

Recognition of Deferred Tax Assets for Unrealised losses (Amendments to NZ IAS 12)

This Standard was issued on 31 March 2016 by the New Zealand Accounting Standards Board of the External Reporting Board pursuant to section 12(a) of the Financial Reporting Act 2013.

This Standard is a disallowable instrument for the purposes of the Legislation Act 2012, and pursuant to section 27(1) of the Financial Reporting Act 2013 takes effect on 28 April 2016.

Reporting entities that are subject to this Standard are required to apply the Standard in accordance with the effective date set out in Part C.

In finalising this Standard, the New Zealand Accounting Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This Standard has been issued to amend NZ IAS 12 *Income Taxes* for Tier 1 and Tier 2 for-profit entities as a result of changes to IAS 12 *Income Taxes*.

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The following is available in New Zealand on the XRB website as additional material

Approval by the IASB of *Recognition of Deferred Tax Assets for Unrealised Losses* (Amendments to IAS 12) issued in January 2016

Amendments to the Basis for Conclusions on IAS 12 *Income Taxes*

Amendments to The Illustrative Examples on IAS 12 *Income Taxes*

Part A

Introduction

This Standard sets out amendments to NZ IAS 12 *Income Taxes*.

These amendments update and finalise proposals in IASB Exposure Draft ED/2014/3 *Recognition of Deferred Tax Assets for Unrealised Losses* (Proposed Amendments to IAS 12) that was issued in August 2014.

The amendments clarify how to account for deferred tax assets related to debt instruments measured at fair value with effect from annual reporting periods on or after 1 January 2017.

Part B

Scope

This Standard applies to Tier 1 and Tier 2 for-profit entities.

Amendments to New Zealand Equivalent to International Accounting Standard 12 *Income Taxes*

Paragraph 29 is amended and paragraphs 27A, 29A and 98G are added. An example following paragraph 26 is also 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 a deductible temporary difference at the end of Year 2:

Entity A purchases for CU1,000, at the beginning of Year 1, a debt instrument with a nominal value of CU1,000 payable on maturity in 5 years with an interest rate of 2% payable at the end of each year. The effective interest rate is 2%. The debt instrument is measured at fair value.

At the end of Year 2, the fair value of the debt instrument has decreased to CU918 as a result of an increase in market interest rates to 5%. It is probable that Entity A will collect all the contractual cash flows if it continues to hold the debt instrument.

Any gains (losses) on the debt instrument are taxable (deductible) only when realised. The gains (losses) arising on the sale or maturity of the debt instrument are calculated for tax purposes as the difference between the amount collected and the original cost of the debt instrument.

Example illustrating paragraph 26(d)

Accordingly, the tax base of the debt instrument is its original cost.

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)), irrespective of whether Entity A expects to recover the carrying amount of the debt instrument by sale or by use, ie by holding it and collecting contractual cash flows, or a combination of both.

This is because deductible temporary differences are differences between the carrying amount of an asset or 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 (see paragraph 5). Entity A obtains a deduction equivalent to the tax base of the asset of CU1,000 in determining taxable profit (tax loss) either on sale or on maturity.

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, it considers whether tax law restricts the sources of taxable profits against which it 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 of 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 asset 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.
 - (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.
- (b) tax planning opportunities are available to the entity that will create taxable profit in appropriate periods.

29A The estimate of probable future taxable profit may include the recovery of some of an entity's assets for more than their carrying amount if there is sufficient evidence that it is probable that the entity will achieve this. For example, when an asset is measured at fair value, the entity shall consider whether there is

sufficient evidence to conclude that it is probable that the entity will recover the asset for more than its carrying amount. This may be the case, for example, when an entity expects to hold a fixed-rate debt instrument and collect the contractual cash flows.

...

Effective date

...

98G *Recognition of Deferred Tax Assets for Unrealised Losses* (Amendments to NZ IAS 12), issued in March 2016, 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 1 January 2017. 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 NZ IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. However, on initial application of the amendment, the change in the opening equity of the earliest comparative period may be recognised in opening retained earnings (or in another component of equity, as appropriate), without allocating the change between opening retained earnings and other components of equity. If an entity applies this relief, it shall disclose that fact.

Part C

Effective Date

This Standard is effective for annual reporting periods beginning on or after 1 January 2017. Earlier application is permitted.