AASB 22-23 October 2014
Agenda paper 7.3 (M141)

AASB Exposure Draft

ED 253
August 2014

Recognition of Deferred Tax Assets for Unrealised Losses

(Proposed amendments to AASB 112)

Comments to the AASB by 20 November 2014

Australian Government

Australian Accounting Standards Board

Commenting on this AASB Exposure Draft

Constituents are strongly encouraged to respond to the AASB and the IASB. The AASB is seeking comment by 20 November 2014. This will enable the AASB to consider Australian constituents' comments in the process of formulating its own comments to the IASB, which are due by 18 December 2014. Comments should be addressed to:

The Chairman
Australian Accounting Standards Board
PO Box 204
Collins Street West Victoria 8007
AUSTRALIA
E-mail: standard@aasb.gov.au

Respondents to the IASB are asked to send their comments electronically to the IFRS Foundation website (www.ifrs.org), using the 'Comment on a proposal' page.

All submissions on possible, proposed or existing financial reporting requirements, or on the standard-setting process, will be placed on the public record unless the Chairman of the AASB agrees to submissions being treated as confidential. The latter will occur only if the public interest warrants such treatment.

Obtaining a Copy of this AASB Exposure Draft

This AASB Exposure Draft is available on the AASB website: www.aasb.gov.au. Alternatively, printed copies of this AASB Exposure Draft are available by contacting:

The Customer Service Officer
Australian Accounting Standards Board
Level 7
600 Bourke Street
Melbourne Victoria
AUSTRALIA

Phone: (03) 9617 7637
Fax: (03) 9617 7608
E-mail: publications@aasb.gov.au
Postal address:
PO Box 204
Collins Street West Victoria 8007

Other Enquiries

Phone: (03) 9617 7600
Fax: (03) 9617 7608
E-mail: standard@aasb.gov.au

ISSN 1030-5882

AASB REQUEST FOR COMMENTS

The proposed amendments to IAS 12 (incorporated into AASB 112 *Income Taxes*) seek to clarify the accounting, where the entity reports tax losses, for deferred tax assets related to debt instruments measured at fair value, by clarifying the application of some of the principles in IAS 12. The proposed amendments to IAS 12 clarify:

(a) that decreases in the carrying amount of a fixed-rate debt instrument for which the principal is paid on maturity give rise to a deductible temporary difference if the debt instrument is measured at fair value and if its tax base remains at cost, irrespective of whether the debt instrument's holder expects to recover the carrying amount of the asset by holding it to maturity, or whether it is probable that the issuer will pay all the contractual cash flows;

(b) the extent to which an entity's estimate of future taxable profit includes amounts from recovering assets for more than their carrying amounts;

(c) that an entity's estimates of future taxable profits excludes tax deductions resulting from the reversal of deductible temporary differences; and

(d) that an entity assesses whether to recognise the tax effect of a deductible tax difference as a deferred tax asset in combination with other deferred tax assets. If tax law restricts the utilisation of tax losses so that an entity can only deduct tax losses against income of a specified type or specified types, the entity must still assess a deferred tax asset in combination with other deferred tax assets, but only with deferred tax assets of the appropriate type.

In light of the Australian Accounting Standards Board's (AASB's) policy of incorporating International Financial Reporting Standards (IFRSs) into Australian Accounting Standards, the AASB is inviting comments on:

(a) any of the proposals in the attached International Accounting Standards Board (IASB) Exposure Draft, including the specific questions on the proposals as listed in the Invitation to Comment section of the attached IASB Exposure Draft; and

(b) the 'AASB Specific Matters for Comment' listed below.

Submissions play an important role in the decisions that the AASB will make in regard to a Standard. The AASB would prefer that respondents supplement their opinions with detailed comments, whether supportive or critical, on the major issues. The AASB regards both critical and supportive comments as essential to a balanced review and will consider all submissions, whether they address all specific matters, additional issues or only one issue.

Due Date for Comments to the AASB

Comments should be submitted to the AASB by 20 November 2014. This will enable the AASB to consider those comments in the process of formulating its own comments to the IASB. Constituents are also strongly encouraged to send their response to the IASB.

Reduced Disclosure Requirements

AASB 1053 *Application of Tiers of Australian Accounting Standards* establishes a differential reporting framework consisting of two tiers of reporting requirements for preparing general purpose financial statements:

(a) Tier 1: Australian Accounting Standards; and

(b) Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements.

Tier 2 comprises the recognition and measurement requirements of Tier 1 and substantially reduced disclosures corresponding to those requirements.

The proposals in this Exposure Draft do not make amendments to any disclosure requirements. Accordingly, this Exposure Draft does not give rise to any particular implications for Tier 2 disclosures.

AASB Specific Matters for Comment

The AASB would particularly value comments on the following:

1. whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:

    (a) not-for-profit entities; and

    (b) public sector entities, including GAAP/GFS implications;

2. whether, overall, the proposals would result in financial statements that would be useful to users;

3. whether the proposals are in the best interests of the Australian economy; and

4. unless already provided in response to specific matters for comment 1 – 3 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative.

August 2014

Exposure Draft ED/2014/3

Recognition of Deferred Tax Assets for Unrealised Losses

Proposed amendments to IAS 12

Comments to be received by 18 December 2014

IASB®

IFRS®

Recognition of Deferred Tax Assets for Unrealised Losses

(Proposed amendments to IAS 12)

Comments to be received by 18 December 2014

Exposure Draft ED/2014/3 *Recognition of Deferred Tax Assets for Unrealised Losses* (Proposed amendments to IAS 12) is published by the International Accounting Standards Board (IASB) for comment only. The proposals may be modified in the light of the comments received. Comments need to be received by **18 December 2014** and should be submitted in writing to the address below or electronically using our 'Comment on a proposal' page.

All comments will be on the public record and posted on our website unless the respondent requests confidentiality. Such requests will not normally be granted unless supported by good reason, for example, commercial confidence. Please see our website for details on this and how we use your personal data.

ISBN: 978-1-909704-55-8

IFRS Foundation Publications Department
30 Cannon Street, London EC4M 6XH, United Kingdom
Tel: +44 (0)20 7332 2730 Fax: +44 (0)20 7332 2749
Email: publications@ifrs.org Web: www.ifrs.org

IFRS®

CONTENTS

Introduction

This Exposure Draft, published by the International Accounting Standards Board (IASB), contains proposed amendments to IAS 12 *Income Taxes*.

The proposed amendments to IAS 12 are in response to a request to the IFRS Interpretations Committee (the 'Interpretations Committee') to clarify the recognition of a deferred tax asset that is related to a debt instrument measured at fair value in circumstances in which:

(a) changes in the market interest rate decrease the fair value of the debt instrument below cost.

(b) it is probable that the debt instrument's holder will receive all the contractual cash flows if it holds the debt instrument until maturity.

(c) the debt instrument's holder has the ability and intention to hold the debt instrument until the decrease in its fair value reverses (which may be at its maturity).

(d) the tax base of the debt instrument remains at cost until the debt instrument is sold or until maturity. The tax base of the debt instrument is not reduced by an impairment loss, because the criteria for recognising an impairment loss for tax purposes are not met.

(e) the probable future taxable profits of the debt instrument's holder are insufficient for the utilisation of all of its deductible temporary differences.

The issue arises, for example, when an entity that reports tax losses acquires a 5-year fixed rate bond that is issued at the prevailing market interest rate, and subsequently the market rate of interest increases. In this circumstance the fair value of the debt instrument may fall in response to the increase in the market interest rate even if there is no deterioration in the credit quality of the bond.

The Interpretations Committee reported to the IASB that there is diversity in practice because of divergent views on the following issues that IAS 12 does not address directly:

(a) Do decreases in the carrying amount of a fixed-rate debt instrument for which the principal is paid on maturity always give rise to a deductible temporary difference if this debt instrument is measured at fair value and if its tax base remains at cost? In particular, do they give rise to a deductible temporary difference if the debt instrument's holder expects to recover the carrying amount of the asset by use, ie holding it to maturity, and if it is probable that the issuer will pay all the contractual cash flows?

(b) Does an entity assume that it will recover an asset for more than its carrying amount when estimating probable future taxable profit against which deductible temporary differences are assessed for utilisation if such recovery is probable? This question is relevant when taxable profit from other sources is insufficient for the utilisation of the deductible temporary differences related to debt instruments measured at fair value. In this case, an entity might only be able to recognise deferred tax assets for its deductible temporary differences if it is probable that it will collect the entire cash flows from the debt instrument and therefore recover it for more than its carrying amount.

(c) When an entity assesses whether it can utilise a deductible temporary difference against probable future taxable profit, does that probable future taxable profit include the effects of reversing deductible temporary differences?

(d) Does an entity assess whether a deferred tax asset is recognised for each deductible temporary difference separately, or in combination with other deductible temporary differences? This question is relevant, for example, when tax law distinguishes capital gains and losses from other taxable gains and losses and capital losses can only be offset against capital gains.

The IASB observed that the main reason for the diversity in practice is uncertainty about the application of some of the principles in IAS 12.

The IASB concluded that the best way to address this diversity in practice is to clarify issues (a)–(d) in the mandatory guidance of IAS 12 and to add an illustrative example that would illustrate the application of the principle in IAS 12 in accounting for deferred tax assets for changes in the carrying amount of debt instruments measured at fair value through other comprehensive income.

To avoid undue cost and effort the IASB proposes that retrospective application of the proposed amendments to IAS 12 is limited. As proposed, restatements of the opening retained earnings or other components of equity of the earliest comparative period presented should be allowed but not be required.

Full retrospective application would be required for first-time adopters of IFRS. Many first-time adopters of IFRS have to determine the cumulative amounts of deferred tax that would have been recognised in profit or loss, other comprehensive income or directly in equity up to the date of transition to IFRSs. IFRS 1 *First-time Adoption of International Financial Reporting Standards* does not include an exception to, or exemption from, the retrospective application of this general requirement. Consequently, the IASB is not proposing an amendment to IFRS 1.

Next step

The IASB will consider the comments that it receives on the proposals and will decide whether it will proceed with the proposed amendments to IAS 12.

Invitation to comment

The IASB invites comments on the proposals in this Exposure Draft, particularly on the questions set out below. Comments are most helpful if they:

(a) comment on the questions as stated;

(b) indicate the specific paragraph(s) to which they relate;

(c) contain a clear rationale; and

(d) describe any alternative that the IASB should consider, if applicable.

The IASB is not requesting comments on matters that are not addressed in this Exposure Draft.

Comments should be submitted in writing so as to be received no later than **18 December 2014**.

Questions for respondents

Question 1—Existence of a deductible temporary difference
The IASB proposes to confirm that decreases in the carrying amount of a fixed-rate debt instrument for which the principal is paid on maturity give rise to a deductible temporary difference if this debt instrument is measured at fair value and if its tax base remains at cost. This applies irrespective of whether the debt instrument's holder expects to recover the carrying amount of the debt instrument by sale or by use, ie by holding it to maturity, or whether it is probable that the issuer will pay all the contractual cash flows. Do you agree with the proposed amendment? Why or why not? If not, what alternative do you propose?

Question 2—Recovering an asset for more than its carrying amount
The IASB proposes to clarify the extent to which an entity's estimate of future taxable profit (paragraph 29) includes amounts from recovering assets for more than their carrying amounts. Do you agree with the proposed amendment? Why or why not? If not, what alternative do you propose?

Question 3—Probable future taxable profit against which deductible temporary differences are assessed for utilisation
The IASB proposes to clarify that an entity's estimate of future taxable profit (paragraph 29) excludes tax deductions resulting from the reversal of deductible temporary differences. Do you agree with the proposed amendment? Why or why not? If not, what alternative do you propose?

Question 4—Combined versus separate assessment
The IASB proposes to clarify that an entity assesses whether to recognise the tax effect of a deductible temporary difference as a deferred tax asset in combination with other deferred tax assets. If tax law restricts the utilisation of tax losses so that an entity can only deduct tax losses against income of a specified type or specified types (eg if it can deduct capital losses only against capital gains), the entity must still assess a deferred tax asset in combination with other deferred tax assets, but only with deferred tax assets of the appropriate type. Do you agree with the proposed amendment? Why or why not? If not, what alternative do you propose?

Question 5—Transition
The IASB proposes to require limited retrospective application of the proposed amendments for entities already applying IFRS. This is so that restatements of the opening retained earnings or other components of equity of the earliest comparative period presented should be allowed but not be required. Full retrospective application would be required for first-time adopters of IFRS. Do you agree with the proposed amendment? Why or why not? If not, what alternative do you propose?

How to comment

Comments should be submitted using one of the following methods.

Electronically (our preferred method)	Visit the 'Comment on a proposal page', which can be found at: go.ifrs.org/comment
Email	Email comments can be sent to: commentletters@ifrs.org
Postal	IFRS Foundation 30 Cannon Street London EC4M 6XH United Kingdom

All comments will be on the public record and posted on our website unless confidentiality is requested. Such requests will not normally be granted unless supported by good reason, for example, commercial confidence. Please see our website for details on this and how we use your personal data.

[Draft] Amendments to IAS 12 *Income Taxes*

Paragraph 29 is amended and paragraphs 27A, 29A and 98G and the example following paragraph 26 are added. New text is underlined. Paragraphs 24, 26(d), 27 and 28 have not been amended but are included for ease of reference.

Deductible temporary differences

24 **A deferred tax asset shall be recognised for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilised, unless the deferred tax asset arises from the initial recognition of an asset or liability in a transaction that:**

(a) is not a business combination; and

(b) at the time of the transaction, affects neither accounting profit nor taxable profit (tax loss).

However, for deductible temporary differences associated with investments in subsidiaries, branches and associates, and interests in joint arrangements, a deferred tax asset shall be recognised in accordance with paragraph 44.

...

26 The following are examples of deductible temporary differences that result in deferred tax assets:

(a) ...

(d) certain assets may be carried at fair value, or may be revalued, without an equivalent adjustment being made for tax purposes (see paragraph 20). A deductible temporary difference arises if the tax base of the asset exceeds its carrying amount.

Example illustrating paragraph 26(d)

Identification of deductible temporary difference at the end of Year 2:

Entity A invests CU1,000 at the beginning of Year 1 in a debt instrument with a nominal value of CU1,000 payable on maturity in 5 years.

Interest is paid at the end of each year at a rate of 2 per cent, taxable when received. The contractual interest rate of 2 per cent equals the market interest rate at the beginning and the end of Year 1. The market interest rate increases at the end of Year 2 to 5 per cent, which results in a decline in the fair value of the debt instrument at the end of Year 2 to CU918. This decline is solely due to the difference between the market interest rate and the nominal interest rate of the debt instrument. It is probable that Entity A will receive all the contractual cash flows if it holds the debt instrument until maturity.

The tax base of the debt instrument is its original cost.

Tax law determines that taxable profit (tax loss) upon which income taxes are payable (recoverable) is increased (reduced) by gains arising on the sale of the debt instrument and reduced (increased) by losses arising on such transactions.

These gains and losses are calculated for tax purposes as the difference between the proceeds received and the tax base of the debt instruments.

Tax law also determines that taxable profit (tax loss) upon which income taxes are payable (recoverable) is reduced (increased) by losses that arise if the issuer of the debt instrument fails to pay the principal in full on maturity. Such losses are calculated for tax purposes as the difference between the amount that the issuer pays as principal and the tax base.

Furthermore, the tax base of the debt instrument is reduced by the deduction of impairment losses. However, the criteria for deducting impairment losses for tax purposes are not met in the case of this debt instrument.

Tax law does not explicitly specify any tax consequences resulting from the payment of the entire principal of CU1,000.

The difference between the carrying amount of the debt instrument in Entity A's statement of financial position of CU918 and its tax base of CU1,000 gives rise to a deductible temporary difference of CU82 at the end of Year 2 (see paragraphs 20 and 26(d)). This is because deductible temporary differences are temporary differences between the carrying amount of an asset or a liability in the statement of financial position and its tax base that will result in amounts that are deductible in determining taxable profit (tax loss) of future periods, when the carrying amount of the asset is recovered or the liability is settled (see paragraph 5).

continued...

...continued

Example illustrating paragraph 26(d)
This difference gives rise to a deductible temporary difference irrespective of whether Entity A expects to recover the carrying amount of the debt instrument by sale or by use, ie by holding it until maturity and collecting contractual cash flows, or a combination of both. In all of these scenarios, Entity A deducts the tax base of the asset of CU1,000 in determining taxable profit (tax loss):   *(a) If Entity A sells the debt instrument, it will deduct the tax base of CU1,000 in determining taxable profit of the period in which the debt instrument is sold.*   *(b) If Entity A holds the debt instrument until maturity at the end of Year 5, it will deduct the tax base of the debt instrument in determining taxable profit of the period that includes the end of Year 5, ie maturity (irrespective of whether the issuer actually pays full principal of CU1,000 or not).*   *It is irrelevant that tax law does not explicitly specify any tax consequences resulting from the payment of the entire principal of CU1,000. Tax law is based on the principle that gains and losses arising on the sale or on maturity of the debt instruments are determined as the difference between the inflow of economic benefits and the tax base. As a result, taxable profit (tax loss) upon which income taxes are payable (recoverable) includes the inflow of economic benefits from the payment of the principal of CU1,000 and the deduction of the tax base of the debt instrument, which also equals CU1,000.*

27 The reversal of deductible temporary differences results in deductions in determining taxable profits of future periods. However, economic benefits in the form of reductions in tax payments will flow to the entity only if it earns sufficient taxable profits against which the deductions can be offset. Therefore, an entity recognises deferred tax assets only when it is probable that taxable profits will be available against which the deductible temporary differences can be utilised.

27A When an entity assesses whether taxable profits will be available against which it can utilise a deductible temporary difference, the entity considers whether tax law restricts the sources of taxable profits against which the entity may make deductions on the reversal of that deductible temporary difference. If tax law imposes no such restrictions, an entity assesses a deductible temporary difference in combination with all its other deductible temporary differences. However, if tax law restricts the utilisation of losses to deduction against income of a specific type, a deductible temporary difference is assessed in combination only with other deductible temporary differences of the appropriate type.

28 It is probable that taxable profit will be available against which a deductible temporary difference can be utilised when there are sufficient taxable temporary differences relating to the same taxation authority and the same taxable entity which are expected to reverse:

(a) in the same period as the expected reversal of the deductible temporary difference; or

(b) in periods into which a tax loss arising from the deferred tax asset can be carried back or forward.

In such circumstances the deferred tax asset is recognised in the period in which the deductible temporary differences arise.

29 When there are insufficient taxable temporary differences relating to the same taxation authority and the same taxable entity, the deferred tax is recognised to the extent that:

(a) it is probable that the entity will have sufficient taxable profit relating to the same taxation authority and the same taxable entity in the same period as the reversal of the deductible temporary difference (or in the periods into which a tax loss arising from the deferred tax asset can be carried back or forward). In evaluating whether it will have sufficient taxable profit in future periods, an entity:

(i) compares the deductible temporary differences with future taxable profit that excludes tax deductions resulting from the reversal of those deductible temporary differences. This comparison shows the extent to which the future taxable profit is sufficient for the entity to deduct the amounts resulting from the reversal of those deductible temporary differences; and

(ii) ignores taxable amounts arising from deductible temporary differences that are expected to originate in future periods, because the deferred tax asset arising from these deductible temporary differences will itself require future taxable profit in order to be utilised; or

(b) tax planning opportunities are available to the entity that will create taxable profit in appropriate periods.

29A Estimating taxable profit in future periods (see paragraph 29(a)) requires assessing whether and to what extent it is probable that the assets of the entity will be recovered for more than their carrying amount. An entity considers all relevant facts and circumstances when making this assessment. Recovery of an asset for more than its carrying amount is unlikely to be probable if, for example, it was recently impaired. Conversely, recovery of an asset for more than its carrying amount is likely to be probable, if, for example, it is measured at cost and used in a profitable operation.

...

Effective date

...

98G [Draft] *Recognition of Deferred Tax Assets for Unrealised Losses* (Amendments to IAS 12), issued in [date], amended paragraph 29 and added paragraphs 27A, 29A and the example following paragraph 26. An entity shall apply those amendments for annual periods beginning on or after [date]. Earlier application is permitted. If an entity applies those amendments for an earlier period, it shall disclose that fact. An entity shall apply those amendments retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. However, an entity is not required to restate the opening retained earnings or other components of equity of the earliest comparative period presented. If an entity does not make such restatements, it shall disclose that fact.

Approval by the Board of *Recognition of Deferred Tax Assets for Unrealised Losses* (Proposed amendments to IAS 12) published in August 2014

The Exposure Draft *Recognition of Deferred Tax Assets for Unrealised Losses* was approved for publication by the fourteen members of the International Accounting Standards Board.

Hans Hoogervorst	Chairman
Ian Mackintosh	Vice-Chairman
Stephen Cooper	
Philippe Danjou	
Martin Edelmann	
Patrick Finnegan	
Amaro Luiz de Oliveira Gomes	
Gary Kabureck	
Suzanne Lloyd	
Takatsugu Ochi	
Darrel Scott	
Chungwoo Suh	
Mary Tokar	
Wei-Guo Zhang	

Basis for Conclusions on the Exposure Draft *Recognition of Deferred Tax Assets for Unrealised Losses* (Proposed amendments to IAS 12)

This Basis for Conclusions accompanies, but is not part of, the proposed amendments.

Recognition of deferred tax assets for unrealised losses

BC1 The IFRS Interpretations Committee (the 'Interpretations Committee') was asked to provide guidance on how an entity determines, in accordance with IAS 12 *Income Taxes*, whether to recognise a deferred tax asset when:

(a) the entity has a debt instrument that is classified as an available-for-sale financial asset in accordance with IAS 39 *Financial Instruments: Recognition and Measurement* (AFS debt instrument) with a fair value below its cost (ie it has an 'unrealised loss'). An AFS debt instrument is measured at fair value after recognition, with gains and losses recognised in other comprehensive income (OCI), except for interest recognised in applying the effective interest method, impairment losses and foreign exchange gains and losses, which are recognised in profit or loss in accordance with IAS 39, until the debt instrument is derecognised.

(b) it is probable that the issuer of the debt instrument will make all the contractual payments.

(c) the tax base of the AFS debt instrument is cost.

(d) tax law does not allow a loss to be deducted on a debt instrument until it is realised for tax purposes.

(e) the entity has the ability and intention to hold the AFS debt instrument until the unrealised loss reverses (which may be at its maturity).

(f) tax law distinguishes between capital gains and losses and ordinary income and losses. While capital losses can only be offset against capital gains, ordinary losses can be offset against both capital gains and ordinary income.

(g) the entity has insufficient taxable temporary differences and no other probable taxable profits against which the entity can utilise deductible temporary differences.

BC2 The Interpretations Committee reported to the IASB that practice differed because of divergent views on the following questions:

(a) Do decreases in the carrying amount of a fixed-rate debt instrument for which the principal is paid on maturity always give rise to a deductible temporary difference if this debt instrument is measured at fair value and if its tax base remains at cost? In particular, do they give rise to a deductible temporary difference if the debt instrument's holder expects to recover the carrying amount of the asset by use, ie holding it to maturity, and if it is probable that the issuer will pay all the contractual cash flows (see paragraphs BC3–BC8)?

(b) Does an entity assume that it will recover an asset for more than its carrying amount when estimating probable future taxable profit against which deductible temporary differences are assessed for utilisation if such recovery is probable? This question is relevant when taxable profit from other sources is insufficient for the utilisation of the deductible temporary differences related to debt instruments measured at fair value. In this case, an entity might only be able to recognise deferred tax assets for its deductible temporary differences if it is probable that it will collect the entire cash flows from the debt instrument and therefore recover it for more than its carrying amount (see paragraphs BC9–BC16).

(c) When an entity assesses whether it can utilise a deductible temporary difference against probable future taxable profit, does that probable future taxable profit include the effects of reversing deductible temporary differences (see paragraphs BC17–BC18)?

(d) Does an entity assess whether a deferred tax asset is recognised for each deductible temporary difference separately, or in combination with other deductible temporary differences? This question is relevant, for example, when tax law distinguishes capital gains and losses from other taxable gains and losses and capital losses can only be offset against capital gains (see paragraphs BC19–BC21).

Existence of a deductible temporary difference

BC3 In the case of many debt instruments, the payment of the principal on maturity does not increase or decrease taxable profit that is reported for tax purposes. This is the case, for example, in the example illustrating paragraph 26(d) of IAS 12. Interest is paid at the contractual rate each year, and on maturity of the debt instrument the issuer pays the principal of CU1,000. In this example, if the investor holds the debt instrument over the period to maturity, the investor only pays taxes on the interest income. The payment of the principal does not trigger any tax payments.

BC4 Because the payment of the principal does not increase or decrease the taxable profit that is reported for tax purposes, some believe that the payment of the principal is a non-taxable event. Sometimes, tax law does not explicitly address whether the payment of the principal has tax consequences. Consequently, proponents of this view think that a difference between the carrying amount of the debt instrument in the statement of financial position and its higher tax base does not give rise to a deductible temporary difference, if this difference results from a loss that they expect will not be realised for tax purposes.

BC5 Those who hold this view think that the loss will not be realised for tax purposes if the entity has the ability and intention to hold the debt instrument over the period until the loss reverses (which might be until maturity). In other words, it is probable that the entity will receive all the contractual cash flows. In this case, differences between the carrying amount of the debt instrument in the statement of financial position and its tax base reverse over the period to maturity, merely as a result of continuing to hold the debt instrument.

BC6 The IASB considered the guidance in IAS 12 on the identification of temporary differences and rejected the reasoning presented in paragraph BC4. The IASB concluded that decreases below cost in the carrying amount of a fixed-rate debt instrument for which principal is paid on maturity give rise to a deductible temporary difference if the debt instrument is measured at fair value and if its tax base remains at cost. This applies irrespective of whether the debt instrument's holder expects to recover the carrying amount of the debt instrument by sale or by use, ie holding it to maturity, or whether it is probable that the issuer will pay all the contractual cash flows. The payment of the entire principal does not increase or decrease taxable profit that is reported for tax purposes, because the tax base equals the inflow of taxable economic benefits when the principal is paid. Paragraphs 20 and 26(d) of IAS 12 specify that a difference between the carrying amount of an asset measured at fair value and its higher tax base gives rise to a deductible temporary difference. The tax base of the debt instrument is deducted either on sale or on maturity.

BC7 The economic benefit embodied in the related deferred tax asset results from the ability of the holder of the debt instrument to achieve future taxable gains in the amount of the deductible temporary difference without paying taxes on those gains. In contrast, an entity that acquires the debt instrument described in the example illustrating paragraph 26(d) of IAS 12 for its fair value (in the example, CU918) and holds it to maturity has to pay taxes on a gain of CU82, whereas the entity in that example will not pay any taxes on the payment of the CU1,000 of principal. The different tax consequences for these two holders of the same instrument should be reflected in the deferred tax accounting for the debt instrument.

BC8 The IASB proposes to add an example after paragraph 26 of IAS 12 to illustrate the identification of a deductible temporary difference in the case of a fixed-rate debt instrument measured at fair value for which the principal is paid on maturity.

Recovering an asset for more than its carrying amount

BC9 The IASB noted that paragraph 29 of IAS 12 identifies taxable profit in future periods as one source of taxable profits against which an entity can utilise deductible temporary differences. Future taxable profit has to be probable to justify the recognition of deferred tax assets. Consequently, only the conditions that will probably prevail when the deductible temporary differences are utilised determine the estimate of future taxable profit.

BC10 The guidance in paragraph 29 of IAS 12 does not refer to the carrying amount of assets within the context of estimating probable future taxable profit. Some think, however, that the carrying amount of an asset to which a temporary difference is related limits the estimate of future taxable profit. They argue that accounting for deferred taxes should be based on consistent assumptions, which implies that an entity cannot assume that, for one and the same asset:

(a) the entity will recover it for its carrying amount when determining deductible temporary differences and taxable temporary differences; as well as

(b) recovering it for more than its carrying amount when estimating probable future taxable profit against which deductible temporary differences are assessed for utilisation.

BC11 Consequently, proponents of this view think that an entity cannot assume that it will collect the entire principal of CU1,000 in the example illustrating paragraph 26(d) of IAS 12 when determining probable future taxable profit. Instead, they think an entity must assume that it will collect only the part of the principal that equals the carrying amount of the asset, ie fair value.

BC12 The IASB noted however that determining temporary differences and estimating probable future taxable profit against which deductible temporary differences are assessed for utilisation are two separate steps and the carrying amount of an asset is relevant only to determining temporary differences. The carrying amount of an asset does not limit the estimation of probable future taxable profit. In its estimate of probable future taxable profit, an entity includes the probable inflow of taxable economic benefits that results from recovering an asset. This probable inflow of taxable economic benefits may exceed the carrying amount of the asset.

BC13 Moreover, a limitation on the estimate of probable future taxable profits by the carrying amount of assets can lead to inappropriate results in scenarios like the following one that are prevalent in practice: a profitable manufacturing entity applies IAS 12 in accounting for its deferred tax assets and deferred tax liabilities. A significant part of the assets of the manufacturing entity is property, plant and equipment and inventories. Property, plant and equipment is measured using the cost model (paragraph 30 of IAS 16 *Property, Plant and Equipment*) and inventories are measured at the lower of cost and net realisable value (paragraph 9 of IAS 2 *Inventories*). Consequently, the assumption of recovering these assets for only their carrying amount leads to inappropriate results if it conflicts with an expectation that the entity will generate future taxable profits. This is because a significant part of the manufacturing entity's probable future taxable profits results from using those assets to generate taxable profits in excess of their carrying amount.

BC14 The conflict cannot be avoided by applying the limitation on the estimate of probable future taxable profits only to assets to which temporary differences are related. There is no basis for a different assessment depending on whether a deductible temporary difference is related to an asset or not. If such a limitation was made then, for the purposes of consistency, the entity would need to assume that it will not recover any of its assets for more than their carrying amounts.

BC15 However, the IASB also noted that there are cases in which it may not be probable that an asset will be recovered for more than its carrying amount, especially if the asset is measured on the basis of expected cash flows. Examples of this are many assets measured at fair value or assets that have been impaired recently.

BC16 The IASB proposes to add paragraph 29A to IAS 12 to clarify to what extent an entity's estimate of future taxable profit (paragraph 29) includes amounts from recovering assets for more than their carrying amounts.

Probable future taxable profit against which deductible temporary differences are assessed for utilisation

BC17 The Interpretations Committee observed that there is uncertainty about how to define probable future taxable profit against which deductible temporary differences are assessed for utilisation when this profit is to support the recognition of all deferred tax assets. The uncertainty related to the question of whether deductible temporary differences should be compared with probable future taxable profit, determined excluding tax deductions for which those deductible temporary differences exist, or including them.

BC18 The IASB noted that deductible temporary differences are utilised by deduction against the amount of taxable profit, excluding tax deductions for which those deductible temporary differences exist. If those deductions were not excluded, then they would be counted twice. The IASB proposes to amend paragraph 29(a) of IAS 12 to clarify this.

Combined versus separate assessment

BC19 The IASB considered the guidance in IAS 12 on the recognition of deferred tax assets. Paragraph 24 of IAS 12 requires that deferred tax assets are recognised only to the extent of probable future taxable profit against which the deductible temporary differences can be utilised. Paragraph 27 of IAS 12 explains that:

(a) the deductible temporary differences are utilised when their reversal results in deductions that are offset against taxable profits of future periods; and

(b) economic benefits in the form of reductions in tax payments will flow to the entity only if it earns sufficient taxable profits against which the deductions are offset.

BC20 The IASB noted that:

(a) Tax law determines which deductions are offset in determining taxable profits. The IASB also noted that paragraph 5 of IAS 12 defines taxable profit as the profit of a period, determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable.

(b) No deferred tax asset is recognised if the reversal of the deductible temporary difference will not lead to tax deductions.

BC21 Consequently, if tax law offsets a deduction against taxable income on an entity basis, without segregating deductions from different sources, an entity carries out a combined assessment of all its deductible temporary differences relating to the same taxation authority and the same taxable entity. However, if tax law offsets specific types of loss only against a particular type or particular types of income (for example, if it limits the offset of capital losses to capital gains), an entity assesses a deductible temporary difference in combination with other deductible temporary differences of that type(s), but separately from other deductible temporary differences. Only segregating deductible temporary differences in accordance with tax law and assessing them on such a combined basis determines whether taxable profits are sufficient to utilise deductible temporary differences. The IASB proposes to add paragraph 27A to IAS 12 to clarify this.

Structure of the amendments to IAS 12

BC22 The IASB observed that the main reason for diversity in practice in accounting for deferred tax assets for changes in the carrying amount of debt instruments measured at fair value is uncertainty about the application of some of the principles in IAS 12.

BC23 Consequently, the IASB decided to add an example in the illustrative computations and presentation section that would illustrate the application of the principles in IAS 12 in accounting for such deferred tax assets.

Transition

BC24 The IASB proposes a limited mandatory retrospective application for entities already applying IFRS. Restatements of the opening retained earnings or other components of equity of the earliest comparative period presented should be allowed but not be required. This is to avoid undue cost and effort.

BC25 The IASB noted that, with the exception of the amounts that would have to be restated within equity, the accounting required by these proposed amendments is on amounts and estimates at the end of the reporting periods. The changes to these amounts and estimates resulting from the proposed amendments are mechanical in nature.

BC26 The IASB proposes no transition relief for first-time adopters. This is consistent with the fact that IFRS 1 *First-time Adoption of International Financial Reporting Standards* does not include an exception to, or exemption from, the retrospective application of the requirements in IAS 12.

[Draft] Amendments to the illustrative computations and presentation on IAS 12 *Income Taxes*

Extracts from statements of financial position and statements of comprehensive income are provided to show the effects on these financial statements on the transactions described below. These extracts do not necessarily conform with all the disclosure and presentation requirements of other Standards.

All the examples below assume that the entities concerned have no transactions other than those described.

Note for respondents to the Exposure Draft:

The existing illustrative computations and presentation of IAS 12 do not include paragraph numbers and we do not intend to change their format.

However, for ease of reference by respondents, we have used paragraph numbers for draft Example 7—Debt instruments measured at fair value.

Example 7—Debt instruments measured at fair value is added. New text is underlined.

Example 7—Debt instruments measured at fair value

Debt instruments

IE1 At 31 December 20X1, Entity Z holds a portfolio of three debt instruments:

	31 December 20X1		
Debt instrument	**A**	**B**	**C**
Cost	2,000,000	750,000	2,000,000
Fair value on 31 December 20X1	1,942,857	778,571	1,961,905
Contractual interest rate in per cent	2.00	9.00	3.00

IE2 Entity Z acquired all the debt instruments on issuance for their nominal value. The terms of the debt instruments require the issuer to pay the nominal value of the debt instruments on their maturity on 31 December 20X2.

IE3 Interest is paid at the end of each year at the contractually fixed rate, which equalled the market interest rate when the debt instruments were issued. At the end of 20X1, the market interest rate is 5 per cent, which has caused the fair value of Debt instruments A and C to fall below their cost and the fair value of Debt instrument B to rise above cost.

IE4 The decreases in the fair values on the Debt instruments A and C are solely due to the difference between the contractual interest rate and the market interest rate on 31 December 20X1. It is probable that Entity A will receive all the contractual cash flow if it holds Debt instruments A and C to maturity.

IE5 At the end of 20X1, Entity Z expects that it will recover the carrying amounts of Debt instruments A and B through use, ie by holding them over the period to maturity and collecting contractual cash flows. In addition, it expects to recover the carrying amount of Debt instrument C by sale at the beginning of 20X2 for CU1,961,905, which is its fair value on 31 December 20X1.

IE6 The debt instruments are measured at fair value through other comprehensive income (FVOCI). Consequently, gains and losses are recognised in other comprehensive income, except for interest recognised in applying the effective interest method, impairment gains and losses and foreign exchange gains and losses, until the financial asset is derecognised or reclassified out of the FVOCI category.[1]

Tax law

IE7 The tax base of the debt instruments is cost, which tax law allows to be offset either on maturity when principal is paid or against the sale proceeds when the debt instruments are sold. Consequently, tax law does not allow Entity Z to deduct any losses on the debt instruments until they are realised for tax purposes, ie by selling the debt instruments or by failure of the issuer to pay the principal on maturity. Furthermore, the tax base of the debt instruments is reduced by the deduction of impairment losses if the conditions specified by tax law for deducting impairment losses are met. However, these conditions are not satisfied for Debt instruments A and C. Similarly, gains on the debt instruments are not taxable until realised.

IE8 Tax law distinguishes ordinary gains and losses from capital gains and losses. Ordinary losses can be offset against both ordinary gains and capital gains. Capital losses can only be offset against capital gains. Capital losses can be carried forward for 5 years and ordinary losses can be carried forward for 20 years.

IE9 Ordinary gains are taxed at 30 per cent and capital gains are taxed at 10 per cent.

IE10 Tax law classifies interest income from the debt instruments as 'ordinary' and gains and losses arising on the sale of the debt instruments as 'capital'. Losses that arise if the issuer of the debt instrument fails to pay the principal on maturity are classified as 'ordinary' by tax law.

1 For entities that have not yet applied IFRS 9 *Financial Instruments* (2014) and still apply IAS 39 *Financial Instruments: Recognition and Measurement* paragraph IE6 reads as follows: The debt instruments are classified as available-for-sale financial assets. Consequently, they are measured at fair value after initial recognition (see paragraph 46 of IAS 39) with gains and losses recognised in other comprehensive income, except for interest recognised in applying the effective interest method, impairment losses and foreign exchange gains and losses, until the financial assets are derecognised (see paragraph 55(b) of IAS 39).

General

IE11 On 31 December 20X1, Entity Z has from other sources:

(a) taxable temporary differences of CU50,000, for which the deferred tax liabilities are recognised with a corresponding expense in profit or loss; and

(b) deductible temporary differences of CU430,000, for which the deferred tax assets are recognised with a corresponding gain in profit or loss, if it is probable that they can be utilised.

IE12 The temporary differences from other sources will reverse in 20X2 and the tax consequences resulting from their reversal will be included in ordinary taxable profit (or ordinary tax loss) in 20X2.

IE13 At the end of 20X1, it is probable that Entity Z will report to the tax authorities an ordinary tax loss of CU200,000 for the year 20X2. This tax loss includes all the amounts that will be taxable or tax-deductible on the reversal of the temporary differences described in the previous paragraphs and that are classified as ordinary by tax law. These amounts contribute equally to the loss for the period according to tax law.

IE14 Entity Z has no capital gains against which it can utilise capital losses arising in the years 20X1–20X2.

IE15 Except for the information given in the previous paragraphs, there is no further information that is relevant to its accounting for deferred taxes in the periods 20X1–20X2.

Temporary differences

IE16 At the end of 20X1, Entity Z identifies the following temporary differences:

	31 December 20X1			
	Debt instruments			Other sources
	A	**B**	**C**	
Carrying amounts	1,942,857	778,571	1,961,905	Not specified
Tax bases	2,000,000	750,000	2,000,000	Not specified
Taxable temporary differences		28,571		50,000
Deductible temporary differences	57,143		38,095	430,000

Debt instrument A

IE17 The difference between the carrying amount of Debt instrument A in Entity Z's statement of financial position of CU1,942,857 and its tax base of CU2,000,000 gives rise to a deductible temporary difference of CU57,143 on 31 December 20X1 (see paragraphs 20 and 26(d) of IAS 12). This is because deductible temporary differences are temporary differences between the carrying amount of an asset or a liability in the statement of financial position and its tax base that will result in amounts that are deductible in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled (paragraph 5 of IAS 12).

IE18 At the end of 20X1, Entity Z expects to hold Debt instrument A to maturity and it is probable that Entity Z will collect all the contractual cash flows. Consequently, the difference between the carrying amount of Debt instrument A in Entity Z's statement of financial position of CU1,942,857 and its tax base of CU2,000,000 is expected to reverse over the period to maturity while Entity Z recovers the carrying amount of Debt instrument A by collecting the interest payment of CU40,000 for 20X2 and the payment of the principal of CU2,000,000 on maturity on 31 December 20X2.

IE19 Furthermore, the difference between the carrying amount of Debt instrument A in Entity Z's statement of financial position of CU1,942,857 and its tax base of CU2,000,000 is expected to result in an amount that will be deducted in determining taxable profit (tax loss) of 20X2.

Debt instrument B

IE20 The difference between the carrying amount of Debt instrument B in Entity Z's statement of financial position of CU778,571 and its tax base of CU750,000 gives rise to a taxable temporary difference of CU28,571 on 31 December 20X1 (see paragraph 20 of IAS 12). This is because taxable temporary differences are temporary differences between the carrying amount of an asset or a liability in the statement of financial position and its tax base, which will result in taxable amounts in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled (paragraph 5 of IAS 12).

IE21 Entity Z expects to hold Debt instrument B to maturity and it is probable that Entity Z will collect all the contractual cash flows. Consequently, the difference between the carrying amount of Debt instrument B in Entity Z's statement of financial position of CU778,571 and its tax base of CU750,000 is expected to reverse over the period to maturity, while Entity Z recovers the carrying amount of Debt instrument B by collecting the interest payment of CU67,500 for 20X2 and the payment of the principal of CU750,000 on maturity on 31 December 20X2.

IE22 Furthermore, the difference between the carrying amount of Debt instrument B in Entity Z's statement of financial position of CU778,571 and its tax base of CU750,000 is expected to result in an amount that is taxable in determining taxable profits (tax losses) of the year 20X2. This difference of CU28,571 reflects an interest payment that is above the market interest rate and that Entity Z will collect in the year 20X2.

Debt instrument C

IE23 The difference between the carrying amount of Debt instrument C in Entity Z's statement of financial position of CU1,961,905 and its tax base of CU2,000,000 gives rise to a deductible temporary difference of CU38,095 on 31 December 20X1 (see paragraphs 20 and 26(d) of IAS 12). This is because deductible temporary differences are temporary differences between the carrying amount of an asset or a liability in the statement of financial position and its tax base, which will result in amounts that are deductible in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled (paragraph 5 of IAS 12).

IE24 Entity Z expects to sell Debt instrument C at the beginning of year 20X2 for its fair value of CU1,961,905 on 31 December 20X1. Consequently, the difference between the carrying amount of Debt instrument C in Entity Z's statement of financial position of CU1,961,905 and its tax base of CU2,000,000 is expected to reverse on the sale of Debt instrument C at the beginning of the year 20X2 and is expected to result in an amount that is deducted in determining Entity Z's taxable profit (tax loss) for the year 20X2 when the entire tax base of Debt instrument C is deducted on its sale.

Utilisation of deductible temporary differences

IE25 With some exceptions, deferred tax assets arising from deductible temporary differences are recognised to the extent that sufficient future taxable profits will be available against which the deductible temporary differences are utilised (see paragraph 24 of IAS 12).

IE26 Paragraphs 28–29 of IAS 12 identify three sources of taxable profits against which an entity can utilise deductible temporary differences. They are:

(a) future reversal of existing taxable temporary differences;

(b) taxable profit in future periods; and

(c) tax planning opportunities.

IE27 Deferred tax assets arising from deductible temporary differences are recognised only to the extent that it is probable that at least one of these sources of taxable profits is available. Beyond this extent, no deferred tax asset is recognised.

IE28 Paragraphs 28–29 of IAS 12 require an assessment of the utilisation of deferred tax assets arising from deductible temporary differences in two successive steps:

(a) an entity assesses in a first step (Step 1) whether there are sufficient taxable temporary differences relating to the same taxation authority and the same taxable entity, which are expected to reverse:

  (i) in the same period as the expected reversal of the deductible temporary difference; or

  (ii) in periods into which a tax loss arising from the deferred tax asset can be carried back or forward; and

(b) if the assessment in Step 1 does not result in the recognition of all deferred tax assets arising from deductible temporary differences, the entity assesses in a second step (Step 2) whether:

(i) it is probable that the entity will have sufficient taxable profit relating to the same taxation authority, and the same taxable entity, in the same period as the reversal of the deductible temporary difference (or in the periods into which a tax loss arising from the deferred tax asset can be carried back or forward); or

(ii) tax planning opportunities are available to the entity that will create taxable profit in appropriate periods.

IE29 The deductible temporary difference of CU38,095 that arises from Debt instrument C is assessed separately for utilisation, whereas the other deductible temporary differences are assessed in combination with one another for utilisation. This is because tax law classifies the loss resulting from recovering the carrying amount of Debt instrument C by sale as 'capital' and allows capital losses to be offset only against capital gains. This is the only one of Entity Z's deductible temporary differences for which tax law classifies the related tax deductions as 'capital'.

IE30 The separate assessment results in not recognising a deferred tax asset for the deductible temporary difference that arises from Debt instrument C, because Entity Z has no source of taxable profit available that tax law classifies as 'capital'.

IE31 In contrast, the deductible temporary difference of CU57,143 that arises from Debt instrument A and the deductible temporary differences of CU430,000 arising from other sources are assessed for utilisation in combination with one another. This is because their related tax deductions are classified as 'ordinary' by tax law.

IE32 This classification as 'ordinary' of the tax deductions that are represented by the deductible temporary differences related to Debt instrument A follows from the fact that the tax law classifies the effect on taxable profit (tax loss) from deducting the tax base on maturity as 'ordinary'. For example, if the issuer fails to pay the principal on maturity, tax law classifies the loss as ordinary and allows it to be offset against ordinary gains and losses and capital gains and losses.

Step 1: Utilisation of deductible temporary differences for which tax law classifies the related tax deductions as ordinary because of the future reversal of existing taxable temporary differences

IE33 Entity Z first assesses the availability of taxable temporary differences relating to the same taxation authority that are expected to reverse in the same period, or in periods into which an ordinary tax loss arising from the deferred tax asset can be carried back or forward, on 31 December 20X1 as follows:

	Year 20X2
Expected reversal of deductible temporary difference related to Debt instrument A	57,143
Expected reversal of deductible temporary differences from other sources	430,000
Total reversal of deductible temporary differences	487,143
Expected reversal of taxable temporary difference related to Debt instrument B	(28,571)
Expected reversal of taxable temporary differences from other sources	(50,000)
Total reversal of taxable temporary differences	(78,571)
Utilisation in the period	78,571
Reversing deductible temporary differences requiring further assessment of utilisation	408,572

Step 2: Utilisation of deductible temporary differences for which tax law classifies the related tax deductions as ordinary because of future taxable profit

IE34 In this step, Entity Z assesses the availability of future taxable profit relating to the same taxation authority, and the same taxable entity, in the same period as the reversal of the deductible temporary difference, or in periods into which an ordinary tax loss arising from the deferred tax asset can be carried back or forward, as follows:

	Deductible temporary differences	Future taxable profit	Utilisation
Debt instrument A	57,143		
Deductible temporary differences from other sources	430,000		
Total deductible temporary differences	487,143		
Deductible temporary differences utilised because of reversal of existing taxable temporary differences (Step 1)	(78,571)		
Deductible temporary differences requiring further assessment of utilisation	408,572		
Probable future tax loss in 20X2		(200,000)	
Taxable profits already considered as part of Step 1		(78,571)	
Excluding tax deductions from deductible temporary differences		487,143	
Adjusted taxable profit (tax loss) for assessing utilisation of deductible temporary differences		208,572	
Total utilisation because of future taxable profit (Step 2)	408,572	208,572	208,572
Utilisation because of future reversal of existing taxable temporary differences (Step 1)			78,571
Total utilisation			**287,143**

IE35 Taxable profit (tax loss) is the profit (loss) for a period, determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable (recoverable) (see paragraph 5 of IAS 12).

IE36 Taxable profit (tax loss) upon which income taxes are payable (recoverable) includes all taxable economic benefits and tax deductions of a period. Consequently, the probable future ordinary tax loss of Entity Z in 20X2 includes the taxable economic benefit of CU2,000,000 from the payment of the principal of Debt instrument A and the equivalent tax deduction. It also includes the taxable amounts from recovering Debt instrument B and the taxable amounts and deductible amounts for which temporary differences from other sources exist on 31 December 20X1. In other words, with the exception of the tax deduction for which the deductible temporary difference related to Debt instrument C exists, it includes all amounts for which temporary differences exist on 31 December 20X1.

IE37 The probable future ordinary tax loss of Entity Z in 20X2 includes the taxable economic benefit of CU2,000,000 from the payment of the principal of Debt instrument A, because it is probable that Entity Z will receive CU2,000,000 on maturity of Debt instrument A as the payment of the principal and will therefore recover the debt instrument for more than its carrying amount of CU1,942,857.

IE38 The utilisation of deductible temporary differences is not, however, assessed against probable future taxable profit for a period upon which income taxes are payable (see paragraph 5 of IAS 12). The utilisation of deductible temporary differences is assessed against probable future taxable profit that excludes tax deductions resulting from the reversal of deductible temporary differences (see paragraph 29(a) of IAS 12).

Measurement of deferred tax assets and deferred tax liabilities

IE39 Entity Z presents the following deferred tax assets and deferred tax liabilities in its financial statements on 31 December 20X1:

	31 December 20X1				
	Taxable temporary differences	Deductible temporary differences	Tax rate	Deferred tax liabilities	Deferred tax assets
Total taxable temporary differences	78,571	–	30%	23,571	
Total utilisable deductible temporary differences	–	287,143	30%		86,143
Total				23,571	86,143

IE40 The deferred tax asset related to Debt instrument A and the deferred tax liability related to Debt instrument B are measured using the tax rate for ordinary gains of 30 per cent, because that is the tax rate that applies to gains and losses

resulting from recovering debt instruments by holding them to maturity and collecting contractual cash flows (paragraph 51A of IAS 12).

Allocation of changes in deferred tax assets between profit or loss and other comprehensive income

IE41 Changes in deferred tax that arise from items that are recognised in profit or loss are recognised in profit or loss (see paragraph 58 of IAS 12). Changes in deferred tax that arise from items that are recognised in other comprehensive income are recognised in other comprehensive income (see paragraph 61A of IAS 12).

IE42 Entity Z did not recognise deferred tax assets for all of its deductible temporary differences on 31 December 20X1, and according to tax law all the tax deductions represented by the deductible temporary differences contribute equally to the tax loss for the period. Consequently, the assessment of the utilisation of deductible temporary differences does not specify whether the taxable profits are utilised for deferred tax items that are recognised in profit or loss (ie the deductible temporary differences from other sources) or whether instead the taxable profits are utilised for deferred tax items that are recognised in Other Comprehensive income (ie the deductible temporary difference related to Debt instrument A).

IE43 For such situations, paragraph 63 of IAS 12 requires the changes in deferred taxes to be allocated to profit or loss and other comprehensive income on a reasonable pro rata basis.

