STAFF PAPER

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IASB Meeting

Project	**Deferred Tax Related to Assets and Liabilities arising from a Single Transaction (Amendments to IAS 12)**
Paper topic	Feedback Summary—Alternative approaches, transition and other comments

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Introduction and structure

1. As discussed in Agenda Paper 12G for this meeting, this paper summarises feedback on particular aspects of the proposed amendments to IAS 12 *Income Taxes*, included in the Exposure Draft *Deferred Tax related to Assets and Liabilities arising from a Single Transaction*. In particular, this paper summarises:
   (a) respondents' suggestions on alternate approaches to address the matter (paragraphs 2–9);
   (b) feedback on the proposed transition requirements (paragraphs 10–11); and
   (c) requests for application guidance and examples, and other comments (paragraphs 12–14).

Alternative approaches

2. This section summarises the following alternative approaches suggested by respondents who disagree with particular aspects of the proposed amendments:
   (a) applying a 'net approach' (paragraphs 3–4);
   (b) requiring attribution of tax deductions to the asset (paragraph 5);

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(c) removing the capping proposal (paragraph 6);

(d) developing an interpretation (paragraph 7); and

(e) broader review of IAS 12 and the recognition exemption (paragraphs 8–9).

Applying a 'net' approach

3. Some suggest requiring a 'net' approach, according to which an entity would consider an asset and liability arising from a single transaction (such as a lease) as a single unit of account when applying IAS 12. A few respondents acknowledge that this approach would be inconsistent with the requirements in IAS 12—which applies to assets and liabilities separately—but nonetheless say there is merit in considering such an approach. EFRAG explains the net approach and says:

> EFRAG considers that the single unit of account (referred to as the net approach) perspective has conceptual merits in reflecting that the transaction is a single contract (in the case of a lease) or a single transaction. Furthermore, applying the net approach will solve the operational issues that arise on initial recognition in cases where the recognition 'cap' under paragraph 22A(b) of the [Exposure Draft] needs to be applied. Under the net approach, on the initial recognition no deferred tax or liability would be recognised as their net amount would be nil. In subsequent periods, an entity would apply the principles in IAS 12.

4. However, EY says:

> [The net approach] is often applied to decommissioning obligations that are not fully tax deductible. However, the approach may be less attractive to apply in case of a large portfolio of leases, as it would require an entity to maintain a link between each right-of-use asset and its corresponding lease liability.

Requiring attribution of tax deductions to the asset

5. In the FRC (UK)'s view, the proposed amendments are not the most cost-effective way of achieving the Board's objectives. As discussed in paragraph 28 of Agenda

Paper 12H, the FRC (UK) instead suggests requiring entities to assume that tax deductions relate to the asset. It says such an approach would remove many of the complexities inherent in the proposed amendments.

Removing the capping proposal

6. As discussed in Agenda Paper 12H, many respondents say the proposed amendments (and in particular the capping proposal) would be complex to apply. As discussed in paragraphs 10–11 of Agenda Paper 12H, a few respondents suggest removing the capping proposal and either:

   (a) recognising any initial difference between the deferred tax asset and liability in profit or loss; or

   (b) limiting the scope of the proposed amendments so that they would apply only in situations in which it is readily determinable that the recoverability requirement is fully met (ie situations in which an entity recognises the full amount of deferred tax asset).

Developing an Interpretation

7. Deloitte suggests addressing the matter through an Interpretation (as discussed in paragraph BC13–BC15 of the Exposure Draft). Such an interpretation would explain how an entity applies the requirements in IAS 12 without changing the scope of the recognition exemption. This approach could result in an entity not recognising deferred tax assets or liabilities on initial recognition of a lease when tax deductions relate to the lease liability.

Broader review of IAS 12 and the recognition exemption

8. Some say the proposed amendments highlight broader concerns about the application of IAS 12, particularly the recognition exemption. Of these respondents:

   (a) some suggest removing the recognition exemption—in their view, the exemption is inappropriate and leads to inadequate financial information; and

   (b) a few suggest undertaking a comprehensive review of IAS 12.

9. A few suggest finalising the proposed amendments and then undertaking a review of the recognition exemption or, more broadly, IAS 12.

Proposed transition requirements

Background

10. The Board proposed requiring entities to apply the amendments retrospectively, but to provide relief in relation to the assessment of the recoverability requirement—an entity would be permitted to assess the recoverability requirement only at the beginning of the earliest comparative period presented. Paragraphs BC33–BC37 of the Exposure Draft explain the Board's rationale:

> BC33 Apart from assessing the recoverability requirement, retrospective application would require entities to consider only the amount of temporary differences that exist at the beginning of the earliest comparative period presented, and apply applicable tax rates at that date to those temporary differences. At that date, any temporary differences affected by the proposed amendments would generally equal the carrying amounts of the related asset or liability (see paragraph BC31(b)). Accordingly, the Board expects that entities would not incur undue costs in applying the amendments retrospectively.
>
> **Transition relief**
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> BC34 The proposed amendments would require the recognition of deferred tax assets and liabilities for particular transactions to the extent that an entity recognises a deferred tax asset and liability of the same amount. To the extent that an entity does not recognise a deferred tax asset because of the recoverability requirement, it would also not recognise a deferred tax liability.
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> BC35 As a consequence, retrospective application of the proposed amendments would require an entity to assess the recoverability requirement on initial recognition of the

> transaction that gave rise to the temporary differences. For both leases and decommissioning obligations, an entity might have initially recognised the related transaction some considerable time ago. In such situations, assessing the recoverability requirement could be impracticable or result in undue costs.
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> BC36 IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* does not require an entity to apply a change retrospectively to the extent that retrospective application is impracticable. However, to address situations in which applying the recoverability requirement retrospectively is not impracticable but may result in undue costs, the Board decided to provide transition relief that would permit an entity to assess the recoverability requirement only at the beginning of the earliest comparative period presented.
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> BC37 The Board decided to make the proposed transition relief optional. The different views on the existing requirements in IAS 12 mean that some entities may already have applied accounting that is aligned with the proposed amendments. Therefore, making the transition relief mandatory could result in some entities being required to change their accounting solely because of the transition relief. The Board concluded that this outcome would be undesirable.

Feedback

11. Many respondents do not comment on the proposed transition requirements. A few respondents explicitly agree with the proposed transition requirements, however a few disagree. In particular:

    (a) a few say the calculation of deferred tax assets or liabilities for the earliest comparative period could (i) be challenging and (ii) result in undue costs. For example, RioTinto says:

    > We consider that requiring entities to retrospectively assess deferred tax asset (DTA) recoverability without hindsight in all comparatives presented is likely to result in significant re-work

and re-calculation of previously reported amounts (including for example gains or losses arising from divestments and impairment charges), where such adjustment is virtually meaningless.

These respondents suggest requiring or permitting entities to apply the amendments retrospectively with the cumulative effect recognised at the date of initial application of the amendments (ie without restatement of comparative periods).

(b) Deloitte suggests permitting entities to recognise and measure deferred tax based on the temporary differences determined at the beginning of the earliest comparative period presented with the difference recognised in opening retained earnings (or other component of equity). They say this approach would be appropriate considering that deferred tax assets and liabilities are reassessed and remeasured at each reporting period.

(c) A few say the proposed transition requirements could lead to different accounting outcomes for economically similar situations depending on whether an entity applies the transition relief—this is because, applying the amendments retrospectively, an entity assesses the recoverability requirement at the date of the transaction, which could be some time ago. However, applying the transition relief, it assesses the recoverability requirement at the beginning of the earliest comparative period presented.

(d) A few ask how the proposed transition requirements interact with IFRS 16's transition requirements. For example, RSM International says applying the transition relief in IFRS 16, it is possible that the carrying amount of the lease asset and lease liability will not be the same at the date of initial application of IFRS 16—it suggests clarifying whether the amendments would apply in this situation.

(e) KPMG suggests allowing an entity to apply the amendments retrospectively only to the extent the entity can do so without the use of hindsight.

(f) Abrasca – Brazilian Association of Publicly-Held Companies suggests including transition requirements for entities that already recognise deferred tax on leases.

Requests for application guidance and examples, and other comments

Requests for application guidance and illustrative examples

12. Many respondents suggest providing application guidance and examples illustrating the application of the proposed amendments—in their view, the proposed amendments would be difficult to understand and apply without such guidance and examples. Respondents suggest including application guidance and examples illustrating how an entity applies:

    (a) the requirement to assess whether tax deductions are attributable to the lease asset or lease liability;

    (b) the proposed amendments to a lease with advance payments and initial direct costs (see also paragraphs 30–33 of Agenda Paper 12H);

    (c) the capping proposal, including the subsequent accounting for the deferred tax asset and liability (see also paragraphs 16–22 of Agenda Paper 12H);

    (d) the proposed amendments when the entity has pre-existing deferred tax assets related to unrecognised tax losses (see also paragraph 8 of Agenda Paper 12H); and

    (e) the proposed transition requirements.

13. A few respondents suggest explaining how to account for deferred tax if an entity subsequently adjusts the carrying amount of a lease asset or lease liability, such as when it modifies a lease or otherwise reassesses the lease liability.

Other comments

14. Some respondents make other comments including the following:

    (a) EY suggests requiring entities to disclose information to help users of financial statements understand the amount and nature of any unrecognised deferred tax liabilities.

    (b) The Institute of Singapore Chartered Accountants suggests providing practical expedients, such as allowing an entity to apply the proposed amendments to a portfolio of leases rather than to each individual lease. In its view, this could help reduce the cost of applying the amendment.

    (c) A few say paragraphs 15, 22 and 24 of IAS 12 refer to the initial recognition of an asset *or* liability and not to the initial recognition of an asset *and* a liability. Accordingly, in their view, the proposed amendments introduce inconsistencies within those paragraphs.

    (d) Some suggest drafting improvements.

    (e) A few suggest finalising the proposed amendments as quickly as possible to allow entities to apply the amendments as close to the adoption of IFRS 16 as practicable.