ACTIVE STANDARD

INTERNATIONAL FINANCIAL REPORTING STANDARDS

IAS 12

Income Taxes

Current and deferred tax accounting — updated for Pillar Two and IFRS 18

BD

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ROADMAP

What We Will Cover

Foundations & Key Definitions

Accounting profit, taxable profit, tax base, and the concept of temporary differences

Recognition & Measurement

Current tax, deferred tax, the initial recognition exemption, and the decision framework

Worked Illustrations

Three practical scenarios covering taxable and deductible temporary differences

Pillar Two & the Single-Transaction Amendment

The two most consequential recent changes to IAS 12

Impact of IFRS 18

How the new income taxes category reshapes presentation from 2027

PART I — FOUNDATIONS

Key Definitions & the Tax Base

IAS 12 accounts for the current and future tax consequences of transactions and events already recognized in the financial statements.

FOUNDATIONS

Definitions — Profit & Tax Expense

Accounting Profit

Profit or loss for a period before deducting tax expense.

Taxable Profit (Tax Loss)

Profit or loss for a period, determined per tax authority rules, upon which income taxes are payable (recoverable).

Tax Expense (Tax Income)

The aggregate amount included in determining profit or loss for the period in respect of current tax and deferred tax.

Current Tax

The amount of income taxes payable (recoverable) in respect of the taxable profit (tax loss) for a period.

FOUNDATIONS

Definitions — Deferred Tax

Deferred Tax Liabilities

The amounts of income taxes payable in future periods in respect of taxable temporary differences.

IAS 12 mandates recognition of a deferred tax liability in full, subject to specific exceptions covered later in this deck.

Deferred Tax Assets

Amounts of income taxes recoverable in future periods in respect of:

- a Deductible temporary differences
- b The carry-forward of unused tax losses
- c The carry-forward of unused tax credits

A deferred tax asset or liability arises whenever recovery or settlement of an asset or liability affects the amount of future tax payments.

FOUNDATIONS

Temporary Differences

Temporary differences are differences between the carrying amount of an asset or liability in the statement of financial position and its tax base.

Taxable Temporary Differences

Temporary differences that will result in taxable amounts in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled.

→ Gives rise to a deferred tax liability

Deductible Temporary Differences

Temporary differences 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.

→ Gives rise to a deferred tax asset

FOUNDATIONS

What is the Tax Base?

The tax base of an asset or liability is the amount attributed to that asset or liability for tax purposes.

Tax Base of an Asset

The amount that will be deductible for tax purposes against any taxable economic benefits that will flow to the entity when it recovers the carrying amount of the asset.

If those economic benefits will not be taxable, the tax base equals the carrying amount.

Tax Base of a Liability

Its carrying amount, less any amount that will be deductible for tax purposes in respect of that liability in future periods.

For revenue received in advance, the tax base of the resulting liability is its carrying amount, less revenue that will not be taxable in future periods.

FOUNDATIONS

Tax Base of an Asset — Examples

Machine (cost $100)

$30 tax depreciation already deducted; remaining cost deductible later. Tax base = $70.

Interest receivable ($100)

Interest taxed on a cash basis when received. Tax base = nil.

Trade receivables ($100)

Related revenue already included in taxable profit. Tax base = $100.

Dividends receivable ($100)

Dividends not taxable — entire carrying amount is effectively deductible. Tax base = $100.

Loan receivable ($100)

Repayment has no tax consequences. Tax base = $100.

FOUNDATIONS

Tax Base of a Liability — Examples

Accrued expenses ($100)

Deducted for tax on a cash basis when paid. Tax base = nil.

Interest received in advance ($100)

Interest revenue taxed on a cash basis. Tax base = nil.

Accrued expenses, already deducted ($100)

Expense already deducted for tax. Tax base = $100.

Fines & penalties ($100)

Not deductible for tax purposes at all. Tax base = $100.

Loan payable ($100)

Repayment has no tax consequences. Tax base = $100.

PART II — RECOGNITION & MEASUREMENT

From Tax Base to Deferred Tax

How current and deferred tax move from definition to a recognized asset or liability on the balance sheet.

Current Tax Liabilities & Assets

Current tax for current and prior periods shall, to the extent unpaid, be recognised as a liability. If the amount already paid in respect of current and prior periods exceeds the amount due for those periods, the excess shall be recognised as an asset.

The benefit relating to a tax loss that can be carried back to recover current tax of a previous period shall be recognised as an asset — since it is virtually certain the benefit will be realized through a refund of tax already paid.

RECOGNITION & MEASUREMENT

Deferred Tax — Recognition & Measurement Principles

Probability test

Deferred tax on unused tax losses and unused tax credits is recognized only to the extent it is probable that future taxable profit will be available to utilize them.

Rates & discounting

Measured at the tax rates expected to apply when the asset is realized or the liability settled, based on rates (or laws) enacted or substantively enacted by the reporting date. Deferred tax balances are never discounted.

Where it is recognized

The tax consequence of a transaction or event is recognized in the same statement as the transaction itself — profit or loss, other comprehensive income, or directly in equity.

Business combinations

Deferred tax arising as part of a business combination is recognized as an identifiable asset or liability at the acquisition date under IFRS 3.

Taxable Temporary Differences

A deferred tax liability shall be recognised for all taxable temporary differences, except to the extent that the deferred tax liability arises from:

(a) Initial recognition of goodwill

(b) Initial recognition of an asset or liability in a transaction that (i) is not a business combination, and (ii) at the time of the transaction affects neither accounting profit nor taxable profit

Exception to the exception: for taxable temporary differences associated with investments in subsidiaries, branches, associates, and interests in joint ventures, a deferred tax liability IS recognised (subject to specific conditions in the standard).

RECOGNITION & MEASUREMENT

Deductible Temporary Differences

A deferred tax asset shall be recognised for all deductible temporary differences to the extent it is probable that taxable profit will be available against which the difference can be utilised, unless the asset arises from:

(a) Initial recognition of an asset or liability in a transaction that is not a business combination

(b) A transaction that, at the time it occurs, affects neither accounting profit nor taxable profit (tax loss)

As with taxable temporary differences, a deferred tax asset IS recognised for deductible temporary differences associated with investments in subsidiaries, branches, associates, and joint ventures, subject to specific conditions.

Decision Framework

Carrying amount of asset/liability differs from its tax base

Does recovery/settlement increase future tax (taxable) or decrease it (deductible)?

TAXABLE

Deferred Tax Liability

Unless it arises from goodwill, or an excluded single-transaction initial recognition

Since 2023: the initial-recognition exemption no longer applies to transactions (like leases and decommissioning) that create equal and offsetting taxable and deductible differences at inception — both sides must now be recognized.

DEDUCTIBLE

Deferred Tax Asset

Only to the extent future taxable profit is probable to be available

Separately: Pillar Two top-up taxes are outside this framework — entities apply a mandatory exception and do not recognize or disclose related deferred tax.

PART III — APPLICATION

Worked Illustrations

Three practical scenarios covering taxable temporary differences, the initial recognition exemption, and deductible temporary differences.

Illustration I — Taxable Temporary Difference

Fact pattern

An asset which cost $150 has a carrying amount of $100. Cumulative depreciation for tax purposes is $90, and the tax rate is 25%.

Solution

Tax base = $150 cost − $90 cumulative tax depreciation = $60.

To recover the carrying amount of $100, the entity must earn taxable income of $100 but can only deduct tax depreciation of $60 — so it will pay income tax of $10 ($40 at 25%) when it recovers the asset.

The difference between the carrying amount ($100) and the tax base ($60) is a taxable temporary difference of $40. The entity therefore recognises a deferred tax liability of $10 ($40 × 25%).

Illustration II — Initial Recognition Exemption

Fact pattern

An entity uses an asset costing $1,000 throughout its five-year useful life, then disposes of it for nil residual value. The tax rate is 40%. Depreciation is not deductible for tax purposes, and any capital gain or loss on disposal is neither taxable nor deductible.

Solution

As it recovers the carrying amount, the entity will earn taxable income of $1,000 and pay tax of $400 — but it does NOT recognise the resulting deferred tax liability, because it results from the initial recognition of the asset.

In the following year, the carrying amount is $800. In earning that taxable income the entity will pay tax of $320 — again, no deferred tax liability of $320 is recognised, for the same reason.

Illustration III — Deductible Temporary Difference

Fact pattern

An entity recognises a liability of $100 for gratuity and leave encashment expenses. For tax purposes, this amount is not deductible until it is actually paid. The tax rate is 25%.

Solution

Tax base of the liability = $100 carrying amount − $100 future tax deduction = nil.

In settling the liability, the entity will reduce future taxable profit by $100, reducing future tax payments by $25 ($100 × 25%). The difference between the carrying amount ($100) and the tax base (nil) is a deductible temporary difference of $100.

The entity recognises a deferred tax asset of $25, provided it is probable that sufficient taxable profit will be available in future periods to benefit from the reduction in tax payments.

PART IV — RECENT DEVELOPMENTS

Amendments & IFRS 18 Impact

The two most consequential recent changes to IAS 12, plus how IFRS 18 reshapes income tax presentation from 2027.

Deferred Tax on a Single Transaction

Deferred Tax related to Assets and Liabilities arising from a Single Transaction (Amendments to IAS 12) — issued May 2021, effective for annual periods beginning on or after 1 January 2023.

1

The problem

The initial recognition exemption left it unclear whether entities should recognize deferred tax on transactions like leases and decommissioning obligations, which give rise to equal and offsetting taxable and deductible temporary differences on day one.

2

The fix

The amendments narrow the exemption in paragraphs 15 and 24: it no longer applies to transactions that, on initial recognition, give rise to equal amounts of taxable and deductible temporary differences.

3

The effect

A lessee now recognizes both a deferred tax asset (on the lease liability) and a deferred tax liability (on the right-of-use asset) at commencement — typically presented net where a legal right of offset exists.

RECENT DEVELOPMENTS

Pillar Two — Mandatory Temporary Exception

International Tax Reform — Pillar Two Model Rules (Amendments to IAS 12), issued 23 May 2023, to address the OECD/G20 BEPS Pillar Two global minimum tax rules now enacted in many jurisdictions.

What Pillar Two does

Large multinational groups (consolidated revenue exceeding €750m in at least two of the last four years) become subject to a 15% global minimum effective tax rate, jurisdiction by jurisdiction, with top-up taxes charged where local rates fall short.

The mandatory exception

Entities apply a mandatory temporary exception to recognizing and disclosing deferred tax assets and liabilities arising from Pillar Two legislation that is enacted or substantively enacted — including QDMTT. This exception applies immediately and retrospectively under IAS 8, and its use must itself be disclosed.

RECENT DEVELOPMENTS

Pillar Two — Disclosure Requirements

Beyond the exception itself, targeted disclosures help users understand an entity's exposure to Pillar Two income taxes — particularly before the legislation takes effect.

1

Current tax, separately

Disclose current tax expense (income) related to Pillar Two income taxes separately from other current tax.

2

Before legislation takes effect

Where Pillar Two law is enacted or substantively enacted but not yet in effect, disclose known or reasonably estimable qualitative and quantitative information about exposure.

3

If not estimable

If information is not known or reasonably estimable, disclose that fact and describe progress made in assessing the exposure.

Impact of IFRS 18 on Income Tax Presentation

IFRS 18 Presentation and Disclosure in Financial Statements replaces IAS 1 and is effective for annual periods beginning on or after 1 January 2027 (early application permitted).

1

A dedicated income taxes category

IFRS 18 requires every item of income and expense in profit or loss to sit in exactly one of five categories — operating, investing, financing, income taxes, or discontinued operations. All tax income and expense recognized under IAS 12, plus related foreign exchange differences, sits in the income taxes category.

2

New mandatory subtotals

“Operating profit” and “Profit before financing and income taxes” become required subtotals. Tax stays below both — sharpening the line between operating performance and the tax charge, but leaving IAS 12 recognition and measurement unchanged.

3

What does NOT change

IFRS 18 does not alter how current or deferred tax is recognized, measured, or disclosed under IAS 12 — including the effective tax rate reconciliation. The impact is presentation and structure, not measurement.

SUMMARY

Key Takeaways

Start from the tax base

Every temporary difference begins with comparing carrying amount to tax base, asset by asset and liability by liability

Recognize DTLs in full

Deferred tax liabilities are recognized for essentially all taxable temporary differences, with narrow, defined exceptions

Apply the probability test to DTAs

Deferred tax assets require probable future taxable profit before they can be recognized

Watch the narrowed exemption

Since 2023, leases and decommissioning obligations no longer escape deferred tax through the initial recognition exemption

Apply the Pillar Two exception

Ignore deferred tax on enacted Pillar Two legislation, but disclose the exception and quantify exposure where possible

Prepare for IFRS 18

From 2027, income tax gets its own dedicated category on the face of profit or loss — recognition under IAS 12 is unchanged

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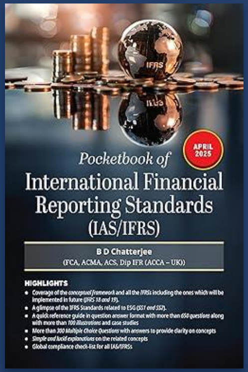

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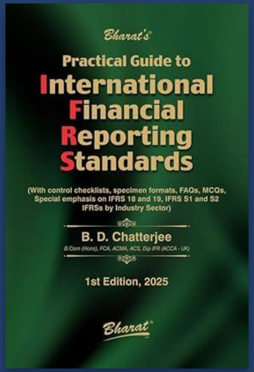

Practical Guide to International Financial Reporting Standards

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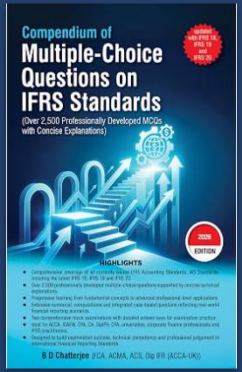

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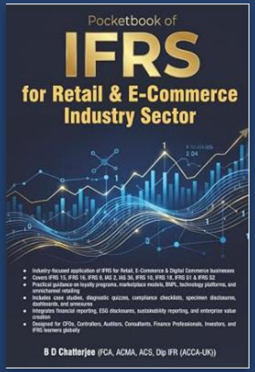

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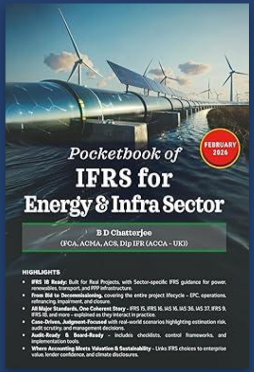

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