Single Rulebook Q&A

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Status	Final Q&A
Legal act	Regulation (EU) No 575/2013 (CRR)
Topic	Own funds
Article	36
Paragraph	1
Subparagraph	b
COM Delegated or Implementing Acts/RTS/ITS/GLs/Recommendations	Not applicable
Article/Paragraph	not applicable
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Disclose name of institution / entity	No
Type of submitter	Credit institution
Subject matter	Deduction of software
Question	Should software be deducted from own funds net of the whole amount of tax deductible amortisation that will be recorded throughout their life?
Background on the question	Investment in software are recorded as an asset in the balance sheet and amortised over their life. Amortisation is tax deductible, which recreates CET1. Consequently, it is unclear whether it would be acceptable that investments in software are deducted with an exposure net of the upfront amount of amortisation that will be tax deductible.
Final answer	According to Article 36(1)b) of Regulation (EU) No 575/2013 (CRR), as amended by Regulation (EU) 2019/876, Institutions shall deduct from CET1 items their 'intangible assets with the exception of prudently valued software assets the value of which is not negatively affected by resolution, insolvency or liquidation of the institution'. For those prudently valued software assets, a specific prudential treatment has been recently introduced to the Commission Delegated Regulation (EU) No 241/2014 (RTS), which, under Article 13 a), envisages an amortization for prudential purposes over a period of maximum three years.

	Moreover, Article 37(a) CRR requires that ‘the amount to be deducted shall be reduced by the amount of associated deferred tax liabilities that would be extinguished if the intangible assets became impaired or were derecognised under the applicable accounting framework’. The interplay between Article 13a RTS and Article 37(a) CRR has been recently clarified by Q&A 5567. The answer specifies that for prudently valued software the amount to be deducted from CET1 items – as calculated according to the mentioned Article 13 a) - shall be reduced only by the corresponding portion of the associated deferred tax liabilities (DTLs) and not by the full amount of DTLs related to the software assets at stake. From the example provided by the submitter, it is understood that the positive tax effect mentioned is the one associated with the ordinary fiscal deductibility of the amortization of the software during its residual life. As it is assumed that the accounting amortization of each period will be entirely deductible for tax purposes (implying that the tax and accounting value of the assets will be aligned over the period) no temporary differences (neither DTLs nor DTAs) will arise for the case presented. Therefore, the tax deductibility of the accounting amortization will only impact the determination of the current tax of each year that will be lower than the amount would have been determined without the accounting amortization and its fiscal deduction. Thus, the net effect reflected in the P&L of each year due to the accounting amortization will be equal to the value of the amortization (recorded as an expense in each year) minus the tax saving that will emerge due to its tax deductibility. In formula: Net effect P&L = Accounting amortization in each year * (1- tax rate). As the positive effect of the tax deductibility is already considered in the calculation of the profit and loss of the period, positively affecting the CET1, the same effect shall not be considered in the calculation of the prudential deduction of prudently valued software. This in fact would constitute a double counting of the positive effects of the tax saving that would artificially inflate the CET1. Therefore, software assets shall not be netted of the “upfront amount of amortization that will be tax deductible”. On the contrary, should the positive tax effect mentioned by the submitter refer to the DTLs associated with the intangible assets (instead of the current tax of each year) the clarifications provided by Q&A 5567 remain valid.
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