IFRS

STAFF PAPER

July 2014

IFRS Interpretations Committee Meeting

Sep and Nov 2011,
May 2012, Mar 2014

Project	**Finalisation of tentative agenda decision**
Paper topic	IAS 12 *Income Taxes*—Recognition of deferred tax for a single asset in a corporate wrapper

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Introduction

1. In March 2014, the IFRS Interpretations Committee (the Interpretations Committee) published a tentative agenda decision not to add to its agenda a request to clarify the accounting for deferred tax in the consolidated financial statements of the parent, when the subsidiary has only one single asset within it (the asset inside) and the parent expects to recover the carrying amount of the asset inside by selling the shares in the subsidiary (the shares).

2. The Interpretations Committee noted significant diversity in practice in accounting for deferred tax when tax law attributes a separate tax base to the asset inside and to the parent's investment in the shares, and each tax base is separately deductible for tax purposes (ie tax law considers the asset inside and the parent's investment in the shares to be two separate assets):

    (a) some follow the tax perspective and recognise deferred tax related to both the asset inside and the shares; while

    (b) others recognise only the deferred tax related to the shares.

    (c) A third group of preparers determines deferred tax by comparing the carrying amount (in the consolidated financial statements) of the asset inside with the tax base of the shares, and using the tax rate that applies if the parent recovers the carrying amount of the shares.

3. The Interpretations Committee discussed the issue thoroughly at four meetings and consulted the IASB members on it. The results from these discussions and consultations can be summarised as follows:

Existing requirements are clear

4. IAS 12 *Income Taxes* does not need to be clarified as far as the accounting for deferred tax in the consolidated financial statements of the parent is concerned, when the subsidiary has only one single asset inside and the parent expects to recover the carrying amount of the asset inside by selling the shares.

5. This is because the requirements are clear:

   (a) Paragraph 11 of IAS 12 requires the entity to determine temporary differences in the consolidated financial statements by comparing the carrying amounts of assets and liabilities in the consolidated financial statements with the appropriate tax base. In the case of an asset or liability of a subsidiary that files separate tax returns, this is the amount that will be taxable or deductible on the recovery (settlement) of the asset (liability) in the tax returns of the subsidiary.

   (b) The requirement in paragraph 11 of IAS 12 is complemented by the requirement in paragraph 38 of IAS 12 to determine the temporary difference related to the shares of the parent in the subsidiary by comparing the parent's share of the net assets of the subsidiary in the consolidated financial statements, including the carrying amount of goodwill, with the tax base of the shares for purpose of the parent's tax returns.

6. The Interpretations Committee also noted that these paragraphs require a parent to recognise both the deferred tax related to the asset inside and the deferred tax related to the shares, if:

   (a) tax law attributes separate tax bases to the asset inside and the shares;

(b) in the case of deferred tax assets, the related deductible temporary differences can be utilised as specified in paragraphs 24–31 of IAS 12; and

(c) no specific exceptions in IAS 12 apply.

7. Please note that for the ease of reference, we do not make reference the requirements in paragraphs 6(b) and 6(c) when we discuss the recognition of deferred tax. We do not make reference to these two general requirements, although they are relevant for the issue discussed in this paper. This is merely to simplify the reading of the staff analysis.

Interpretations Committee cannot address concerns raised

8. The reason for the diversity in practice is not unclear requirements in the existing guidance in IAS 12; these requirements are clear (see paragraphs 4–6). Instead, the reason for the diversity in practice is concerns about the accounting outcome that follows from the existing requirements.

9. Analysing and assessing these concerns, however, would require a broader project than the Interpretations Committee could perform on behalf of the IASB.

10. Consequently, the Interpretations Committee tentatively decided not to take the issue onto its agenda, but instead to recommend to the IASB that it should analyse and assess these concerns in its research project on Income Taxes.

11. The Interpretations Committee considered that in the light of its analysis of the existing requirements, neither an IFRIC Interpretation nor an amendment to a Standard that the Interpretations Committee would develop on behalf of the IASB was necessary and consequently decided to issue a tentative agenda decision that can be found in the *IFRIC Update* of March 2014.[1]

[1] http://media.ifrs.org/2014/IFRIC/March/IFRIC-Update-March-2014.pdf

Objective of Staff Paper

12. The objective of this Staff Paper is to:

    (a) provide an analysis of the comments received on the tentative agenda decision;

    (b) make a recommendation; and

    (c) set out the wording for the final agenda decision (refer to **Appendix A**).

13. **Appendix B** contains the comment letters that we received on the tentative agenda decision that can be found in the *IFRIC Update* of March 2014.

Comment letter analysis

Overview

14. The comment period for the tentative agenda decision ended on 9 June 2014. We received **five** responses. These comment letters are attached to the paper as **Appendix B**.

15. Four respondents (AcSB, CPC, ESMA and EY) support the Interpretations Committee's tentative agenda decision not to add this issue to its agenda. Only DTT proposed that the issue should be added to the Interpretations Committee's agenda and that the Interpretations Committee should develop an IFRIC Interpretation.

16. While the AcSB also agreed with the Interpretations Committee's stated reasons for its conclusions, the comments from the other respondents are diverse and are therefore analysed separately.

Comments received—CPC

17. CPC supports the decision made by the Interpretations Committee related to this project, ie not to require an IFRIC Interpretation or an amendment to IAS 12 or IFRS 10 *Consolidated Financial Statements*. However, they recommend that the

IASB should consider performing a complete project to revise IAS 12 in its entirety.

18. Furthermore, they agreed with an argument raised by the staff in Agenda Paper 3 for the March 2014 Interpretations Committee meeting:[2]

> The paragraphs 11 and 38 of IAS 12 require distinguishing between the asset inside and the shares in the subsidiary in accounting for deferred taxes in the consolidated financial statements, if tax law distinguishes both assets. In our jurisdiction, the income taxes are based on the results of each entity and not on a consolidated basis.
>
> We analyse the Staff Paper (March 2014) and on the basis of this analysis we agree with the argument that the deferred tax liability related to the asset inside represents future tax payments that result from achieving taxable inflows of economic benefits by using the asset inside. These tax payments affect the value of the shares in the subsidiary.
>
> Thus, if the tax law attributes separate tax bases to the asset inside, and the parent's investment in the shares and each tax base is separately deductible for tax purposes (ie tax law considers the asset inside and the parent's investment in the shares to be two separate assets), we agree that the entity must recognize deferred tax related to both the asset inside and the subsidiary's shares.

Staff analysis of comments from CPC

19. We agree with the CPC's analysis, which supports the tentative agenda decision of the Interpretations Committee. Furthermore, we note that the IASB has added a project on Income Taxes to its research agenda. Such a project is the first step

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[2] http://www.ifrs.org/Meetings/MeetingDocs/Interpretations%20Committee/2014/March/AP03%20-%20Cover%20note%20-%20IAS%2012%20Recognition%20of%20DT%20for%20a%20single%20asset%20in%20a%20corporate%20wrapper.pdf

of a comprehensive review of an existing IFRS or the development of a new Standard (see paragraph 4.6 of the *Due Process Handbook*). In other words, the IASB is already considering whether a project to revise IAS 12 in its entirety should be performed.

Comments received—ESMA

20. ESMA agrees with the Interpretations Committee's tentative decision not to add the issue to its agenda because it requires a broader project than the Interpretations Committee could perform on behalf of the IASB.

21. However, ESMA is concerned that referring the issue to the IASB's research project on Income Taxes implies that the existing diversity in practice on this issue will remain over a long period of time before the IASB is able to address the issue. Consequently, ESMA recommends that the IASB should address the issue in a narrow-scope project to amend IAS 12 on a timely basis.

22. ESMA thinks that the issue can be addressed by the IASB in a separate narrow-scope project to amend IAS 12, because the diversity in practice is caused by the concern that IAS 12 requires recognising the deferred tax related to both the asset inside and the shares, even if the likelihood and timing of the realisation of the tax consequences represented by deferred tax related to the asset inside is remote. In particular, ESMA explains:

> ESMA agrees with the IFRS IC's decision not to add this specific topic to its active agenda as the issue requires a broader project than the IFRS IC could perform on behalf of the IASB. However, ESMA is concerned that the decision to recommend to the IASB to analyse and assess the issue in its broad research project on *Income Taxes* implies that the existing diversity in practice related to the accounting for deferred taxes in corporate wrapper structures would continue over a long period of time.
>
> ESMA notes that diversity in the recognition and measurement of deferred taxes for corporate wrapper structures is widespread, notably in the real estate

> industry. This diversity is caused by the concerns with respect to the current IAS 12 requirements, which result in the recognition of deferred tax for both the asset encapsulated into the corporate wrapper and the shares of the corporate wrapper, even if the likelihood and timing of the consumption of the deferred tax related to the asset is remote.
>
> Therefore, ESMA believes that the issue is too broad to be addressed by the IFRS IC, but is sufficiently limited to be dealt with by the IASB as a narrow scope project resulting in an amendment of IAS 12. Accordingly, ESMA urges the IFRS IC to refer this matter to the IASB with an invitation for them to address the issue as a separate project on a timely basis.

Staff analysis about comments from ESMA

23. The concern that IAS 12 requires recognising the deferred tax related to both the asset inside and the shares, even if the likelihood and timing of the realisation of the tax consequences represented by the deferred tax related to the asset inside is remote, is one of the concerns that the Interpretations Committee discussed at its meeting in March 2014 after consulting IASB members (see paragraph 29(a) of Staff Paper 3 presented at the March 2014 Interpretations Committee meeting).[3] It discussed this concern as part of the analysis on the concerns raised by commentators in respect of the existing requirements in IAS 12. As a result of this discussion, the Interpretations Committee noted that analysing and assessing these concerns would require a broader project than the Interpretations Committee could perform on behalf of the IASB.

[3] http://www.ifrs.org/Meetings/MeetingDocs/Interpretations%20Committee/2014/March/AP03%20-%20Cover%20note%20-%20IAS%2012%20Recognition%20of%20DT%20for%20a%20single%20asset%20in%20a%20corporate%20wrapper.pdf

24. Furthermore, we do not see that the issue can be addressed in a narrow-scope project to amend IAS 12. This is because the Interpretations Committee noted that:

(a) the deferred tax accounting in respect of which concerns are raised by commentators results from the application of the fundamental principles in IAS 12;

(b) the concern that IAS 12 requires recognising the deferred tax related to both the asset inside and the shares, even if the likelihood and timing of the realisation of the tax consequences represented by the deferred tax related to the asset inside is remote (see paragraph 22), is not the sole concern that is raised by commentators in respect of the existing requirements in IAS 12. We noted further concerns (see paragraph 29 of Staff Paper 3 presented at the March 2014 Interpretations Committee meeting)[4] and we think a narrow-scope project to amend IAS 12 would need to analyse and assess all of them; and

(c) our analysis of the concerns raised by commentators with respect to the existing requirements in IAS 12 did not clearly indicate that the requirements in IAS 12 should be amended to address these concerns (see paragraphs 28–59 of Staff Paper 3 presented at the March 2014 Interpretations Committee meeting[5] and paragraphs 1–33 of Staff Paper 3A presented at the March 2014 Interpretations Committee meeting[6]). There are significant arguments that support the existing accounting requirements in IAS 12. The Interpretations Committee's analysis and

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[4] http://www.ifrs.org/Meetings/MeetingDocs/Interpretations%20Committee/2014/March/AP03%20-%20Cover%20note%20-%20IAS%2012%20Recognition%20of%20DT%20for%20a%20single%20asset%20in%20a%20corporate%20wrapper.pdf

[5] http://www.ifrs.org/Meetings/MeetingDocs/Interpretations%20Committee/2014/March/AP03%20-%20Cover%20note%20-%20IAS%2012%20Recognition%20of%20DT%20for%20a%20single%20asset%20in%20a%20corporate%20wrapper.pdf

[6] http://www.ifrs.org/Meetings/MeetingDocs/Interpretations%20Committee/2014/March/AP03A%20-%20Appendix%20A%20-%20IAS%2012%20Recognition%20of%20DT%20for%20a%20single%20asset%20in%20a%20corporate%20wrapper.pdf

the consultation of the IASB members highlighted pros and cons of both the accounting required by IAS 12 (see also the argument highlighted by CPC, which is reproduced in paragraph 18) and an accounting that responds to the concerns raised by commentators in respect of these requirements.

25. Consequently, we disagree with ESMA that the IASB can address the issue of this Staff Paper in a separate narrow-scope project to amend IAS 12 and do not think that the Interpretations Committee should suggest such a separate narrow-scope project to the IASB. Nevertheless, we think that ESMA's proposal could be considered as part of a broader IASB project on Income Taxes.

Comments received—EY

26. EY supports the Interpretations Committee's decision not to take the issue onto its agenda and recommends that the IASB should analyse and assess the concerns raised by considering them in its research project on Income Taxes.

27. However, EY makes the criticism that the tentative agenda decision describes only one of the three approaches that have been identified as being applied in practice, thereby implying that it is the only acceptable approach. EY would consider it unfortunate if the agenda decision were to result in a change in practice before the IASB had even undertaken the analysis and assessment of the concerns raised. To avoid this, the agenda decision should (1) describe the issue, (2) acknowledge the existing diversity in practice and (3) outline the recommendation of the Interpretations Committee to the IASB. In particular, EY explains:

> … Nevertheless, we disagree with the Tentative Agenda Decision, as worded in the March 2014 IFRIC Update.
>
> In May 2012, the Committee identified three different approaches that are applied in practice in accounting for deferred tax when (1) tax law attributes separate tax bases to the asset inside and the parent's investment in the shares and (2) each tax base is separately deductible for tax purposes. At the time the Committee decided not to recommend an Annual Improvement, but to explore further

options to address this issue. In March 2014, the Committee's concluded that analysing and assessing the concerns raised would require a broader project than the Committee could perform on behalf of the IASB.

We therefore do not understand why the Tentative Agenda Decision describes only one of the three approaches applied in practice, thereby implying that it is the only acceptable approach. It would be unfortunate if this agenda decision were to result in a change in practice before the Board undertakes the very analysis of concerns that the Committee has recommended. We believe that the Tentative Agenda Decision would better reflect the inconclusive debate that took place in the Committee by merely: (1) describing the issue; (2) acknowledging the existing diversity in practice; and (3) outlining the recommendation to the Board.

Staff analysis of comments from EY

28. While we agree that the project did not reach a conclusion on whether the existing requirements in IAS 12 should be amended in the light of the concerns raised by commentators in respect to these requirements, we do not think that the debate was inconclusive.

29. The submission to the Interpretations Committee that started this project asked the Interpretations Committee to clarify what tax base paragraph 11 of IAS 12 requires the use of in the case of a single-asset entity and that the submission had noted different views on whether it is the tax base of the asset inside or the tax base of the shares (see Appendix A of Staff Paper 13 presented at the September 2011 Interpretations Committee meeting).[7]

[7] http://www.ifrs.org/Meetings/Documents/IFRICSep11/131109AP13IAS12corporatewrapper.pdf

30. We think the discussions of the Interpretations Committee and the consultation with the IASB members showed that:

    (a) the existing requirements in IAS 12 are clear and, in particular, paragraph 11 of IAS 12 requires the use of the tax base of the asset inside when determining deferred tax related to this asset;

    (b) the diversity in practice does not result from unclear requirements in IAS 12. It results from concerns about the accounting outcome from applying these existing requirements; and

    (c) the discussion identified several important arguments for and against the existing requirements in IAS 12.

31. Consequently, we think the work of the Interpretations Committee was conclusive and productive. It pointed out the existing requirements in IAS 12 and moved the discussion of this issue significantly forward.

32. We think the agenda decision should reflect all the results from the discussions. It should include the conclusion of the Interpretations Committee that the requirements in IAS 12 on the issue raised are clear and it should summarise them: IAS 12 requires to recognise the deferred tax related to both the asset inside and the shares, if tax law attributes separate tax bases to the asset inside and the shares. Without this clarification in the agenda decision, we think that the agenda decision would omit an important result from the Interpretations Committee's discussions.

33. We also think the tentative agenda does not simply imply that only one of the three approaches which have been observed in practice is acceptable. We think the tentative agenda decision is clear in explaining that only one of these approaches is consistent with IAS 12. Consequently, we do not think that the wording of the agenda decision needs to be amended to clarify the existing requirements in IAS 12.

34. In addition, EY explains that the agenda decision should not clarify that only one approach applied in practice is consistent with IAS 12. This is to avoid a change in practice before the IASB addresses the issue as part of a bigger project. Practice should not be changed until then.

35. While we see the benefits of not causing changes to practice until the IASB has addressed the issue as part of a bigger project, we have significant concerns about EY's proposal from our perspective as a standard-setter. This is because we understand that the effect of EY's proposal is that preparers might (mis)understand IAS 12 to be unclear on the issue addressed in this Staff Paper, citing an agenda decision of the Interpretations Committee, although IAS 12 is, on the contrary, clear on this issue. We think that the wording of the agenda decision should, to the extent possible, outline the existing accounting requirements. It should, to the extent possible, avoid uncertainties and misunderstandings.

Comments received—DTT

36. DTT is the only commentator that disagrees with the tentative decision not to take the issue onto the Interpretations Committee agenda. DTT disagrees because they think that:

    (a) the tentative agenda decision provides only one possible description of the current requirements of IAS 12;

    (b) diversity in practice exists because other treatments lead to better financial reporting in a jurisdiction where (as a result of local tax considerations) all market participants will purchase and sell property within a corporate shell; and

    (c) the circumstances described in (b) raise important questions relevant to both IAS 12 and IFRS 13 *Fair Value Measurement*, including:

        (i) the relevance of the deferred tax related to the asset inside in a market where this is highly unlikely to crystallise; and

        (ii) whether in consolidated financial statements the fair value of a property should be measured at the price that would be achieved by selling the property itself or at a price that would be achieved by selling the corporate shell.

37. For these reasons, DTT recommends that the Interpretations Committee should add the item to its agenda in order to provide a clear IFRIC Interpretation. In particular, DTT explains:

> We agree that the tentative agenda decision provides one possible description of the current requirements of IAS 12. However, we believe that in a jurisdiction where (as a result of local tax considerations) all market participants will purchase and sell property within a corporate shell there are other treatments that lead to better financial reporting and thus diversity in practice exists. Such circumstances raise important questions relevant to both IAS 12 and IFRS 13 *Fair Value Measurement*, including:
>
> - the relevance of the 'inside basis' deferred tax asset or liability in a market where this is highly unlikely to crystallise; and
> - whether in consolidated financial statements the fair value of a property should be measured at the price that would be achieved by selling the property itself (a buyer would logically pay less for an asset purchased in a tax inefficient manner) or at a higher price that would be achieved by selling the corporate shell.
>
> For these reasons, we do not believe that an agenda decision is the appropriate means to address this issue and recommend that the Committee add this item to its agenda with a view to providing a clear interpretation.

Staff analysis of comments from DTT

38. DTT argues that accounting treatments other than the one described in the tentative agenda decision exist, which result in better financial reporting for jurisdictions where, as a result of local tax consideration, all market participants will purchase and sell property within a corporate shell. This argument has been considered in the discussions of the Interpretations Committee and the consultation with the IASB members.

39. In particular, proposal 2 (Unit of account), which was presented in paragraph 15 of Staff Paper 3A for the March 2014 Interpretations Committee meeting[8], required for its proposed application that the asset inside is usually bought and sold in the jurisdiction by buying and selling the shares in the entity housing it.

40. Nevertheless, the Interpretations Committee did not decide to amend IAS 12 to consider the concerns raised by commentators in respect of the existing requirements of IAS 12. It noted that analysing and assessing these concerns would require a broader project than the Interpretations Committee could perform on behalf of the IASB.

41. We think that DTT's reference to the important questions on IAS 12 and IFRS 13 in their comment letter actually supports the Interpretations Committee's conclusion presented in paragraph 40. DTT explains that in developing the IFRIC Interpretation recommended by them, the Interpretations Committee would need to analyse and assess:

    (a) the relevance of the deferred tax asset, or the deferred tax liability, related to the asset inside in a market where this asset or liability is unlikely to crystallise; and

    (b) whether in consolidated financial statements the fair value of a property should be measured at the price that would be achieved by selling the property itself or at a higher price that would be achieved by selling the corporate shell.

42. We think analysing and assessing both questions would require a broader project than the Interpretations Committee could perform on behalf of the IASB. We note that:

    (a) the Interpretations Committee reached this conclusion for the argument in paragraph 41(a) at its meeting in March 2014. It is one of the concerns raised by commentators with respect to the existing

[8] http://www.ifrs.org/Meetings/MeetingDocs/Interpretations%20Committee/2014/March/AP03A%20-%20Appendix%20A%20-%20IAS%2012%20Recognition%20of%20DT%20for%20a%20single%20asset%20in%20a%20corporate%20wrapper.pdf

requirements in IAS 12 which the Interpretations Committee discussed at its March 2014 meeting (see paragraph 29(a) of Staff Paper 3 presented at the March 2014 Interpretations Committee meeting).[9]

(b) the issue reproduced in paragraph 41(b) raises multiple questions related to fair value measurement and the impact of taxation on fair value measurement in scenarios in which the deferred tax issue that is addressed in this Staff Paper arises. Consequently, we think it should be analysed and assessed in the same project as the concern in paragraph 41(a) and the other concerns raised by commentators in respect of the existing requirements in IAS 12.

43. Furthermore, we do not think that an IFRIC Interpretation can address the issue in order to introduce the accounting that differs from the one described in the tentative agenda decision. This is because IFRIC Interpretations must not change or conflict with IFRSs (paragraph 7.8 of the *Due Process Handbook*).

44. The tentative agenda decision does not provide only one of several possible descriptions of the existing requirements in IAS 12. It describes the existing requirements in IAS 12. The Interpretations Committee discussed the issue at four meetings and consulted the IASB on it. In every meeting, the Interpretations Committee noted/confirmed that the IAS 12 requires the parent to recognise both the deferred tax related to the asset inside and the deferred tax related to the shares, if tax law allocates separate tax bases to them.

45. Consequently, we think that an IFRIC Interpretation is not an option to address the issue discussed in this Staff Paper.

[9] http://www.ifrs.org/Meetings/MeetingDocs/Interpretations%20Committee/2014/March/AP03%20-%20Cover%20note%20-%20IAS%2012%20Recognition%20of%20DT%20for%20a%20single%20asset%20in%20a%20corporate%20wrapper.pdf

Staff recommendation

46. After considering the comments received on the tentative agenda decision, the previous discussions of the Interpretations Committee and the results from the consultations with IASB members, we think the Interpretations Committee reached the correct conclusions in its previous discussions (see paragraphs 4–11).

47. The comments received did not present any relevant argument that the Interpretations Committee has not considered in its previous discussions.

48. DTT and EY disagree with the conclusion that the existing requirements are clear, however they do not explain which paragraphs in IAS 12 cause the requirements to be unclear and why.

49. Practice is divided on the question of whether the existing requirements in IAS 12 lead to appropriate accounting results. Some support the existing accounting requirements, whereas others believe that other treatments lead to a better financial reporting in a jurisdiction where, as a result of local tax considerations, all market participants will purchase and sell property within a corporate shell (see also the comments letter from CPC and DTT).

50. Consequently, we recommend that the Interpretations Committee should finalise its decision not to add this issue to its agenda. The agenda decision should be finalised without any changes to the wording of the tentative decision. The wording of the final agenda decision is included in Appendix A.

Questions for the Interpretations Committee

Questions for the Interpretations Committee
1. Does the Interpretations Committee agree with the staff's recommendation that the Interpretations Committee should finalise its decision not to add this issue to its agenda? 2. Does the Interpretations Committee have any comments on the proposed wording in Appendix A for the final agenda decision?

Appendix A—Proposed wording for the final agenda decision

A1. The proposed wording for the final agenda decision is as follows (deleted text is struck through):

IAS 12 *Income Taxes*—recognition of deferred tax for a single asset in a corporate wrapper

The Interpretations Committee received a request to clarify the accounting for deferred tax in the consolidated financial statements of the parent, when a subsidiary has only one asset within it (the asset inside) and the parent expects to recover the carrying amount of the asset inside by selling the shares in the subsidiary (the shares).

The Interpretations Committee noted that:

a. Paragraph 11 of IAS 12 requires the entity to determine temporary differences in the consolidated financial statements by comparing the carrying amounts of assets and liabilities in the consolidated financial statements with the appropriate tax base. In the case of an asset or liability of a subsidiary that files separate tax returns, this is the amount that will be taxable or deductible on the recovery (settlement) of the asset (liability) in the tax returns of the subsidiary.

b. The requirement in paragraph 11 of IAS 12 is complemented by the requirement in paragraph 38 of IAS 12 to determine the temporary difference related to the shares of the parent in the subsidiary by comparing the parent's share of the net assets of the subsidiary in the consolidated financial statements, including the carrying amount of goodwill, with the tax base of the shares for purposes of the parent's tax returns.

The Interpretations Committee also noted that these paragraphs require a parent to recognise both the deferred tax related to the asset inside and the deferred tax related to the shares, if:

- tax law attributes separate tax bases to the asset inside and the shares;
- in the case of deferred tax assets, the related deductible temporary differences can be utilised as specified in paragraphs 24-31 of IAS 12; and
- no specific exceptions in IAS 12 apply.

The Interpretations Committee noted that several concerns were raised with respect to the current requirements in IAS 12. However, analysing and assessing these concerns requires a broader project than the Interpretations Committee could perform on behalf of the IASB.

Consequently, the Interpretations Committee ~~[~~decided~~]~~ not to take the issue onto its agenda but instead to recommend to the IASB that it should analyse and assess these concerns in its research project on Income Taxes.

Appendix B—Comment letters received on the tentative agenda decision

B1. We received five comment letters on the tentative agenda decision IAS 12 *Income Taxes*—recognition of deferred tax for a single asset in a corporate wrapper in the *IFRIC Update* of March 2014:

(a) Accounting Standards Board (AcSB), Canada, as of 9 June 2014;

(b) Brazilian Accounting Pronouncements Committee (CPC), as of 30 May 2014;

(c) Deloitte Touche Tohmatsu Limited (DTT), as of 9 June 2014;

(d) European Securities and markets Authority (ESMA), as of 4 June 2014; and

(e) Ernst & Young Global Limited (EY), as of 9 June 2014.

B2. In this sequence, the comment letters are attached to this Staff Paper.

Accounting Standards Board AcSB CNC Conseil des normes comptables

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June 9, 2014

(By e-mail to ifric@ifrs.org)

IFRS Interpretations Committee
30 Cannon Street,
London EC4M 6XH
United Kingdom

Dear Sirs,

Re: Tentative agenda decisions arising from the Committee's March meeting

This letter is the response of the staff of the Canadian Accounting Standards Board (AcSB) to the IFRS Interpretations Committee's tentative agenda decisions published in the March 2014 IFRIC Update.

The views expressed in this letter take into account comments from individual members of the AcSB staff but do not necessarily represent a common view of the AcSB or its staff. Views of the AcSB are developed only through due process.

We agree with the Committee's tentative decisions not to add any of the four items to its agenda. In the case of the issues involving IAS 12, IAS 34 and IAS 39, we agree with the Committee's stated reasons for its conclusions.

In the case of the IAS 1 issue, we cannot identify a clear, direct statement of the Committee's reason(s) for not taking that issue onto its agenda. We think it might help constituents if such a statement could be drafted into the final version of the decision. In that connection, we note the Committee's final agenda decision on issue IAS 1-5 in July 2010.

We do not understand the comment in the discussion of the IAS 1 issue that paragraph 122 of that standard would apply to going concern. Paragraph 122 deals with disclosures of judgments made in applying an entity's accounting policies. We do not think that a judgment as to whether an entity is a going concern is a matter of accounting policy. Rather, it is a judgment of fact concerning a more fundamental issue. The discussion of going concern within IAS 1 is separated from paragraph 122 by almost 100 paragraphs of discussion on other topics, which suggests that they are not closely related issues. If the Committee nevertheless continues to think that paragraph 122 does apply to going concern uncertainties, it could propose to the IASB that going concern be added to the list of examples in paragraph 123 through an annual improvement. However, we think that, if any clarification to IAS 1 is desirable, a more logical approach would be to add to the disclosure requirement in the third sentence in paragraph 25 of IAS 1. That sentence could be amended to add a requirement to disclose the judgments made in concluding whether there are material uncertainties related to events or conditions that may cast doubt upon the entity's ability to continue as a going concern. Readers of IAS 1 would be more likely to notice and apply such a requirement while considering the other going concern requirements than if the disclosure requirement were included in paragraphs 122-123.

We would be pleased to provide more detail if you require. If so, please contact me at +1 416 204-3276 (e-mail pmartin@cpacanada.ca), or Rebecca Villmann, Director-designate, Accounting Standards at +1 416 204-3464 (email rvillmann@cpacanada.ca).

Yours truly,

Peter Martin

Peter Martin, CPA, CA
Director, Accounting Standards

May 30, 2014

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International Accounting Standards Board
IFRS Interpretations Committee
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RE: Outreach Request - IAS 12 - Income Taxes - Recognition of deferred tax for a single asset in a corporate wrapper

Dear Board Members,

The Comitê de Pronunciamentos Contábeis - CPC (Brazilian Accounting Pronouncements Committee)[1] welcomes the opportunity to respond to the Outreach Request – IAS 12 - Income Taxes - Recognition of deferred tax for a single asset in a corporate wrapper.

We are a standard-setting body engaged in the study, development and issuance of accounting standards, interpretations and guidance for Brazilian companies.

Background of the issue

The Interpretations Committee received a request to clarify the accounting for deferred tax in the consolidated financial statements of the parent, when a subsidiary has only one asset within it (the asset inside) and the parent expects to recover the carrying amount of the asset inside by selling the shares in the subsidiary (the shares).

The Interpretations Committee noted significant diversity in practice in accounting for deferred tax when tax law attributes separate tax bases to the asset inside and the parent's investment in the shares and each tax base is separately deductible for tax purposes:

a) some follow the tax perspective and recognise deferred tax related to both the asset inside and the shares; while
b) others recognise only the deferred tax related to the shares.
c) A third group of preparers determines deferred tax by comparing the carrying amount (in the consolidated financial statements) of the asset inside with the tax base of the shares and using the tax rate that applies if the parent recovers the carrying amount of the shares.

The Interpretations Committee also noted that current IAS 12 requires the parent to recognize both the deferred tax related to the asset inside and the deferred tax related

[1] The Brazilian Accounting Pronouncements Committee (CPC) is a standard-setting body engaged in the study, development and issuance of accounting standards, interpretations and guidances for Brazilian companies. Our members are nominated by the following entities: ABRASCA (Brazilian Listed Companies Association), APIMEC (National Association of Capital Market Investment Professionals and Analysts), BMFBOVESPA (Brazilian Stock Exchange and Mercantile & Future Exchange), CFC (Federal Accounting Council), FIPECAFI (Financial and Accounting Research Institute Foundation) and IBRACON (Brazilian Institute of Independent Auditors).

to the shares, if tax law considers the asset inside and the shares to be two separate assets and if no specific exceptions in IAS 12 apply.

The Interpretations Committee noted that such amendments would be more than simply clarifying or correcting in nature and would therefore be beyond the scope of the Annual Improvements project. However, targeted narrow-scope amendments to IAS 12 could be developed by the Interpretations Committee in consultation with the IASB as separate amendments to IAS 12 (limited scope project to amend IAS 12).

Consequently, the staff analysed whether the requirements of IAS 12 should be amended in a limited scope project to amend IAS 12 in response to the concerns raised by commentators and consulted IASB members at various meetings in December 2013 to obtain their individual views on possible amendments to the principles in IAS 12.

Our comments

The paragraphs 11 and 38 of IAS 12 require distinguishing between the asset inside and the shares in the subsidiary in accounting for deferred taxes in the consolidated financial statements, if tax law distinguishes both assets. In our jurisdiction, the income taxes are based on the results of each entity and not on a consolidated basis.

We analyse the Staff Paper (March 2014) and on the basis of this analysis we agree with the argument that the deferred tax liability related to the asset inside represents future tax payments that result from achieving taxable inflows of economic benefits by using the asset inside. These tax payments affect the value of the shares in the subsidiary.

Thus, if the tax law attributes separate tax bases to the asset inside, and the parent's investment in the shares and each tax base is separately deductible for tax purposes (ie tax law considers the asset inside and the parent's investment in the shares to be two separate assets), we agree that the entity must recognize deferred tax related to both the asset inside and the subsidiary's shares.

So, we support the decision made by the Interpretations Committee related to this project, i.e., not to require an interpretation or an amendment in the IAS 12 or IFRS 10. However, we recommend that the IASB consider performing a complete project to revise entirely the IAS 12.

If you have any questions about our comments, please contact us at operacoes@cpc.org.br.

Yours sincerely,

Idésio da Silva Coelho Júnior
Chair of International Affairs
Comitê de Pronunciamentos Contábeis (CPC)

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Wayne Upton
Chairman
IFRS Interpretations Committee
30 Cannon Street
London
United Kingdom
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Email: ifric@ifrs.org

9 June 2014

Dear Mr Upton

Tentative agenda decision - IAS 12 *Income Taxes*: Recognition of deferred tax for a single asset in a corporate wrapper

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the March IFRIC Update of the tentative decision not to take onto the Committee's agenda a request for guidance on the accounting for deferred tax in the consolidated financial statements of a parent that has a subsidiary with only one asset within it and expect to recover the value of that asset by selling shares in the subsidiary.

We agree that the tentative agenda decision provides one possible description of the current requirements of IAS 12. However, we believe that in a jurisdiction where (as a result of local tax considerations) all market participants will purchase and sell property within a corporate shell there are other treatments that lead to better financial reporting and thus diversity in practice exists. Such circumstances raise important questions relevant to both IAS 12 and IFRS 13 *Fair Value Measurement*, including:

- the relevance of the 'inside basis' deferred tax asset or liability in a market where this is highly unlikely to crystallise; and
- whether in consolidated financial statements the fair value of a property should be measured at the price that would be achieved by selling the property itself (a buyer would logically pay less for an asset purchased in a tax inefficient manner) or at a higher price that would be achieved by selling the corporate shell.

For these reasons, we do not believe that an agenda decision is the appropriate means to address this issue and recommend that the Committee add this item to its agenda with a view to providing an clear interpretation.

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0)20 7007 0884.

Yours sincerely

Veronica Poole
Global IFRS Leader

European Securities and Markets Authority

The Chair

Date: 4 June 2014
ESMA/2014/602

Wayne Upton
Chair
IFRS Interpretations Committee
30 Cannon Street
London, EC4M 6XH
United Kingdom

Re: The IFRS Interpretations Committee's tentative agenda decision on IAS 12 – *Income Taxes*: recognition of deferred tax for a single asset in a corporate wrapper

Dear Mr. Upton,

The European Securities and Markets Authority (ESMA) thanks you for the opportunity to respond to the IFRS Interpretations Committee's (IFRS IC) publication in the March IFRIC Update of the tentative decision related to application of IAS 12 – *Income Taxes*. We are pleased to provide you with the following comments with the aim of improving the consistent application and enforceability of IFRSs.

ESMA has considered the IFRS IC's tentative decision not to add to its agenda the request for clarification it received on the accounting for deferred tax in the consolidated financial statements of the parent, when a subsidiary has only one asset and the parent expects to recover the carrying amount of this asset by selling all the shares in that subsidiary.

ESMA agrees with the IFRS IC's decision not to add this specific topic to its active agenda as the issue requires a broader project than the IFRS IC could perform on behalf of the IASB. However, ESMA is concerned that the decision to recommend to the IASB to analyse and assess the issue in its broad research project on *Income Taxes* implies that the existing diversity in practice related to the accounting for deferred taxes in corporate wrapper structures would continue over a long period of time.

ESMA notes that diversity in the recognition and measurement of deferred taxes for corporate wrapper structures is widespread, notably in the real estate industry. This diversity is caused by the concerns with respect to the current IAS 12 requirements, which result in the recognition of deferred tax for both the asset encapsulated into the corporate wrapper and the shares of the corporate wrapper, even if the likelihood and timing of the consumption of the deferred tax related to the asset is remote.

Therefore, ESMA believes that the issue is too broad to be addressed by the IFRS IC, but is sufficiently limited to be dealt with by the IASB as a narrow scope project resulting in an amendment of IAS 12. Accordingly, ESMA urges the IFRS IC to refer this matter to the IASB with an invitation for them to address the issue as a separate project on a timely basis.

We would be happy to discuss these issues further with you.

Steven Maijoor
Chair
European Securities and Markets Authority

Cc: Hans Hoogervorst, Chairman, International Accounting Standards Board

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Committee
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9 June 2014

Dear IFRS Interpretations Committee members

Invitation to comment – *Tentative agenda decision – IAS 12 Income Taxes– Recognition of deferred tax for a single asset in a corporate wrapper*.

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on the above tentative agenda decision of the IFRS Interpretations Committee ('Committee') published in the March 2014 IFRIC Update.

The Committee received "a request to clarify the accounting for deferred tax in the consolidated financial statements of the parent, when a subsidiary has only one asset within it (the asset inside) and the parent expects to recover the carrying amount of the asset inside by selling the shares in the subsidiary (the shares)."

We support the Committee's decision not to take the issue onto its agenda and we recommend that the IASB analyses and assesses these concerns in its research project on income taxes. Nevertheless, we disagree with the Tentative Agenda Decision, as worded in the March 2014 IFRIC Update.

In May 2012, the Committee identified three different approaches that are applied in practice in accounting for deferred tax when (1) tax law attributes separate tax bases to the asset inside and the parent's investment in the shares and (2) each tax base is separately deductible for tax purposes. At the time the Committee decided not to recommend an Annual Improvement, but to explore further options to address this issue. In March 2014, the Committee's concluded that analysing and assessing the concerns raised would require a broader project than the Committee could perform on behalf of the IASB.

We therefore do not understand why the Tentative Agenda Decision describes only one of the three approaches applied in practice, thereby implying that it is the only acceptable approach. It would be unfortunate if this agenda decision were to result in a change in practice before the Board undertakes the very analysis of concerns that the Committee has recommended. We believe that the Tentative Agenda Decision would better reflect the inconclusive debate that took place in the Committee by merely: (1) describing the issue; (2) acknowledging the existing diversity in practice; and (3) outlining the recommendation to the Board.

Should you wish to discuss the contents of this letter with us, please contact Leo van der Tas at the above address or on +44 (0)20 7951 3152.

Yours faithfully

Ernst & Young