9 November 2010

International Financial Reporting Standards

Income Taxes

ED Deferred Tax: Recovery of Underlying Assets

Global Preparers' Forum, November 2010
Agenda paper 7

The views expressed in this presentation are those of the presenter, not necessarily those of the IASB or IFRS Foundation.

Why did the IASB publish this ED

- Income tax project started in 2002 as an item of short term convergence with US GAAP
- The exposure draft was published in March 2009 to reduce gaps with US GAAP and also to solve some issues in practice
- The IASB and the FASB announced in October 2009 that they will consider fundamentally reviewing the accounting for income tax sometime in future (rather than pursuing the convergence in the area of income tax)
- But, there are still some issues that remain unsolved in practice
- In September 2010, the IASB published an exposure draft to solve one of the practice issues
  - Issue: deferred tax relating to remeasurement of investment properties
  - The comment period ends on **9 November 2010**.
  - The IASB plans to discuss other practice issues including the issue of uncertain tax positions and to publish a separate exposure draft in due course.

What is the issue?

- Divergence in practice
  - Measurement of deferred tax asset and liability arising from fair valuing a property is often difficult and subjective when an entity expects to use the property and then sell it
  - Divergence exists as to which tax base and tax rate an entity should use.
  - Impact is often significant in jurisdictions where a tax rate applied to gain on sale is different from a tax rate applied to income from use

- Relevance of the information
  - Methods often used in practice require to include, wholly or partially, tax consequences of using the property (ie tax that an entity will pay on future rental income)
  - But, the Board was told that tax consequences of using the property are less relevant when properties are fair valued
  - This is particularly the case when entities do not expect that the carrying amount of the property will decline before sale

Exception or guidance?

- Principle
  - Is that an entity determines tax base and a tax rate based on a manner in which it expects to recover the carrying amount of underlying asset; but
  - Is difficult to apply in specific circumstances.
- Guidance
  - Can avoid creating another exception; but
  - May create unintended consequences.
- An exception
  - Is simple; and
  - Can avoid unintended consequences by limiting its scope.

Scope

- Investment Property
  - Primary issue arises from investment property
- Property, plant and equipment
  - Similar to investment property if they are measured using the revaluation model
- Intangible assets
  - Revaluation model similar to property, plant and equipment
- Other assets
  - Outside the scope because of different characters of assets that would require different measurement models

Measurement base
(rebuttable presumption of sale)

- Sale base measurement;
  - is generally more relevant than use base when property is fair valued; and
  - avoids other problems such as double counting of tax effect
- Use base measurement;
  - is appropriate when an entity expects to consume all economic benefits from the asset throughout its economic life (ie an asset will never be sold and will be devalued to an almost negligible amount)
  - In other situations, a presumption of sale applies as a practical solution

Transition

- Full retrospective application
- No exception for previous business combinations

Questions or comments?

Expressions of individual views by members of the IASB and its staff are encouraged. The views expressed in this presentation are those of the presenter. Official positions of the IASB on accounting matters are determined only after extensive due process and deliberation.