

Amendment IAS 12 – International Tax Reform – Pillar Two Model Rules Cover Note

Objective

- 1 The objective of this session is to:
 - (a) Introduce the fast-track project to the FRB; and
 - (b) Discuss and agree the approval process for the DCL, FCL, DEA and FEA by EFRAG FRB.

Background

Project Information

- 2 In November 2022, the IASB discussed a [potential amendment to IAS 12](#) as a result of the Organisation for Economic Co-operation and Development (OECD) project. At its November meeting, the IASB tentatively decided to propose amendments to IAS 12 Income Taxes to introduce a temporary exception from accounting for deferred taxes arising from the implementation of the OECD's Pillar Two model rules, as well as targeted disclosures for affected entities. The exposure draft is expected to be published beginning of January 2023 with a comment period of 60 days. The IASB expects to publish the amendments in Q2 2023.
- 3 In October 2021, more than 130 countries – representing more than 90% of global GDP – agreed to implement a [minimum tax regime for multinationals, “Pillar Two”](#). In December 2021, the OECD released the Pillar Two model rules (the Global Anti-Base Erosion Proposal, or “GloBE”) to reform international corporate taxation. Pillar Two aims to ensure that applicable multinationals - with a global turnover exceeding €750 million – are liable to a minimum effective corporate tax rate of 15%.
- 4 The OECD rules are due to be passed into national legislation based on each country's approach. In Europe it is planned that the Council Directive ([here](#)) be approved in the upcoming days and that the individual jurisdictions enact the related law before 31 December 2023. The law will apply in Europe for annual periods starting on 1 January 2024.
- 5 Large multinational enterprises within the scope of the OECD rules are required to calculate their GloBE effective tax rate for each jurisdiction where they are operating. They will be liable to pay a top-up tax for the difference between their GloBE effective tax rate per jurisdiction and the 15% minimum tax rate.
- 6 Applying the GloBE rules and determining their impact on the IFRS financial statements are likely to be complex and result in a number of practical challenges. Top-up tax differs from income taxes that arise under known (local) tax regimes. Traditional income taxes are generally based on a company's taxable profit, while top-up tax will arise only if a group pays an insufficient amount of income taxes at a jurisdictional level. The accounting practical challenges are:
 - (a) Is the top-up tax within the scope of IAS 12;
 - (b) Do the GloBE model rules create additional temporary differences;
 - (c) Which tax rate has to be applied to measure deferred tax impacts of top-up tax; and

- (d) Does a company need to remeasure its existing temporary differences in relation to deferred tax recognised?
- 7 The IASB did not decide whether such top-up tax is within the scope of IAS 37 or of IAS 12. Such decision might depend on the implementation of the OECD rules in the different jurisdictions. If in scope of IAS 12, it is not immediately apparent how an entity would apply the principles and requirements in IAS 12 in accounting for top-up tax arising from the Pillar Two model rules- specifically, whether the recognition and measurement of deferred tax assets and liabilities would be impacted. With uncertainty on whether any jurisdiction (outside the EU) expects to implement the GloBE model rules as early as the first half of 2023, stakeholders were asking for urgent clarity. For these reasons, the IASB in its meeting in November 2022 decided on a fast-track project to do standard-setting in response to the imminent implementation of the Pillar Two model rules.
- 8 In its November meeting the IASB discussed the potential effects of the OECD's Pillar Two model rules on the accounting for income taxes by an entity applying IAS 12 Income Taxes. The IASB tentatively decided to introduce a mandatory temporary exception from accounting for deferred taxes arising from application of the OECD's Pillar Two model rules (including any qualified domestic minimum top-up tax). The mandatory exception would apply until the IASB either removes the exception or makes it permanent.
- 9 In addition, the IASB decided to propose that a company provides new disclosures. There are disclosures before and after top-up tax becomes effective. A company may be required to disclose the following in its annual financial statements for periods beginning on 1 January 2023.
- 10 The IASB tentatively decided to amend IAS 12 to require an entity to disclose, in periods before the Pillar Two model rules are in effect, and for the current period only:
- (a) information about legislation enacted or substantively enacted, to implement the Pillar Two model rules in jurisdictions in which the entity operates.
 - (b) either:
 - (i) whether the entity operates in jurisdictions in which it reasonably expects to be taxed below the minimum rate in accordance with the specific requirements of the Pillar Two model rules; or
 - (ii) whether the entity operates in jurisdictions in which its effective tax rate—calculated based on IAS 12 requirements—is below 15% for the current period.
 - (c) the jurisdictions in which the entity's effective tax rate—calculated based on IAS 12 requirements—for the current period is below 15%. The entity would also disclose, for these jurisdictions in aggregate:
 - (i) the accounting profit before tax;
 - (ii) the income tax expense; and
 - (iii) the resulting weighted-average effective tax rate.
 - (d) the entity would prepare this information by disaggregating information disclosed in the reconciliation required by paragraph 81(c) of IAS 12;
 - (e) whether the work it has already done in preparing to comply with the Pillar Two model rules indicates that there are jurisdictions in relation to which the entity:
 - (i) might be exposed to paying top-up tax and that are not included in the jurisdictions identified in (c); or
 - (ii) might not be exposed to paying top-up tax and that are included in the jurisdictions identified in (c).

- 11 The IASB also tentatively decided to amend IAS 12 to require an entity to disclose (after the Pillar Two model rules are in effect):
- (a) that it has applied the temporary exception; and
 - (b) its current tax expense related to Pillar Two top-up tax.
- 12 The IASB tentatively decided to require an entity to apply:
- (a) the proposed amendments to introduce the temporary exception, and to require an entity to disclose the fact that it has applied that exception, immediately upon the issue of the amendments; and
 - (b) the remaining proposed disclosure requirements for annual reporting periods beginning on 1 January 2023.

EFRAG FR TEG Discussions

- 13 The FR TEG received a short introduction to the project shortly after the IASB meeting but did not discuss key messages for the upcoming DCL. FR TEG members welcomed the IASB fast track project. They provided the following comments:
- (a) EFRAG FR TEG Members generally supported the temporary exception for deferred taxes arising from the enactment of Pillar Two rules. They welcomed the IASB intention not to include a sunset clause as they acknowledged that it would take time for tax specialists to assess the effects of the law.
 - (b) Some FR TEG members discussed the fact that the IASB had not concluded whether OECD's Pillar Two model obligations would be accounted for under the scope of IAS 12. This will allow entities to apply judgment and assess whether the impact of these taxes should be accounted for as income taxes, levies, etc. The IASB's staff confirmed an outstanding decision, and indicated that at a group level there was little doubt that the rules should be under the scope of IAS 12. However, they noted that there might be some doubts at a sub-group or subsidiary level that cannot be clarified at this stage, as it would depend, among other things, on how countries adopt these rules.
 - (c) A few FR TEG members shared their concern on the IASB requiring entities to disclose the name of the country where the effective tax rates are below 15%. They saw it as a way of including country by country disclosures in the financial statements through the back door. One member questioned whether it was necessary to require any disclosures as IAS 1 already requires entities to disclose information about new significant transactions and IAS 8 - to disclose information when a new accounting amendment is adopted. Another member expressed the view that these disclosures should be included in the management commentary rather than in the financial statements.
 - (d) A few FR TEG members noted that it would be important to be know what the FASB intends to do on this matter. It would not be understandable for stakeholders that the IASB and the FASB follow a very different approach.
 - (e) A FR TEG member asked whether the IASB had considered whether this exception affects the relevance of financial statements. The IASB staff noted that entities need more time to work through the rules and that the mandatory exception intends to avoid that entities recognise deferred taxes in different ways giving rise to divergence.

Questions for EFRAG FRB members

- 14 Do EFRAG FRB members have any general questions on the expected amendments?
- 15 Do EFRAG FRB members consider this project being significant. Do EFRAG FRB members want to discuss the topic in their meetings?

Intended approval process

- 16 The IASB intends to publish the ED in January 2023 with a comment period of 60 days.
- 17 EFRAG FR TEG will discuss the key messages for the DCL or the DCL itself as early as in the meeting on 18 January 2023. EFRAG should allow its constituents a comment period on the DCL of 28 days. Therefore, EFRAG Secretariat proposes to schedule additional meetings with EFRAG FR TEG (and EFRAG FR Board – if the project is classified as significant) to ensure a fast-track approval process for the DCL and the FCL. Such meetings will be scheduled as soon as the publication date of the ED is known.
- 18 To support a fast endorsement process, the EFRAG Secretariat proposes to publish a pre-consultation document for the DEA together with the publication of the FCL. That would allow to publish a DEA with a comment period of only one week shortly after the issuance of the Amendment to IAS 12. EFRAG Secretariat proposes to schedule additional meetings with EFRAG FR TEG (and EFRAG FR Board – if the project is classified as significant) to ensure a fast-track approval process of the DEA and FEA. Such meetings will be scheduled as soon as the publication date of the Amendments are known.

Questions for EFRAG FRB members

- 19 Do EFRAG FRB members agree to follow a fast-track approval process?
- 20 In case the project is being classified significant do EFRAG FRB members want to discuss the DCL and DEA in physical meetings as well or only the FCL and the FEA?
- 21 Do FRB members agree to issue a pre-consultation document for the draft endorsement advice?

Agenda Papers

- 22 In addition to this cover note, a presentation prepared by the IASB is attached:
 - (a) Agenda paper 11-02 – IASB Presentation