Kris Peach
Chair
Australian Accounting Standards Board
PO Box 204
Collins Street West VIC 8007

via email: standard@aasb.gov.au

18 December 2014

Dear Kris

Re: Exposure draft 253 *Recognition of Deferred Tax Assets for Unrealised Losses*

I am enclosing a copy of PricewaterhouseCooopers' response to the International Accounting Standards Board's exposure draft ED/2014/3 *Recognition of Deferred Tax Assets for Unrealised Losses (Proposed amendments to IAS 12)*.

The letter reflects the views of the PricewaterhouseCoopers (PwC) network of firms and as such includes our own comments on the matters raised in the request for comment. PwC refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

AASB specific matters for comment

We are not aware of any regulatory or other issues that could affect the implementation of the proposals for not-for-profit and public sector entities.

Should the proposed amendments be approved by the IASB, we are not aware of anything that would indicate that the proposals are not in the best interests of the Australian economy.

I would welcome the opportunity to discuss our firm's views at your convenience. Please contact me on (03) 8603 5371 if you would like to discuss our comments further.

Yours sincerely,

Margot Le Bars
Partner, PricewaterhouseCoopers

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17 December 2014

Exposure Draft ED/2014/3 – Recognition of Deferred Tax Assets for Unrealised Losses

We are pleased to respond to the invitation by the IASB to comment on the Exposure Draft, 'Recognition of Deferred Tax Assets for Unrealised Losses' (the 'Exposure Draft'), on behalf of PricewaterhouseCoopers. Following consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of those member firms that commented on the Exposure Draft.

'PricewaterhouseCoopers' refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

We agree with the IASB's conclusions about the recognition of deferred tax assets for unrealised losses on investments in debt instruments, which are consistent with the existing principles in IAS 12. We are concerned however, that the proposed amendments are too detailed and introduce new complexity to a straightforward issue.

We suggest that the proposed amendments are simplified to focus on the questions originally raised to the Interpretations Committee:(1) whether a deductible temporary difference arises in connection with debt instruments measured at fair value; and (2) how future taxable profits are considered to assess whether the resulting deferred tax assets are recognised. The principles applied to address these questions should be explained briefly in the amendment to IAS 12 and supported by adding a simple illustrative example and illustrative computation. Any additional explanation the Board believes to be necessary could then be included in the basis for conclusions.

The proposed new illustrative computation, in particular, is complex and illustrates too many issues. We suggest that it is simplified to address only one instrument and one issue.

Our detailed suggestions, including answers to the specific questions in the Exposure Draft and some suggestions for simplifying the illustrative computation expand the views expressed above and are included in the appendices to this letter.

If you have any questions on this letter, please contact Paul Fitzsimon, PwC Global Chief Accountant (+1 416 869 2322) or Tony de Bell (+44 207 213 5336).

Yours faithfully

PricewaterhouseCoopers

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APPENDIX A

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, i.e. 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?

We agree with the principle confirmed by the proposed amendment that a deductible temporary difference arises when the tax base of an asset, including a debt instrument, exceeds its carrying amount, in particular where the carrying amount is measured at fair value. The basis for conclusions should confirm that the same principle is applied to all deductible and taxable temporary differences.

The illustration in paragraph 26(d) is unnecessary and duplicates much of the proposed illustrative computation in paragraphs IE16 to IE24. We suggest it is deleted in its entirety. The principle is clear from paragraph 26(d) and the application to debt instruments carried at fair value can be illustrated by adding another simple example of such an investment to the existing examples of temporary differences in IAS 12.

We also suggest that the basis for conclusions describing the proposed amendment is clarified. Paragraph BC6 explains why the difference between the carrying amount of an asset and the tax base gives rise to a deductible temporary difference. Paragraph BC7, however, creates complexity by describing how 'different tax consequences for these two holders of the same instrument should be reflected in the deferred tax accounting for the debt instrument'. This discussion is not necessary and we suggest it is deleted. If it is retained, it should be amended to state that the different tax consequences are a result of the two entities having different tax bases, which should be reflected in the deferred tax accounting.

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?

We agree with the principle that the assessment of future taxable profit includes amounts from recovering assets for more than their carrying amounts. We believe, however, that this principle is clearly articulated in IAS 12 and is well understood. Paragraph 29A therefore creates unnecessary complexity. We suggest that this paragraph is deleted and that the principle is confirmed by adding a sentence to the basis for conclusions.

We also suggest that the examples in the last sentence of paragraph BC15 are removed. The reference to 'fair value' is confusing in the context of the instruments addressed by the proposed amendment. It implies that future taxable income from available for sale instruments recorded at fair value should be excluded from an assessment of future taxable profit.

Question 3 – Probable future taxable profit against which deductible temporary differences are assessed for utilization

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?

We agree with the principle that the estimate of future taxable profit excludes tax deductions arising from the reversal of deductible temporary differences. The consequence of including tax deductions resulting from the reversal of deductible temporary differences is to 'double count' the deduction and inappropriately reduce the estimate of future taxable profit.

This is obvious from the existing guidance in IAS 12 and does not need to be stated specifically in a separate paragraph. This paragraph should be deleted and the principle confirmed in the proposed amendments to the basis for conclusions and in a simplified illustrative computation.

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 (e.g. if it can deduct tax 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?

We agree with the principle that deferred tax assets are assessed in combination with other deferred tax assets of an appropriate type. However, we suggest that the amendment might be simplified and that the detailed explanation in paragraph 27A is moved to the basis for conclusions.

We suggest that the following is added to paragraph 27: 'A deductible temporary difference is assessed in combination with all other deductible temporary differences unless tax law restricts the sources of income against which the deduction can be utilised.'

The basis for conclusions should also address the specific questions raised to the Interpretations Committee and should support the guidance in paragraph 27A by confirming that:

- The automatic reversal of a deductible temporary difference at maturity is not sufficient to support the recognition of a deferred tax asset.

- The recognition of deferred tax assets should not be considered in isolation, and therefore a deferred tax asset should be recognised only if there are probable future taxable profits.

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?

We support retrospective application. We do not believe, however, that the relief permitting no restatement of opening retained earnings and other components of equity is necessary. Management is required to perform a similar analysis when applying the backwards tracing model (for example, for a change in tax rate). IAS 8 provides guidance to evaluate if accounting for the change retrospectively is impracticable.

APPENDIX B

We suggest that the illustrative computation focuses on demonstrating how the principles of IAS 12 apply to the particular set of circumstances that were the subject of the original question to the Interpretations Committee. This could be accomplished by applying the principles to one fixed-rate debt instrument measured at fair value and a tax base that remains at cost.

We suggest the following amendments if the IASB decides to retain the illustrative computation in its current form:

- The proposed amendments to the illustrative computation (for example, paragraph IE13) use the term 'tax loss' to refer to the loss before the reversal of temporary differences. We suggest that this is clarified by replacing the term 'tax loss' with 'probable future tax profit (loss) excluding reversal of temporary differences'.
- Paragraphs IE17 to IE23 should be simplified. The description of how the temporary difference is identified and calculated for each instrument is repeated several times in the proposals.
- Paragraphs IE41 to IE43, which address the allocation of deferred taxes between profit or loss and OCI, should be removed. This is a separate issue that adds unnecessary complexity.