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Agenda paper A6 (M143)

Australian Government

Australian Accounting Standards Board

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Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Hans

AASB comments on IASB ED/2014/3
Recognition of Deferred Tax Assets for Unrealised Losses

The Australian Accounting Standards Board (AASB) welcomes the opportunity to provide comments on ED/2014/3 *Recognition of Deferred Tax Assets for Unrealised Losses*. In formulating its comments, the AASB sought and considered the views of Australian constituents through comment letters and other consultation. The comment letters received are published on the AASB's website.

The AASB agrees with the underlying basis for the proposed amendments to IAS 12 *Income Taxes*. However, the AASB considers that a number of aspects of IAS 12, including those relating to the recognition of deferred tax assets for unrealised losses, would benefit from a limited review of the Standard, focusing on clarifying and improving the principles underpinning IAS 12, rather than piecemeal amendments addressing specific practice issues. In addition, the AASB disagrees with the proposed transitional provisions which permit entities a choice as to whether to restate opening retained earnings of the earliest period presented.

The AASB's responses to the specific matters for comment in ED/2014/3 are included in the Appendix to this letter.

If you have queries regarding any matters in this submission, please contact Evelyn Ling (evelynl@aasb.gov.au).

Yours sincerely,

K. E. Peach

Kris Peach
Chair and CEO

APPENDIX

AASB comments on IASB ED/2014/3 *Recognition of Deferred Tax Assets for Unrealised Losses*

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?

The AASB agrees with the underlying basis for the proposed amendment, including the example illustrating paragraph 26(d) of IAS 12.

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?

The AASB agrees with the inclusion of a paragraph similar to paragraph 29A. However, the AASB thinks that paragraph 29A should also address the instrument that is the subject of these amendments. That is, paragraph 29A should include discussion of where recovery of an asset carried at fair value for more than its carrying amount is probable.

Further, the AASB thinks that it is not clear whether the intention of the words "for more than its carrying amount" is to capture a 'fair value' or a 'cash flow' notion. Accordingly, the AASB recommends that an additional sentence be inserted following the proposed first sentence of paragraph 29A, as follows:

> "In estimating future taxable profit, an entity considers all expected future cash flows associated with recovering the asset, including an asset to which a deductible temporary difference is related."

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?

The AASB agrees with the proposed amendments to paragraph 29, but thinks that the second sentence in proposed paragraph 29(a)(i) is unnecessary, given the stem of the paragraph, and could be deleted without any loss of meaning.

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?

The AASB agrees with the proposed amendment.

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?

The AASB disagrees with permitting, but not requiring, entities to restate the opening retained earnings (or other component of equity, as appropriate) of the earliest comparative period presented. The AASB thinks that the transitional provisions should require all entities already applying IFRSs to apply the amendments in the same manner, except where it is impractical for the entity to do so, as comparability between entities may otherwise be compromised. We also note that we do not agree that any changes would be mechanical in nature, as there will be elements of hindsight needed in assessing any recognition of a DTA.

Other comments

Example illustrating paragraph 26(d)

In respect of the Example illustrating paragraph 26(d), the AASB recommends that drafting amendments be made to:

(a) clarify that the debt instrument is measured at fair value in the entity's financial statements;

(b) clarify that the deduction of the tax base is to identify the amounts that are deductible in determining taxable profit, rather than the deduction of the tax base in determining taxable profit; and

(c) conform the language to that currently employed in IAS 12 – e.g. 'through use' and 'through sale' rather than 'by use' and 'by sale'. In addition, the language in the proposed Basis for Conclusions and Illustrative Example should similarly be conformed to that employed in IAS 12.

The AASB also recommends that consideration be given to whether the proposed Illustrative Example could be more succinctly articulated.

Other drafting comments

In addition, the AASB thinks that the drafting of:

(a) paragraphs IE5-IE6 could be improved to clarify that earlier versions of IFRS 9 would not permit such instruments to be measured at fair value through other comprehensive income;

(b) paragraph IE14 should clarify that Entity Z does not expect to make capital gains in the years 20X3-20X6. IE30 assumes that there will be no capital gains for the next 5 years such that it is appropriate that no deferred tax asset is recognised in relation to Debt instrument C; and

(c) Step 2 as illustrated in paragraph IE34 could be simplified by excluding the first 5 rows which largely repeat Step 1 and illustrating the application of paragraphs 28-29 of IAS 12 as an 'if not, then' approach rather than as a two-step approach. For example, IE34 could illustrate paragraph 29 in a manner similar to the below:

	CU
Probable future tax loss in 20X2	(200,000)
Excluding tax deductions from deductible temporary differences	487,143
Total future taxable profit available for utilisation	287,143
Utilisation of tax deductions from deductible temporary differences:	
Utilisation from future reversal of existing taxable temporary differences	78,571
Utilisation because of remaining available future taxable profit	208,572
Total utilisation of deductible temporary differences	287,143