**Need to know**
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# Need to know

## IASB amends IAS 12 for deferred tax related to assets and liabilities arising from a single transaction

Contents



This *Need to know* outlines the recent amendments to IAS 12 *Income Taxes* titled *Deferred Tax related to Assets and Liabilities arising from a Single Transaction* published by the International Accounting Standards Board (Board) in May 2021.

- The amendments introduce an exception to the initial recognition exemption in IAS 12
- Applying this exception, an entity does not apply the initial recognition exemption for transactions that give rise to equal taxable and deductible temporary differences
- The amendments apply to transactions that occur on or after the beginning of the earliest comparative period presented.
- The amendments also apply to taxable and deductible temporary differences associated with right-of-use assets and lease liabilities and decommissioning obligations and corresponding amounts recognised as assets at the beginning of the earliest comparative period presented.
- The amendments are effective for annual reporting periods beginning on or after 1 January 2023. Early application of the amendments is permitted.

### Background

For some transactions, IFRS Standards require the simultaneous recognition of an asset and a liability. A consequence is that IAS 12 could also require the recognition of offsetting temporary differences. Before the amendments, it was not clear whether IAS 12 required recognition of deferred taxes for these temporary differences or whether the initial recognition exemption applied. That exemption prohibits an entity from recognising deferred tax assets and liabilities on initial recognition of an asset or liability in a transaction which is not a business combination and affects neither accounting nor taxable profit.

### The amendments

The Board amends IAS 12 to provide a further exception from the initial recognition exemption. Under the amendments, an entity does not apply the initial recognition exemption for transactions that give rise to equal taxable and deductible temporary differences.

**For more information please see the following websites:**

**www.ukaccountingplus.co.uk**

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Depending on the applicable tax law, equal taxable and deductible temporary differences may arise on initial recognition of an asset and liability in a transaction that is not a business combination and affects neither accounting nor taxable profit. For example, this may arise upon recognition of a lease liability and the corresponding right-of-use asset applying IFRS 16 *Leases* at the commencement date of a lease. Following the amendments to IAS 12, an entity is required to recognise the related deferred tax asset and liability, with the recognition of any deferred tax asset being subject to the recoverability criteria in IAS 12.

The Board also adds an illustrative example to IAS 12 that explains how the amendments are applied.

**Observation**

When the Board exposed the draft amendments, it proposed that the recognition exemption continues to apply to the extent that an entity would otherwise recognise unequal amounts of deferred tax assets and liabilities ("capping"). Applying the capping, an entity would recognise deferred tax assets and liabilities of the same amount and only to the extent that, applying the recoverability requirement, the entity would recognise a deferred tax asset.

The Board decided to remove the capping from the amendments as feedback had shown that it is inconsistent with the principles in IAS 12. In addition, it would have been complex and burdensome to apply.

The amendments might therefore result in the recognition of unequal amounts of deferred tax on initial recognition of a transaction. In such cases, an entity would recognise any difference in profit or loss.

## Transitional provisions and effective date

An entity applies the amendments to transactions that occur on or after the beginning of the earliest comparative period presented.

In addition, at the beginning of the earliest comparative period an entity recognises:

- A deferred tax asset (to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilised) and a deferred tax liability for all deductible and taxable temporary differences associated with:
  - Right-of-use assets and lease liabilities
  - Decommissioning, restoration and similar liabilities and the corresponding amounts recognised as part of the cost of the related asset
- The cumulative effect of initially applying the amendments as an adjustment to the opening balance of retained earnings (or other component of equity, as appropriate) at that date

First-time adopters apply these provisions at the date of transition to IFRS Standards.

The amendments are effective for annual reporting periods beginning on or after 1 January 2023. Application of the amendments before the effective date is permitted.

**Observation**

In the Exposure Draft, the Board proposed full retrospective application for the amendments in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. However, the Board noticed that this would require entities to retrospectively assess whether each lease and decommissioning obligation gave rise to equal taxable and deductible temporary differences on initial recognition.

The Board therefore concluded that the transition approach now included for those items would make the amendments easier and less costly to apply than a full retrospective approach, while achieving the objective of the amendments. This approach also prevents any uncertainties about how the amendments interact with the transition requirements in IFRS 16.

**Application in the UK**
The amendments are not yet endorsed for use in the UK. Given IAS 12 was not clear before the amendments, entities could adopt the accounting in line with the amendment as an accounting policy choice, however this would require full retrospective application in accordance with IAS 8. The transitional provisions of the amendments cannot be applied until the amendment has been endorsed.

## Further information

If you have any questions about the amendments to IAS 12, please speak to your usual Deloitte contact.

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