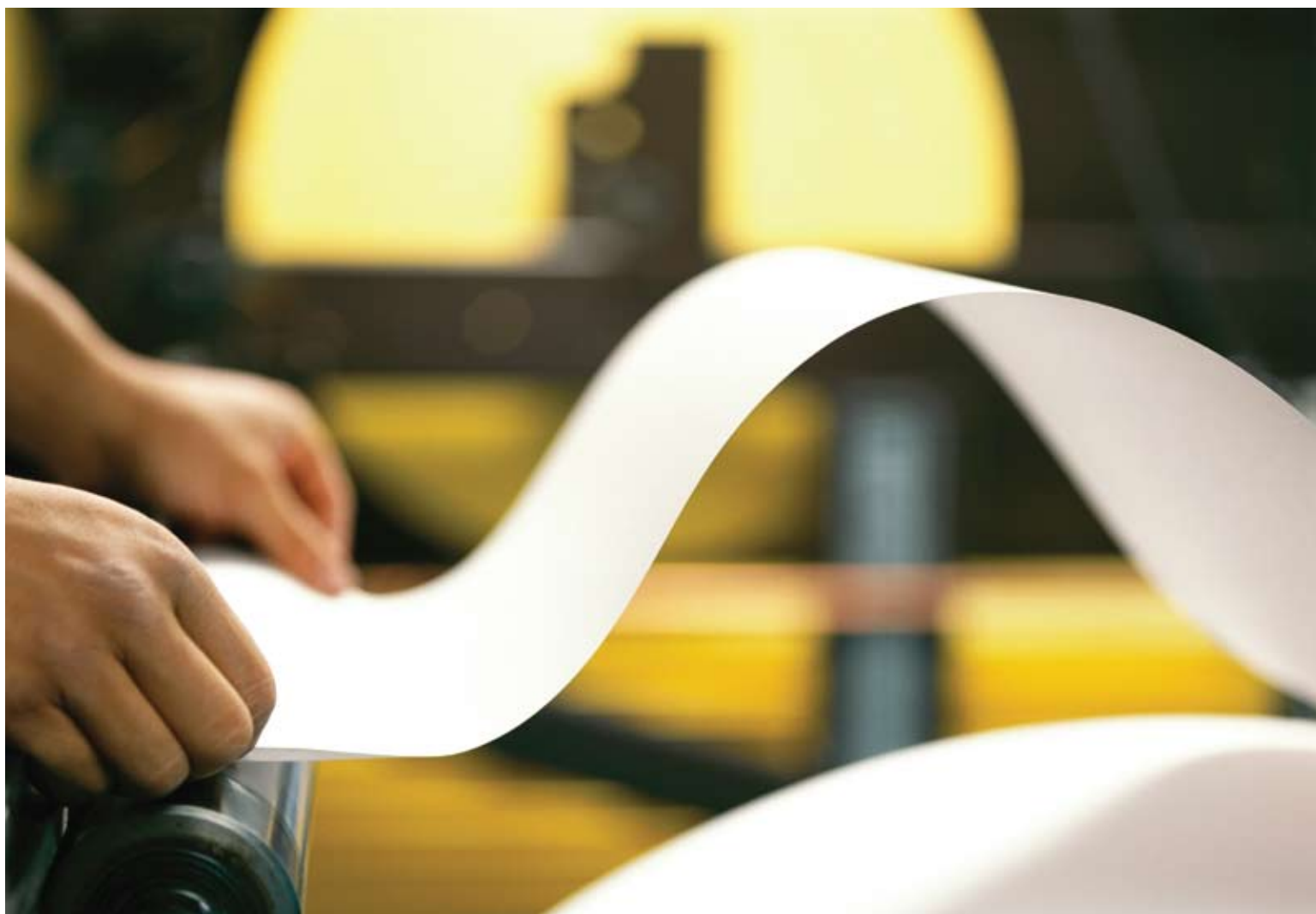


Income Tax Accounting under IFRS: A look ahead*

Financial statement disclosures



About this series

The IASB has proposed significantly changing the current IFRS standard on accounting for income tax. This is the eighth article in a series that explores how the proposed changes might impact companies. Each article focuses on a particular aspect of the IASB's proposal. The articles can be found at www.pwc.com/usifrs/tax.

Background

The IASB's proposal is another step toward providing comparable information to financial statement users. In the proposal, the IASB retains the majority of the disclosure requirements of IAS 12, *Income Taxes*, and incorporates certain disclosure requirements from FAS 109, *Accounting for Income Taxes*. The proposal also requires some entirely new disclosures.

This article highlights some of the proposal's more significant disclosure requirements.

Guidance in the IASB's proposal

Income statement disclosures

The IASB's proposal requires companies to disclose significant components of tax expense. Those components may include current and deferred tax expense, as well as amounts related to changes in (1) tax rates, (2) tax status, and (3) valuation allowance. Disclosure is also required of any adjustments arising from possible outcomes of a review by taxing authorities (i.e., uncertain tax positions). Companies must also reconcile a period's tax expense with tax expense that was based on the parent company's domestic statutory tax rate.

By proposing that the requirement to reconcile the effective tax rate be amended, the IASB is trying to make IAS 12 more consistent with FAS 109. Under IAS 12, companies have the option of aggregating separate reconciliations by using the domestic rate in each jurisdiction. Under the IASB's proposal, the reconciliation must use the domestic rate in the parent company's jurisdiction. Here the proposal is inconsistent with FAS 109, because the proposal has its own definition of "domestic rate." In the proposal, the domestic rate is an aggregate of the national tax rate and any local tax rates if the local taxes are computed on a substantially similar level of taxable profit.

Balance sheet disclosures

The IASB's proposal also requires companies to provide a numerical analysis of the change in deferred tax assets (DTAs) and deferred tax liabilities (DTLs) *for each type of temporary difference*. A company's analysis would include items such as:

- Origination and reversal of the temporary difference
- A change in tax rates, imposition of new taxes, or change in tax status
- A change in measurement of any uncertainty in the tax position
- Amounts recognized in other comprehensive income or directly in equity

The IASB's proposal represents a significant increase in the disclosures required by either IFRS or US GAAP related to DTAs and DTLs. Companies should consider the incremental effort that may be needed to make the proposed disclosures. Companies that operate in multiple jurisdictions will need to have sufficient processes in place to obtain the necessary information at the appropriate level of detail.

Other disclosures

The IASB's proposal also requires disclosure of the following:

- Tax expense related to (1) the gain or loss upon the sale of a discontinued operation and (2) the period's profit or loss related to the discontinued operation
- Aggregate amount of temporary differences related to investments in subsidiaries and joint ventures for which DTLs have not been recognized¹

The IASB decided against requiring additional disclosures related to these unrecorded DTLs. The IASB has asked for suggestions about disclosures that might provide meaningful information to financial statement users.

- Any DTAs and DTLs resulting from transfers of assets and liabilities that (1) are within a consolidated group and (2) are being transferred between taxing jurisdictions that have different tax rates. Companies must also disclose the net tax expense for all such transfers or for those transfers that are not considered customary for the group²

Acknowledging that some financial statement users may have concerns about possible earnings management resulting from the proposed income tax accounting for intercompany transactions, the IASB included new disclosure requirements in the proposal to address those concerns. Companies will need to have sufficient processes in place to obtain the necessary information at the appropriate level of detail.

- Methodology used to record income taxes in the separate financial statements of an entity that is a member of a group filing a consolidated return

How the proposed disclosures compare to existing IFRS and US GAAP

The more notable incremental disclosures from both an IFRS and US GAAP perspective are included in the description above. There are, however, disclosure requirements in IAS 12 and FAS 109 that are not carried over in the IASB's proposal. For example, IAS 12 requires companies to disclose the nature of the evidence supporting a DTA's recognition if (1) realization of the DTA depends on future taxable income and (2) the company had a loss in the current or preceding year. The IASB did not retain this disclosure in the proposal. However, the IASB proposed to require disclosure of the amount of any valuation allowance, any changes in that amount, and the reasons for such a change.

Uncertain tax positions

The IASB's proposal also excludes several US GAAP disclosures related to uncertain tax positions, such as the following:

- Rollforward of unrecognized tax benefits from the beginning to the end of the period

Although the IASB's proposal does not include a tabular reconciliation of unrecognized tax benefits, it requires disclosure of the major sources of estimation uncertainty including (1) a description of the uncertainty, (2) an indication of its possible impact on the financial statements and (3) the timing of such impact.

- Amount of unrecognized tax benefits that may affect the effective tax rate
- Tax years that are open to assessment by the tax authority in a major tax jurisdiction

¹Our seventh article in this series discusses the IASB's proposed accounting for investments in subsidiaries and joint ventures.

²Our fourth article in this series discusses the IASB's proposed accounting for intercompany transactions.

- Significant increases or decreases within the next 12 months that are reasonably possible, including the nature of the uncertainty, the event that would cause the change, and an estimate of the change

The IASB's proposal to disclose major sources of estimation uncertainty partially addresses this disclosure. In addition, IAS 1, *Presentation of Financial Statements*, requires a company to separately disclose those sources of estimation uncertainty that have a significant risk of material adjustment within the next financial year. When viewed together, the IFRS requirement would be similar to the existing US GAAP disclosure for material uncertainties.

- Total amount of interest and penalties expensed in the income statement and accrued in the balance sheet

The IASB's proposal requires disclosure of the company's policy on classification of interest and penalties. However, it does not require disclosure of the amounts of interest and penalties. If material, disclosure may be required under IAS 1.

Next steps

The IASB's proposal was released on March 31, 2009. The comment period ends on July 31, 2009. We encourage companies to consider the impact of the proposed accounting and to provide the IASB with comments.

The FASB plans to issue an Invitation to Comment on the IASB's proposal to solicit input from US constituents as it considers its own convergence efforts. Upon completing its review, the FASB will decide whether and how to proceed with eliminating remaining differences between FAS 109 and IAS 12. We encourage companies to consider the questions that the FASB will pose in its Invitation to Comment and to provide comments to the FASB.

Contacts

Clients of PricewaterhouseCoopers are encouraged to open a dialogue about the IASB's proposal and other IFRS matters with their PwC engagement partner or with the authors of and contributors to this series.

This series of articles was authored by the following individuals:

Tami Van Tassell

Phone: +1 973 236 5049

Email: tami.van.tassell@us.pwc.com

David Beaver

Phone: +1 973 236 4350

Email: david.a.beaver@us.pwc.com

Bill Maloney

Phone: +44 20 7804 9491

Email: william.d.maloney@us.pwc.com

Other contributors to the series include the following individuals:

Jennifer Spang

Phone: +1 973 236 4757

Email: jennifer.a.spang@us.pwc.com

Brett Cohen

Phone: +1 973 236 7201

Email: brett.cohen@us.pwc.com

Tony de Bell

Phone: +44 20 7213 5336

Email: tony.m.debell@uk.pwc.com

PricewaterhouseCoopers is committed to helping companies navigate the conversion from US GAAP to IFRS. With that in mind, please visit www.pwc.com/usifrs/tax or pwc.com/usifrs to view our comprehensive library of our IFRS thought leadership, webcasts and tools addressing the business and technical issues that companies should be considering in anticipation of the move from US GAAP to IFRS.

This document is provided by PricewaterhouseCoopers LLP for general guidance only, and does not constitute the provision of legal advice, accounting services, investment advice, written tax advice under Circular 230 or professional advice of any kind. The information provided herein should not be used as a substitute for consultation with professional tax, accounting, legal, or other competent advisers. Before making any decision or taking any action, you should consult with a professional adviser who has been provided with all pertinent facts relevant to your particular situation. The information is provided 'as is' with no assurance or guarantee of completeness, accuracy, or timeliness of the information, and without warranty of any kind, express or implied, including but not limited to warranties or performance, merchantability, and fitness for a particular purpose.