad and doubtful debts or a provision for obsolete stock/inventory). Strictly speaking, these 'provisions' (or 'impairment allowances', as they are more correctly titled) are adjustments of the carrying amounts of assets rather than the recognition of liabilities. Therefore impairment allowances are not 'provisions' within the meaning of FRS 12/IAS 37/FRS 101/section 21 of FRS 102/section 16 of FRS 105 and are not within the scope of this TDM. See section 7.4 for more details on impairment allowances.

IFRS [IAS 37.36] and Irish GAAP [FRS 101/section 21.7 of FRS 102/section 16.8 of FRS 105] stipulate that the amount to be recognised as a provision is the best estimate of

the expenditure required to settle the present obligation at the reporting date and the accounting standards explain how to estimate this amount. IFRS [IAS 37.59] and Irish GAAP [FRS 101/section 21.11 of FRS 102/section 16.12 of FRS 105] also require that provisions be reviewed at each reporting date and adjusted to reflect the current best estimate of the amount required to settle the obligation. If it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision must be reversed.

The uncertainty regarding the amount and/or timing of provisions requires management to exercise a degree of judgement in determining the amount of the provision (and the accounting standards give guidance on the appropriate exercise of such judgement). As a result, a detailed review of provisions is a normal part of any statutory and Revenue audit.

4.1.2 Onerous contracts

Both IFRS [IAS 37.68] and Irish GAAP [FRS 101/Appendix I of FRS 102/Appendix I of FRS 105] define an onerous contract as a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

Both IFRS [IAS 37.66] and Irish GAAP [FRS 101/section 21.11A of FRS 102/section 16.13 of FRS 105] specifically require that the present obligation under an onerous contract shall be recognised and measured as a provision in accordance with IAS 37/FRS 101/ section 21 of FRS 102/section 16 of FRS 105, as applicable. Therefore, a provision for an onerous contract made in full compliance with IAS 37/FRS 101 or FRS 102 or FRS 105 is subject to the same accounting and tax treatment as any other provision, as discussed at sections 5, 6 and 7 below.

4.1.3 Future operating losses

Both IFRS [IAS 37.63] and Irish GAAP [FRS 101/section 21.11B of FRS 102/section 16.14 of FRS 105] explicitly prohibit the recognition of a provision for future operating losses. Therefore, provisions for future operating losses are prohibited for both accounting and tax purposes.

4.1.4 Restructuring

Both IFRS [IAS 37.10] and Irish GAAP [FRS 101/Appendix I of FRS 102/Appendix I of FRS 105] define a restructuring as “a programme that is planned and controlled by management and materially changes either: (a) the scope of a business undertaken by an entity; or (b) the manner in which that business is conducted”.

IFRS/FRS 101 [IAS 37.70] identify several examples of events that may fall under the definition of restructuring and these are shown overleaf.

- Sale or termination of a line of business.
- Closure of business locations in a country or region or the relocation of business activities from one country or region to another,
- Changes in management structure, for example, eliminating a layer of management.
- Fundamental reorganisations that have a material effect on the nature and focus of the entity's operations.

Both IFRS [IAS 37.71] and Irish GAAP [FRS 101/section 21.11D of FRS 102/section 16.16 of FRS 105] explicitly prohibit the recognition of a provision for restructuring in the absence of a legal or constructive obligation to restructure. Both IFRS [IAS 37.72] and Irish GAAP [FRS 101/ section 21.11C of FRS 102/section 16.15 of FRS 105] state that a constructive obligation to restructure arises only when an entity:

(a) has a detailed formal plan for the restructuring identifying at least:

  (i) the business or part of a business concerned,

  (ii) the principal locations affected,

  (iii) the location, function, and approximate number of employees who will be compensated for terminating their services,

  (iv) the expenditures that will be undertaken, and

  (v) when the plan will be implemented, and

(b) has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

Both IFRS [IAS 37] and Irish GAAP [FRS 101/section 21 of FRS 102/section 16 of FRS 105] specify detailed measurement rules for restructuring provisions. Therefore, a restructuring provision made in full compliance with IAS 37/FRS 101 or FRS 102 or FRS 105 is subject to the same accounting and tax treatment as any other provision, as discussed at sections 5, 6 and 7 below.

4.1.5 Construction contracts

The revenue recognition rules for construction contracts in which the entity is the contractor are set out in the following standards:

- **IFRS**
  - IAS 11: mandatory for financial reporting periods starting on or after 1 January 1995 but before 1 January 2018.
  - IFRS 15: mandatory for financial reporting periods starting on or after 1 January 2018 onwards but earlier application was permitted.

- **Irish GAAP**
  - SSAP 9 (for financial reporting periods beginning before 1 January 2015)
  - FRS 101 (applies the same recognition and measurement rules as IFRS)
  - Section 23 of FRS 102
  - Section 18 of FRS 105

The accounting and tax treatments under these standards are discussed below.

SSAP 9 and IAS 11

Both IAS 11 and SSAP 9 required that an entity should recognise a loss on a contract when it is probable that losses will be incurred in respect of a construction/long-term contract. Similarly, when the outcome of a contract cannot be estimated reliably, no profit should be recognised.

In Tax Briefing 41 (September 2000), Revenue accepted that a provision for a loss on a contract, made in accordance with paragraph 9 of Part 1 of SSAP 9, was no longer precluded on the basis that the provision takes account of expenditure which has not yet been incurred. Revenue stated that such a provision was allowable, subject to normal tax rules (for example, the provision or accrual is sufficiently reliable, as discussed at 6.2 below). For the avoidance of doubt, this TDM confirms that provision for a loss on a contract made in full compliance with IAS 11 is also allowable for tax purposes provided the provision or accrual is sufficiently reliable, as discussed at 6.2 below.

FRS 102 and FRS 105

Section 23.26 of FRS 102 (January 2022) and section 18.23 of FRS 105 (January 2022) provide as follows: "When it is probable that total contract costs will exceed total contract revenue on a construction contract, the expected loss shall be recognised as an expense immediately, with a corresponding provision for an onerous contract [in accordance with section 21 of FRS 102/section 16 of FRS 105, as applicable]". Therefore, a provision for an expected loss on a construction contract made under FRS 102 or FRS 105 is subject to the same accounting and tax treatment as any other provision, as discussed at sections 5, 6 and 7 below.

In September 2024 new iterations of FRS 102 and FRS 105 were published following the periodic review in 2024. As part of this review a new chapter 23 (Revenue from Contracts with Customers) was introduced to FRS 102 which superseded the previous chapter 23 (Revenue).

Similarly, a new chapter 18 (Revenue from Contracts with Customers) was introduced to FRS 105 which superseded the previous chapter 18 (Revenue).

These new chapters align both FRS 102 and FRS 105 more closely to IFRS principles under IFRS 15: Revenue from Contracts with Customers.

The effective date for these amendments to both FRS 102 and FRS 105, with respect to revenue recognition principles, will be for accounting periods beginning on or after 1 January 2026.

Therefore, as outlined with respect to IFRS 15 below, for financial reporting periods starting on or after 1 January 2026, expected losses on construction contracts accounted for in accordance with FRS102 or FRS105 will be no longer recognised, measured or presented and accordingly will not be within the scope of this TDM.

IFRS 15

IFRS 15.107-108 requires that any impairment relating to contracts with customers should be measured, presented and disclosed in accordance with IFRS 9 Financial Instruments. Any difference between the initial recognition of a receivable and the corresponding amount of revenue recognised should also be presented as an expense (for example, an impairment loss). Therefore, for financial reporting periods starting on or after 1 January 2018, expected losses on construction contracts are no longer recognised, measured or presented in accordance with IAS 11 or IAS 37 and accordingly are not within the scope of this TDM.

4.1.6 Pension obligations

When employers provide pension benefits to their staff, both IFRS [IAS 19.26] and current Irish GAAP [FRS 101/section 28.9 of FRS 102/section 23.8 of FRS 105] explicitly require the recognition in the accounts of the employers' estimated obligations under those pension plans. These pension obligations are not 'provisions' within the meaning of IAS 37/FRS 101/section 21 of FRS 102/section 16 of FRS 105 and accordingly are not within the scope of this TDM. Please see the TDM for Pensions for an overview of the tax treatment of employers' contributions to pension schemes.

4.2 Accruals

An accrual is a liability to pay for goods or services which have been received without the supplier issuing an invoice or other formal confirmation of the amount due, including amounts due to employees (for example, amounts relating to accrued holiday pay). Although it is sometimes necessary to estimate the amount or timing of accruals, the uncertainty is generally much less than for provisions. Accruals are often reported as part of trade and other payables in the financial statements whereas provisions are usually reported separately.

4.2.1 "Holiday accruals"

Unlike former Irish GAAP, both IFRS [IAS 19.13] and current Irish GAAP [FRS 101/ section 28.6 of FRS 102/section 23.5 of FRS 105] explicitly require companies to accrue for employees' unused holiday entitlements as at the financial reporting date. These "holiday accruals" effectively reallocate the cost of the extra days worked from the later period (when it is paid) to the earlier period (when it is incurred). "Holiday accruals" recognised in full compliance with IFRS [IAS 19.13] or Irish GAAP [FRS 101 or section 28.6 of FRS 102 or section 23.5 of FRS 105] are allowable deductions in computing profits for income tax and corporation tax purposes provided they are sufficiently reliable, as discussed at 6.2 below.

4.3 Taxation of provisions and accruals

IAS 37.11 states that "Provisions can be distinguished from other liabilities such as trade payables and accruals because there is uncertainty about the timing or amount of the future expenditure required in settlement…Although it is sometimes necessary to estimate the amount or timing of accruals, the uncertainty is generally much less than for provisions." Therefore IFRS/FRS 101 recognise that accruals and provisions are similar, with the distinguishing feature (uncertainty) being present to a greater or lesser degree in each case. Accordingly, provisions and accruals are regarded as substantially the same and are treated identically for tax purposes.
The relevant Irish legislation concerning provisions and accruals is as follows:

- Section 76A(1) TCA 1997 Computation of profits or gains of a company – accounting standards,
- Section 81 TCA 1997 General rule as to deductions, and
- Case law.

Sections 76A(1) and 81 TCA 1997 are discussed in section 5 below while case law principles are discussed in section 6 below.

5 Relevant Irish statute law

5.1 Section 76A(1) TCA 1997

Section 76A(1) TCA 1997 legislates for a long-established case law principle[7] and provides that Case I or Case II profits or gains or losses[8] of a trade or profession carried on by a company are required to be "computed in accordance with generally accepted accounting practice [defined in section 4 TCA 1997 as IFRS or Irish GAAP] subject to any adjustment required or authorised by law in computing such profits or gains [or losses] for those purposes". Therefore, section 76A TCA 1997 is subject to any adjustment required or authorised by law; it cannot override any rule of law. "Law" for these purposes is not defined but it would include statute law, case law, statutory instruments and any directly applicable EU law. The key point is that the accounting treatment is influential but not necessarily determinative of the correct tax treatment. TDM 04-05-03a provides further details regarding section 76A TCA 1997.

5.2 Section 81 TCA 1997

Section 81 TCA 1997 applies to both income tax and corporation tax charged under Case I or II of Schedule D and provides that tax is to be "charged without any deduction other than is allowed by the Tax Acts". Section 81(2) TCA 1997 is concerned with prohibiting deductions from Case I or II profits or gains rather than being directly concerned with the computation of Case I or II profits or gains or losses, the latter question being determined by section 76A TCA 1997 (as discussed at 5.1 above).

Please refer to the Notes for Guidance on section 81 TCA 1997 for further details if required but, for the purposes of this TDM, it is sufficient to note that section 81(2)(a) TCA 1997 states that two of the critical tests of deductibility when computing assessable Case I or II profits or gains or losses for corporation tax or income tax purposes are whether:

1. the expense is "money wholly and exclusively laid out or expended for the purposes of the trade or profession", and
2. there is any tax rule (statutory or case law) precluding a deduction.

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[7] Odeon Associated Theatres Ltd v Jones (HM Inspector of Taxes) [1971] 48 TC 257.

[8] By virtue of section 76B(1)(b) TCA 1997, Case I or Case II losses of a trade or profession carried on by a company are computed in the same way as profits or gains.

The terms “laid out” and “expended” are not defined in statute and are interpreted in accordance with case law principles because, in the absence of specific legislation, the correct tax treatment of any income or expense is a question of law and a matter to be determined by the courts.

6 Relevant case law

6.1 Introduction

Due to the lack of statutory law explicitly dealing with accounting matters, case law principles are often essential in determining the appropriate tax treatment of accounting items. Both the Irish and UK courts have clearly identified the fundamental rule: a taxpayer is to be taxed on his profits, that is, on what remains after deducting expenses properly incurred to earn those profits. The object is to determine, as accurately as possible, the profits or losses of the taxpayer’s business for the accounting periods in question.

6.2 Taxation of provisions and accruals

Most UK and Irish case law concerning accruals deals with the question of whether the accruals basis of accounting (whereby the effects of transactions and other events and circumstances are reflected in the periods in which they occur, even if the resulting cash receipts and payments occur in a different period) is acceptable for tax purposes. However, for tax purposes, provisions and accruals are regarded as substantially the same and are treated identically. Therefore, the case law principles regarding the taxation of provisions also determine the appropriate tax treatment of accruals.

Irish courts have not specifically considered the taxation of provisions but UK courts have held that:

1. The deductibility of a provision depends on whether the accounts adequately state the taxpayer’s profits for the year and whether the provision is sufficiently reliable.
2. The question as to the reliability of the provisions made in the accounts is essentially a question of fact and degree.
3. In the absence of the provision failing to take into account anything which should have been taken into account, the provision is sufficiently precise for tax purposes. However, to the extent that any provision or accrual is insufficiently reliable for tax purposes (for example, where the accounts are based on factual assumptions which are insufficiently reliable or simply inconsistent with the true facts), an approach more correctly or more reliably based on the facts will be adopted for income tax or corporation tax purposes.

It is well established that general provisions are not allowable for tax purposes (because they are not considered sufficiently reliable or precise). However, the introduction (see 7.2 below) of detailed accounting rules (see 4.1.1 above) specifying when provisions may be included in accounts effectively prohibited the recognition of general provisions for accounting purposes.

7 Taxation of provisions and accruals: Ireland

7.1 Irish case law

Irish courts have not specifically considered the taxation of provisions so the principles established by the UK courts (see 6.2 above) have not been tested in Irish courts.

7.2 FRS 12 and IAS 37

FRS 12 Provisions, Contingent Liabilities and Contingent Assets and IAS 37 Provisions, Contingent Liabilities and Contingent Assets were issued in September 1998. These were the first accounting standards to deal specifically with provisions and they were jointly developed by the UK and international standard setting bodies. According to FRS 12: "Apart from the two minor additions to the FRS noted in Appendix VI, the two standards are identical except for phraseology and structure necessary to conform to established practice in each constituency."

7.3 Revenue guidance

Following the introduction of FRS 12 and IAS 37, Revenue was prepared to follow the decisions of the UK courts regarding the taxation of provisions where such provisions had been made in full compliance with FRS 12 or IAS 37. Therefore, Revenue issued Tax Briefing 41 in September 2000 to provide guidance as to how it would apply those case law principles in practice.

The purpose of this TDM is to:

- take account of the introduction of current Irish GAAP (FRS 100 to FRS 105) to replace former Irish GAAP (FRSs, SSAPs, etc.), and
- confirm that, for tax purposes, provisions and accruals are regarded as substantially the same and are treated identically.

This TDM confirms that the position remains unchanged under current Irish GAAP: a provision or accrual recognised in full compliance with IFRS [IAS 1.27, IAS 11, IAS 19.13 and IAS 37] or Irish GAAP [FRS 101/sections 2.48, 21 and 28.6 of FRS 102/sections 2.24, 16 and 23.5 of FRS 105] is acceptable for tax purposes, subject to normal tax rules (for example, the expenditure in respect of which the provision or accrual is made would be an allowable deduction in computing profits for tax purposes and the provision or accrual is sufficiently reliable, as discussed at 6.2 above). For the avoidance of doubt, a provision for expenditure which, under tax law, is considered capital in nature would not be acceptable for tax purposes.

7.4 Impairment Allowances – Bad or Doubtful Debts

Section 81(4) TCA 1997, clarifies the position in relation to the deductibility of impairment allowances for bad or doubtful debts.

During the global financial crisis, it became clear that existing accounting standards for financial instruments deferred the write-off of inevitable bad debts for too long, resulting in financial statements which did not present a true picture of a company's profitability and/or viability.

In response to widespread criticism and demands for change, IFRS 9 was developed. IFRS 9 replaced the previous incurred credit loss (ICL) models for estimating bad and doubtful debts with expected credit loss (ECL) models, which has led to quicker write-off of bad debts.

Under the Expected Credit Loss (ECL) model, impairment losses are measured on a probability-weighted basis which forecasts potential losses. This system considers factors such as the effective interest rate, past events, current conditions and future economic conditions. In contrast, the previous Incurred Credit Loss (ICL) models calculated impairment allowances based on objective evidence of a loss having been incurred.

As a result, impairment allowances calculated under IFRS 9 may contain an element of both general and specific bad debt provisions. Therefore, there are some elements of the allowances that would be deductible under previous tax rules and some elements that may not be deductible.

Section 81(4) TCA 1997 clarifies that impairment allowances for bad or doubtful debts calculated in accordance with generally accepted practice, as defined in section 4 TCA 1997, are deductible for corporation tax purposes, from 1 January 2018.

7.5 Summary

Provisions and accruals (including holiday accruals) made in full compliance with IFRS [IAS 1.27 or IAS 11 or IAS 37 or IAS 19.13] or Irish GAAP [FRS 101 or sections 2.48 and 21 of FRS 102 or sections 2.24 and 16 of FRS 105 or section 28.6 of FRS 102 or section 23.5 of FRS 105] are acceptable for income tax and corporation tax purposes, subject to normal tax rules (for example, the expenditure in respect of which the provision or accrual was made would be an allowable deduction in computing profits for income tax and corporation tax purposes and the provision and accruals are sufficiently reliable, as discussed at 6.2 above).

8 Examples

Please see below and overleaf for some examples of when:

- provisions and accruals are acceptable for tax purposes; and
- adjustments are required to ensure compliance with normal tax rules, for example:
  - (i) because the expenditure in respect of which the provision or accrual was made would not be an allowable deduction in computing profits for income tax and corporation tax purposes; or
  - (ii) because the provision and accruals were not sufficiently reliable (as discussed at 6.2 above).

Example 1

Company A sells electrical products and provides a 12-month warranty which assures that the electrical products will work as intended for 12 months. The warranty is not sold separately. The warranty provision, as correctly calculated in accordance with IAS 37/section 21 of FRS 102/section 16 of FRS 105, is recorded in the profit and loss account (P&L) as follows:

Year	Net P&L posting re. warranty provision (DR = debit; CR = credit)
2019	€250,000 DR
2020	€75,000 DR
2021	€10,000 CR
2022	€50,000 DR
2023	€25,000 CR

As the warranty provision has been correctly calculated in accordance with IAS 37/section 21 of FRS 102/section 16 of FRS 105, and as no adjustment is required to ensure compliance with normal tax rules, the allowable provision for tax purposes is the same as the provision required for accounting purposes.

Example 2

Company Z sells electrical products and provides a 12-month warranty which assures that the electrical products will work as intended for 12 months. The warranty is not sold separately. The warranty provision, as correctly calculated in accordance with IAS 37/section 21 of FRS 102/section 16 of FRS 105, is recorded in the P&L.

The owner and managing director also insists on increasing the warranty provision by 10% to provide a reserve in case of serious product malfunction. Every year the auditor points out that the increased provision is not strictly in accordance with the accounting standards and recommends that the 10% “buffer” be written back. However, as the extra 10% is never sufficiently material in the context of the financial statements, the general provision has always remained unadjusted in the final audited accounts and the auditor has never had to qualify the audit opinion.

The net P&L postings in respect of the specific and general warranty provisions were as follows:

Year	Specific warranty provision (DR = debit; CR = credit)	General warranty provision (DR = debit; CR = credit)
2019	€250,000 DR	€25,000 DR
2020	€75,000 DR	€7,500 DR
2021	€10,000 CR	€1,000 CR
2022	€50,000 DR	€5,000 DR
2023	€25,000 CR	€2,500 CR

To the extent that the warranty provision has been correctly calculated in accordance with IAS 37/section 21 of FRS 102/section 16 of FRS 105 and no adjustment is required to ensure compliance with normal tax rules, it is allowable for tax purposes (i.e. no addback or deduction is required for tax purposes). However, to the extent that the provision is a general provision, it is not sufficiently precise for tax purposes and it is not allowable for tax purposes. Therefore, Company Z must make the following adjustments in its corporation tax computation in respect of the general provision:

Year	Disallowed for tax purposes (i.e. general provision)
2019	€25,000 addback
2020	€7,500 addback
2021	€1,000 deduction
2022	€5,000 addback
2023	€2,500 deduction

Example 3

Taxpayer B commenced trading in 2019 and prepares financial statements in accordance with IFRS. Taxpayer B's employees are only entitled to pay in lieu of leave where they cease employment without having fully utilised their leave entitlement; however, Taxpayer B also allows employees to carry forward leave in excess of the statutory minimum to the next leave year provided that the leave carried forward is used within the first six months of the following year.

Taxpayer B records holiday accruals in accordance with IAS 19: Employee Benefits and calculates the accrual based on holiday records (which show earned but unutilised leave at year end) and average salaries per day (calculated from payroll records). The net P&L postings required to ensure compliance with IAS 19 were as follows:

Year	Net P&L posting re. holiday accrual (DR = debit; CR = credit)
2019	€100,000 DR
2020	€1,000 DR
2021	€1,000 CR
2022	€5,000 DR
2023	€3,000 CR

As the holiday accrual has been correctly calculated in accordance with IAS 19, and as no adjustment is required to ensure compliance with normal tax rules, the allowable accrual for tax purposes is the same as the accrual required for accounting purposes.

Example 4

Employees of Company C are permitted 24 days annual leave which must be taken in the holiday year which commences on 1 April. Employees are permitted to carry forward leave in excess of the statutory minimum to the next leave year provided that the leave carried forward is used within the first six months of the following year. Employees are only entitled to pay in lieu of leave where they cease employment without having fully utilised their leave entitlement.

Company C's financial year end is 31 December. At 31 December an employee is entitled to have taken 18 days' holiday. Company C prepares its accounts in accordance with FRS 102 and its date of transition to FRS 102 was 1 January 2014. Under former Irish GAAP, Company C did not recognise a holiday accrual but it must do so upon transition.

Company C calculates from holiday records that outstanding holidays (i.e. holiday not taken from an allowance of 18 days) were as shown overleaf.

As at 31 December 2013

56 days for all employees; measured at the applicable average salary per day for each employee, this amounts to €7,670.

All but one employee utilised this leave in the first six months of 2014; that employee ceased employment and received pay in lieu of leave carried forward from 2013 amounting to €411.

As at 31 December 2014

40 days for all employees; measured at the applicable average salary per day for each employee, this amounts to €5,615 (all staff were awarded a salary increase of 2.5% from 2013).

All employees utilised this leave in the first six months of 2015; Company C did not have to make any payments in lieu of leave carried forward from 2014.

As at 31 December 2015

35 days for all employees; measured at the average salary per day for each employee (all staff were awarded a salary increase of 2.5% from 2014), this amounts to €5,036.

All but two employees utilised this leave in the first six months of 2016; those employees ceased employment and received pay in lieu of leave carried forward from 2015 amounting to €719.

The accounting journals necessary to record the holiday accruals as well as the calculation of the allowable deductions in the 2015 tax computation are shown overleaf.

Year	Accounting journals for holiday accrual	Accounting journals for pay in lieu of leave	2015 tax computation
2013 (prior period adjustment in 2015)	**DR P&L Reserves €7,670** **CR Holiday accrual €7,670** Posting of accrual as of 31/12/2013.		**Calculate the 'relevant amount'[9]:** (a) calculate retrospective effect: -€5,615 (b) adjust for non-taxable/non-deductible amounts: €nil (c) prevent double tax/deduction: n/a **The 'relevant amount' is -€5,615.**
2014 (prior period adjustment in 2015)	**DR Holiday accrual €7,259** **CR P&L Reserves €7,259** Reversal of accrual as of 31/12/2013. **DR P&L Reserves €5,615** **CR Holiday accrual €5,615** Posting of accrual as of 31/12/2014.	**DR Holiday accrual €411** **CR P&L Pay in lieu €411** Reversal of original 2014 P&L posting re. payments (now included in 2013 accrual).	

[9] Section 76A(4)(c) TCA 1997 provides that, subject to the Tax Acts, the retrospective effect of adopting an accounting standard which is recognised in opening reserves for a period of account in accordance with IFRS or Irish GAAP shall be taxable or deductible, as the case may be, in computing the profits or gains of a company for the purposes of Case I or II of Schedule D. As the retrospective effect is only taxable/deductible 'subject to the Tax Acts', by virtue of section 76A(1) TCA 1997, the calculation of the 'relevant amount' is also 'subject to any adjustment required or authorised by law'. This means that only the amounts of provisions and accruals which would be allowable in accordance with case law principles (as discussed in at section 6.2 of this TDM) may be included in the 'relevant amount'. Also, by virtue of sections 76A(4)(d) and (e), the retrospective effect must be adjusted to ensure that the adoption of the new accounting standard does not result in double taxation of income or double deduction of expenditure; the adjusted amount is referred to as the 'relevant amount'. In addition, section 76A(4)(g) TCA 1997 requires the 'relevant amount' to be taxed/deducted over five years. TDM Part 04-05-03a provides further details regarding section 76A TCA 1997.

2015 (first set of FRS 102 accounts)	**DR Holiday accrual €5,615** **CR P&L €5,615** Reversal of accrual as of 31/12/2014. **DR P&L €5,036** **CR Holiday accrual €5,036** Posting of accrual as of 31/12/2015.	Not applicable: no pay in lieu paid in 2015.	The holiday accrual has been correctly calculated in accordance with section 28.6 of FRS 102. **No adjustment is required.**
NET TAX DEDUCTION IN 2015 [(-€5,615 ÷ 5) + €5,615 - €5,036]			**€544**

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