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International
Accounting Standards
Board

INFORMATION FOR OBSERVERS

IASB Meeting: **February 2006, London**

Project: **Short-term convergence: income taxes – cost benefit and transition – detailed analysis (Agenda Paper 2C)**

Introduction

1. This paper sets out the Board's proposed changes to IAS 12 and any new information needed to comply. It also sets out the detailed staff analysis of the resulting costs and benefits and impact on the transitional arrangements for each change.

Proposed change to IAS 12	**New information required**	**Cost benefit analysis**	**Impact on transitional arrangements**
1 Change of the definition of tax base in IAS 12 to the following: Tax base is a measurement attribute. It is the measurement under existing tax law applicable to a present asset, liability, or equity instrument recognised for tax purposes as a result of one or more past events. That asset, liability, or equity instrument may or may not be recognised for financial reporting. Change to the definition of a temporary difference in IAS 12 so that a temporary difference is a difference between the tax base of an asset or liability and its reported amount in the financial statements that will result in taxable or deductible	Potentially a new analysis of existing information about the tax status of assets and liabilities. Further, if the new analysis results in there being a temporary difference when previously there was none, information relevant to the measurement of those temporary differences will be needed. Also, if the temporary difference is a deductible temporary difference, the need for a valuation allowance will need to be considered.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]

Proposed change to IAS 12	**New information required**	**Cost benefit analysis**	**Impact on transitional arrangements**
amounts when the reported amount of the asset or liability is recovered or settled and to eliminate the requirement in IAS 12 that the tax base of items that have no tax consequences associated with them (ie ‘permanent differences’) be equal to the carrying amount. Change to eliminate the guidance in paragraph 52(b) of IAS 12 that management intent as to the manner in which an entity will recover (settle) the carrying amount of an asset (liability) can affect the tax base of an asset or liability.			

Proposed change to IAS 12	New information required	Cost benefit analysis	Impact on transitional arrangements
2 Elimination of the initial recognition exception. Measurement of all assets and liabilities that do not have a tax base equal to carrying amount on initial recognition at the fair value they would if they had a tax base equal to fair value. Extension of that decision to all assets and liabilities remeasured at fair value.	Entities will need to determine the tax base for assets and liabilities to which the initial recognition exception has been applied. Further, they will need to determine the fair value that the assets and liabilities would have if their tax base equalled fair value. In the case of deductible temporary differences, they will also need to determine whether a valuation allowance is necessary.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]
3 Removal of the prohibition on recognising a deferred tax liability on the initial recognition of goodwill.	The tax base of goodwill.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]

Proposed change to IAS 12	**New information required**	**Cost benefit analysis**	**Impact on transitional arrangements**
4 A change to recognise deferred tax assets and liabilities arising from temporary differences relating to domestic subsidiaries, associates and interests in joint ventures.	The tax base of domestic subsidiaries, associates and interests in joint ventures and information relating to the measurement of the resulting temporary differences.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]
5 Clarification that substantively enacted occurs at the point in the enactment process when the future steps will not change the outcome. In the US tax jurisdiction this is the point of enactment.	No new information.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]
6 Change to valuation approach to the recognition of deferred tax assets.	No new information required, except that IAS 12 does not require an entity to determine the applicable tax rate for unrecognised deferred tax assets. Change is a change of wording rather than a change in substance.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]

Proposed change to IAS 12	**New information required**	**Cost benefit analysis**	**Impact on transitional arrangements**
7 Change to SFAS 109 allocation requirements.	IAS 12 requires changes in tax effects originally recognised in equity to be recognised in equity. If determining that amount is difficult, some reasonable allocation is made. SFAS 109 requires all changes in tax effects subsequent to initial recognition to be recognised in continuing operations, with exceptions related to business combinations and capital transactions. It might be thought that the SFAS 109 requirements require less information, because the changes in tax effects do not need to be traced back to where the tax was originally recognised. However, the original tax recognised in equity is not recycled into profit or loss at the time of the change in tax. Instead it is recycled at the same time as the gain or loss to which it related. This means that, in some cases, records of	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]

Proposed change to IAS 12	New information required	Cost benefit analysis	Impact on transitional arrangements
	tax that no longer exists have to be kept until the gains and losses are recycled.		
8 Change to require balance sheet classification of deferred tax to be based on the classification of the related asset or liability. Any valuation allowance arising in a tax jurisdiction is allocated between current and non current deferred tax assets for that tax jurisdiction on a pro-rata basis.	No new information is needed but new analysis will be.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]
9 Explicit requirements on alternative minimum taxation requirements	Alternative minimum taxation requirements must be factored into the measurement of deferred tax assets and liabilities. This is probably already being done under IAS 12. In any case, the alternative minimum	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]

Proposed change to IAS 12	**New information required**	**Cost benefit analysis**	**Impact on transitional arrangements**
	taxation requirements will not be new information.		
10 Explicit requirements on allocation of tax across entities within a consolidated tax group.	Allocation method must be systematic, rational and consistent with broad principles of standard. If an inappropriate allocation method has been used, or no allocation has been made under IAS 12, new information/systems may be needed.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]
11 Explicit guidance on special deductions – that adjustments to the rate that depend on levels of taxable income or type of taxable income should be included in the determination of the rate used to measure deferred tax assets and liabilities. No other tax rate reductions or tax deductions should be anticipated. The rate used should be a	Impact of adjustments that depend on levels of taxable income or type of taxable income.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]

Proposed change to IAS 12	**New information required**	**Cost benefit analysis**	**Impact on transitional arrangements**
weighted average of the possible rates applicable, based on rates enacted or substantively enacted at the balance sheet date.			
12 Explicit requirements relating to uncertain tax positions, ie that the tax position should be measured at the expected outcome.	The expected outcome of the tax positions taken.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]
13 Additional disclosures on intra-group transfers.	None – the information is already needed to comply with the recognition requirements in IAS 12. Moreover, if the effect is material, it should already show up in the disclosed tax reconciliation.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]

Proposed change to IAS 12	**New information required**	**Cost benefit analysis**	**Impact on transitional arrangements**
14 Requirement for entities not subject to income taxes because their income is taxed directly to their owners to disclose that fact and the net difference between tax bases and carrying amounts.	Tax bases for the assets and liabilities of such entities.	[Not reproduced in Observer Notes.]	[Not reproduced in Observer Notes.]