Basis for Conclusions on AASB 2023-4

This Basis for Conclusions accompanies, but is not part of, AASB 1060. The Basis for Conclusions was originally published with AASB 2023-4 Amendments to Australian Accounting Standards – International Tax Reform – Pillar Two Model Rules: Tier 2 Disclosures.

Introduction

BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board's considerations in reaching the conclusions in this Standard. It sets out the reasons why the Board developed the Standard, the approach taken to developing the Standard and the bases for the key decisions made. In making decisions, individual Board members gave greater weight to some factors than to others.

Background

Pillar Two model rules

BC2 In October 2021 more than 135 jurisdictions agreed to the Organisation for Economic Co-operation and Development (OECD)/G20 Inclusive Framework on Base Erosion and Profit Shifting's *Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy*. Since then, the OECD has published model rules and other documents related to the second pillar of this solution (the Pillar Two model rules). The Pillar Two model rules provide a template that jurisdictions can translate into domestic tax law and implement as part of an agreed common approach.

BC3 The model rules:

(a) aim to ensure that large multinational groups pay a minimum amount of tax on income arising in each jurisdiction in which they operate;

(b) would achieve that aim by applying a system of top-up taxes that results in the total amount of taxes payable on "excess profit" in each jurisdiction representing at least the minimum rate of 15%; and

(c) typically require the ultimate parent entity of a group to pay top-up tax – in the jurisdiction in which it is domiciled – on profits of its subsidiaries that are taxed below 15%.

BC4 The rules are aimed at multinational groups with revenue in their consolidated financial statements exceeding €750 million in at least two of the four preceding fiscal years. The rules specify inclusion thresholds for some jurisdictions and exclude some types of entities from their scope.

Potential implications for income tax accounting

BC5 In response to stakeholder concerns about the implications for income tax accounting, in June 2023 the Board issued AASB 2023-2 *Amendments to Australian Accounting Standards – International Tax Reform – Pillar Two Model Rules*, which amended AASB 112 *Income Taxes* to introduce:

(a) a mandatory temporary exception to accounting for deferred taxes arising from the implementation of the Pillar Two model rules published by the OECD; and

(b) targeted disclosure requirements to help financial statement users better understand an entity's exposure to income taxes arising from the reform, particularly in periods before legislation implementing the rules is in effect.

BC6 The mandatory temporary exception and related disclosures noted in paragraph BC5 apply to both Tier 1 and Tier 2 entities.[1]

BC7 However, to ensure Tier 2 entities are required to comply with disclosure requirements set out in AASB 1060 rather than the new requirements in AASB 112, the Board proposed to amend Appendix A of AASB 112 to

1 AASB 1053 *Application of Tiers of Australian Accounting Standards* outlines that Australian Accounting Standards consist 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 – Simplified Disclosures.

extend the exemption from compliance with the disclosure requirements of AASB 112 for entities applying AASB 1060 to include the disclosure requirements added to AASB 112 by AASB 2023-2.

BC8 In considering whether to propose amendments to AASB 1060 to require targeted disclosures by Tier 2 entities, the Board considered that the Pillar Two model rules could have a material effect on the financial statements of Tier 2 entities. For example, some subsidiaries of large multinational groups may be affected by Pillar Two legislation.[2]

Issue of Exposure Draft ED 325

BC9 The Board's proposals with respect to the amendments finalised in this Standard were exposed for public comment in July 2023 through Exposure Draft ED 325 *International Tax Reform – Pillar Two Model Rules: Tier 2 Disclosures*.

BC10 The significant issues considered by the Board in developing ED 325 are addressed in the following section.

Relevance of the amendments to AASB 1060

BC11 The *AASB For-Profit Entity Standard-Setting Framework* and the *AASB Not-For-Profit Entity Standard-Setting Framework* outline the approach adopted by the Board for considering whether to add to or amend disclosure requirements in AASB 1060 when the IASB makes amendments to full IFRS Standards.

BC12 The standard-setting frameworks first consider whether the amendments introduce a significant recognition and measurement difference between full IFRS Standards and the *IFRS for SMEs* Standard. If they don't, the standard-setting frameworks state that no further action is required unless:

(a) the disclosures address a matter of public policy;

(b) the disclosures are of particular relevance in the Australian environment; or

(c) the amendments clarify or reduce existing disclosure requirements in full IFRS Standards.

BC13 In addition to the principles in the standard-setting frameworks, the Board acknowledged when finalising AASB 1060 that a review of the disclosures in AASB 1060 would need to take place any time the *IFRS for SMEs* Standard is updated (paragraph BC96).

BC14 Although there will be no recognition and measurement differences between full IFRS Standards and the *IFRS for SMEs* Accounting Standard or between Tier 1 and Tier 2 entities in Australia in respect of Pillar Two income taxes, the Board considers that Tier 2 entities applying the mandatory temporary exception should be required to include some disclosures in their financial statements to help users understand the effect of Pillar Two legislation on the financial statements.

BC15 In addition, the Board noted that the IASB proposed amendments to the *IFRS for SMEs* Standard, issuing Exposure Draft IASB/ED/2023/3 *International Tax Reform – Pillar Two Model Rules – Proposed amendments to the* IFRS for SMEs *Standard* in June 2023. IASB/ED/2023/3 proposes amendments to the *IFRS for SMEs* Standard that would:

(a) introduce a temporary exception to accounting for deferred taxes arising from the implementation of the Pillar Two model rules;

(b) introduce targeted disclosure requirements in periods when Pillar Two legislation is in effect; and

(c) clarify that 'other events' in the disclosure objective for income tax include enacted or substantively enacted Pillar Two legislation.

BC16 Therefore, the Board decided to propose amendments to AASB 1060 to require Tier 2 entities applying the temporary exception to include targeted disclosures in their financial statements.

Disclosures

BC17 As noted in paragraph BC6, a Tier 2 entity is required to apply the mandatory temporary exception to accounting for deferred taxes arising from the implementation of the Pillar Two model rules in AASB 112. To make the application of the exception transparent, the Board proposed requiring Tier 2 entities applying the temporary exception to disclose that fact.

2 'Pillar Two legislation' refers to tax law enacted or substantively enacted to implement the Pillar Two model rules published by the Organisation for Economic Co-operation and Development (OECD), including tax law that implements qualified domestic minimum top-up taxes described in those rules. Income taxes arising from Pillar Two legislation are hereafter referred to as 'Pillar Two income taxes'.

BC18 In addition, consistent with the IASB's proposed approach to amending the *IFRS for SMEs* Standard, the Board decided:

(a) in relation to periods before relevant Pillar Two legislation is in effect, not to propose specific disclosure requirements; and

(b) in relation to periods when relevant legislation is in effect, to propose requiring an entity to disclose its current tax expense (income) related to Pillar Two income taxes.

BC19 In making these decisions, the Board considered that:

(a) it was not necessary to add a new disclosure requirement for periods before relevant Pillar Two legislation is in effect because the existing disclosure requirement in paragraph 176 would be expected to result in Tier 2 entities affected by Pillar Two legislation providing some information about the nature and financial effect of enacted or substantively enacted Pillar Two legislation before it applies. However, the Board decided to propose clarifying that the reference in paragraph 176 to 'other events' includes enacted or substantively enacted Pillar Two legislation; and

(b) requiring a Tier 2 entity to disclose its current tax expense (income) related to Pillar Two income taxes when relevant legislation is in effect would help users of the financial statements understand the magnitude of Pillar Two income taxes relative to the entity's overall tax expense (income). The Board considered this disclosure would not be costly to prepare because a Tier 2 entity would already be required in these circumstances to recognise current tax related to Pillar Two income taxes.

Finalisation of ED 325 proposals

BC20 Following the consultation period, and after considering the comments received, the Board decided to proceed with issuing this Standard, with minimal changes from the proposals in ED 325.

Feedback from respondents on ED 325

BC21 The Board received two formal comment letters on ED 325. The feedback received indicated that, in general, both stakeholders were supportive of the proposals. However, one stakeholder provided additional feedback.

BC22 The stakeholder suggested that the proposed clarification to paragraph 176 was not necessary because it is already understood that the "transactions and other events" referred to in paragraph 176 include the enactment or substantive enactment of tax rates and laws. They also suggested that if the Board is concerned that this may not be the case, the clarification should be worded more broadly than specifically referring to Pillar Two legislation, or else the Board could consider clarifying this in the Basis for Conclusions.

BC23 The Board considered this feedback, along with feedback received by the IASB on IASB/ED/2023/3 and decided to generalise the wording of the clarification to paragraph 176 and refer to the Pillar Two legislation as an example.

Effective date

BC24 The Board decided that the amendments should be made effective for annual periods beginning on or after 1 January 2023 that end on or after 30 September 2023, with earlier application permitted, as proposed in ED 325. This is consistent with the effective date of AASB 2023-2 for most entities.

BC25 The Board noted the comment from one of the respondents to ED 325 that the proposed effective date could make Tier 2 entities unsure about the application of the amendments to certain periods, such as the 2022/23 financial year. The Board confirmed the proposed two-pronged effective date, which is required in this case to avoid any mandatory retrospective application to reporting periods that have ended prior to the Board making the Standard. The Board noted that an entity could elect to apply the amendments before their mandatory application date, for example to the 2022/23 financial year or any period ending before 30 September 2023.