IAS 12 *Income Taxes*

Date: June 2023
Addis Ababa

Accounting and Audit Board of Ethiopia
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Aims

- **Understand** IFRS accounting for:
  - current income tax
  - deferred income tax assets in respect of tax losses carried forward
  - other deferred income tax

Current tax

Scope of IAS 12 *Income Taxes* the requirements

- Includes all taxes that are based on taxable income
  - Excludes taxes that are not based on income tax

Current tax *definitions*

- Tax expense/income = current tax + deferred tax.
- Current tax = the amount of income tax payable/recoverable in respect of the taxable profit/loss for the current period or past periods.
- Taxable profit/loss = the profit/loss for a period, determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable/recoverable.

Source: paragraphs 5 and 6 of IAS 12 *Income Taxes*

Current tax
overview of the recognition and measurement requirements

- Recognise a current tax:
  - liability for tax payable on taxable profit for the current and past periods (current tax)
  - asset for overpayments of tax (and for tax losses carried back)
- Measure current tax liability/asset at the amount the entity expects to pay/recover using substantively enacted tax rates

Source: paragraphs 12-15 and 46 of IAS 12 *Income Taxes*

Current tax: permanent differences and tax loss carried forward
Example

- Government specifies that:
  - entities must each year pay a tax = 30% of taxable profit for the year
  - taxable profit is determined in accordance with IFRS adjusted for specified expenses that are excluded from the calculation of taxable income (ie donations and entertainment)
  - If the determination of taxable business income results in a loss in a tax period that loss may be set off against taxable income in the next five (5) tax periods, earlier losses being set off before later losses.

Current tax: permanent differences and tax losses carried forward
Example: summary of class discussion

» Entity determines accounting profit for 2021 in accordance with IFRS to be ETB900,000 (donation expense = ETB100,000).

Entity's current tax expense for **2021** is? Choose one of: 1) ETB1,000,000; 2) ETB900,000; 3) ETB800,000; 4) ETB300,000; 5) ETB230,000; 6) ETB200,000; or 7) nil.

» Entity determines accounting loss for 2022 to be ETB400,000 (entertainment expense = ETB100,000)

Entity's current tax income for **2022** is? Choose one of: 1) ETB500,000; 2) ETB400,000; 3) ETB300,000; 4) ETB130,000; 5) ETB100,000; 6) ETB90,000; or 7) nil.

Current tax: permanent differences and tax losses carried forward
Example: summary of class discussion

	Tax rate	2022	2021
Accounting (loss)/profit		**(400,000)**	**900,000**
Permanent differences:			
- non-deductible entertainment expense		100,000	-
- non-deductible donation expense			100,000
Tax (loss)/profit		**(300,000)**	**1,000,000**
Current tax expense for the year	30%	**Nil***	**300,000**

* **Note: tax loss carried forward = ETB300,000**. Raise deferred tax asset to the extent that recoverability is probable (maximum = ETB90,000, using 30% tax rate).

Current tax: permanent differences and tax losses carried back
Example Scenario 2

» The facts are the same as Scenario 1 except that the tax loss can be carried back one year.

"Losses may be carried back only by **taxpayers engaged in long-term contracts who incur a loss in the final year of a contract** that they otherwise could carry forward but are unable to do so as they are ceasing to carry on business in Ethiopia at the end of the contract. In such circumstances, the taxpayer may carry the loss back to offset profits of the preceding tax year. If the loss cannot be fully offset in the prior year, the unrelieved amount may be carried back to the next preceding tax year. There is no provision for loss carryback for other businesses."

Source: Deloitte Guide to fiscal information | Key economies in Africa 2021, p87

Current tax: permanent differences and tax losses carried back
Example Scenario 2: summary of class discussion

» Entity determines accounting profit for 2021 in accordance with IFRS to be ETB900,000 (donation expense = ETB100,000).

Entity's current tax expense for **2021** is? Choose one of: 1) ETB1,000,000; 2) ETB900,000; 3) ETB800,000; 4) ETB300,000; 5) ETB230,000; 6) ETB200,000; or 7) nil.

» Entity determines accounting loss for 2022 to be ETB400,000 (entertainment expense = ETB100,000)

Entity's current tax income for **2022** is? Choose one of: 1) ETB500,000; 2) ETB400,000; 3) ETB300,000; 4) ETB130,000; 5) ETB100,000; 6) ETB90,000; or 7) nil.

Current tax: permanent differences and tax losses carried forward
Example Scenario 2: summary of class discussion

	Tax rate	2022	2021
Accounting (loss)/profit		**(400,000)**	**900,000**
Permanent differences:			
- non-deductible entertainment expense		100,000	-
- non-deductible donation expense			100,000
Tax (loss)/profit		**(300,000)**	**1,000,000**
Current tax (income)/expense for the year	30%	**(90,000)**	**300,000**

Current tax: capital gains

» Government specifies that:
  - » Corporate normal tax rate = 30%
    - » If the determination of taxable business income results in a loss in a tax period that loss may be set off against taxable income in the next five (5) tax periods, earlier losses being set off before later losses.
  - » Corporate capital gains typically 30%. However, building held for commercial purposes = 15%.
    - » Capital losses may be carried forward indefinitely and offset against capital gains of the same class.

Source: Deloitte Guide to fiscal information | Key economies in Africa 2021, p87

Current tax: capital gains
Example: summary of class discussion

- Entity determines accounting profit and taxable profit for 2021 in accordance with IFRS to be ETB1,100,000 (including capital gain on building held for commercial purposes = ETB100,000).
  - Entity's **current** tax expense for **2021** is? Choose one of: 1) ETB330,000; 2) ETB315,000; or 3) ETB300,000.
- Entity determines accounting profit for 2022 to be ETB900,000 (including accounting loss and tax loss on building held for commercial purposes = ETB100,000).
  - Entity's **current** tax income for **2022** is? Choose one of: 1) ETB300,000; 2) ETB285,000; or 3) ETB270,000.

Note: if recovery of the capital gains tax loss carried forward is probable, ETB15,000 deferred tax income/asset would be recognised in 2022, ie total tax expense for 2022 = ETB285,000.

Current tax: permanent differences and tax losses carried forward
Example: summary of class discussion

2021	Total	Trading	Capital
Accounting and tax profit for 2021	**1,100,000**	**1,000,000**	**100,000**
Tax rate		30%	15%
Current tax expense for 2021	**315,000**	**300,000**	**15,000**

2022	Total	Trading	Capital
Accounting and tax profit/(loss) for 2022	**900,000**	**1,000,000**	**(100,000)**
Tax rate		30%	15%
Current tax expense for 2022	**300,000**	**300,000**	**Nil**

* **Note: tax capital loss carried forward = ETB100,000.** Raise deferred tax asset to the extent that recoverability is probable (maximum = ETB15,000, using 15% tax rate).

Uncertain tax positions

Current tax: uncertain tax position
summary of class discussion

» Corporate tax rate is 30%

» Entity determines for the year ended 31 December 2021:

- » taxable income before uncertain item to be ETB1,000,000
- » 60% probability that a further ETB100,000 gain is taxable

» Entity's current tax expense for 2021 is? Choose one of:

1) ETB300,000 (most favorable outcome);
2) ETB308,000;
3) ETB318,000 (probability weighted outcome);
4) ETB330,000 (most likely outcome); or
5) it depends on how management completed Entity's tax return and which measurement best reflects the expected resolution of the uncertain outcome.

Deferred tax assets:
tax losses carried forward

Deferred tax assets
recoverability recognition requirements

- Deferred tax asset is recognised only to the extent that its recovery is probable
  - tax planning opportunities are available to create taxable profit for the entity in the appropriate future periods; or
  - it is probable that the entity will have sufficient taxable profit relating to the **same taxation authority** and the **same taxable entity** and in the **same period** as the reversal of the deductible temporary difference (or tax loss carryback or carryforward)
    - in making this assessment ignore any deductible temporary differences **originating** in a period after the reporting date because they will themselves require future taxable income in order to be utilised.
- The existence of tax losses is strong evidence that future taxable profit may not be available
  - convincing evidence of probable recovery is needed

Deferred tax assets
recoverability recognition requirements: application guidance

- Deferred tax asset is recognised only to the extent that its recovery is probable
  - KPMG observe that (p779 and p782 of Insights into IFRS 2015/16):
    - probable is not defined in IAS 12
    - consistently with IAS 37 entities often take probable to mean 'more likely than not'
    - however, IAS 12 does not prohibit a higher threshold
    - a 'virtually certain' threshold should not be used
    - portions of unused tax losses should be used when applying the probability threshold
  - Deloitte observe that (p830 iGAAP 2015)
    - probable is not defined in IAS 12
    - probable is generally agreed to mean 'at least more likely than not (ie a probability of greater than 50%)'

Deferred tax asset: tax loss carried forward
example 1 (four scenarios follow)

- In 2022 a manufacturer incurs a **tax loss of ETB100 million**.
- In the jurisdiction in which the manufacturer is based
  - income tax is levied at **30%** on taxable profits
  - taxable profit/loss = accounting profit/loss determined in accordance with the IFRS Accounting Standards.
  - tax losses are carried forward for five years (after which any unutilised tax loss is forfeited).

Deferred tax asset: tax loss carried forward
example 1 ***scenario 1***. *Summary of class discussion.*

» Scenario 1: in 2022 the manufacturer incurred a ETB200 million impairment expense when a meteorite strike obliterated one of its factories. The manufacturer's other factories are unaffected and all operate profitably generating millions of profit each year for decades past, and there is nothing to suggest that they will not continue doing so for the foreseeable future.

» The manufacturer's deferred tax asset at 31 December 2022 is?
Choose one of:
1) ETB100 million;
2) ETB30 million;
3) nil; or
4) another amount.

Deferred tax asset: tax loss carried forward
example 1 ***scenario 2***. *Summary of class discussion.*

» Scenario 2: in 2022 the manufacturer incurred a trading loss for the first time following a steep decline in its profitability due to the elimination of import tariffs resulting in a flood of cheaper imports cannibalising the manufacturer's domestic market. There is little prospect of the manufacturer generating a profit in the next 5 years.

» The manufacturer's deferred tax asset at 31 December 2022 is?
(choose one of):
1) ETB100 million;
2) ETB30 million;
3) nil; or
4) another amount.

Deferred tax asset: tax loss carried forward
example 1 ***scenario 3****. Summary of class discussion.*

» Scenario 3: same as scenario 2 except that Government is consulting on whether to reintroduce import tariffs. At 31/12/2022 there is a 50% probability that tariffs will be reintroduced in the near term.

» The manufacturer's deferred tax asset at 31 December 2022 is? (choose one of):

1) ETB100 million; 2) ETB50 million; 3) ETB30 million;
4) ETB25 million; 5) ETB15 million; or 6) nil; or 7) another amount.

Deferred tax asset: tax loss carried forward
example 1 scenario 4.

» Scenario 4: at 31 December 2022 on the basis of its experience the manufacturer of bespoke heavy machinery reliably forecasts the profit over the next five years as follows:

Probability	Forecast cumulative profit before tax over the next 5 years
40%	ETB100 million profit (2 new orders)
60%	ETB40 million profit (1 new order)
100%	break-even (no new orders)

Deferred tax asset: tax loss carried forward
example 1 ***scenario 4***. *Summary of class discussion*

The manufacturer's deferred tax asset at 31 December 2022 is?

	Amount	Calculation
1)	ETB30 million	30% tax rate x ETB100 million profit (ie profit with 40% probability)
2)	ETB12 million	30% tax rate x ETB40 million profit (ie profit with 60% probability)
3)	nil	30% tax rate x nil profit (ie profit with 100% probability)
4)	ETB14.4 million	Expected value: 30% tax rate x [(40% x ETB100 million) + (20% x ETB40 million) + (40% x nil)]
5)	another	It depends on the level at which the probability recognition threshold is set. For example: if >60% then nil. However, if >50% then ETB12 million.

Deferred tax asset: tax loss carried forward during a tax holiday
Example

- Government grants Entity a tax holiday for 2021 and 2022 (2 years).
- In **2021** Entity's **tax profit** = its **accounting profit** determined in accordance with the IFRS = ETB200 million profit.
- In **2022** Entity's **tax loss** = its **accounting loss** determined in accordance with the IFRS = ETB100 million loss.
- Government levies income tax at **30%** on tax profit
  - specifies that the tax loss carried forward that arose during the tax holiday can be utilsed to reduce income tax payable in 2023 only (if unutilized in 2023 will expire unused).
- Entity realistically forecasts accounting and tax profit for 2023 = ETB40 million; and 2024 = ETB50 million.

KPMG, *Ethiopia Fiscal Guide 2019*, p6 "Business enterprises (registered investments) that suffer losses during a tax holiday period can carry forward such losses for a period equivalent to half of the income tax holiday period. However, this period of carrying forward of losses is capped to 5 years."

Deferred tax asset: tax loss carried forward during a tax holiday
Summary of class discussion

» The carrying amount of the manufacturer's deferred tax at 31/12/2022 is? (choose one of):

1) ETB30 million asset (30% x ETB100 million tax loss carried forward);
2) ETB27 million asset (30% x ETB90 million forecast tax profit for 2023 and 2024);
3) ETB12 million asset (30% x ETB40 million forecast tax profit for 2023 because any unutilised balance expires at end of 2023); or
4) another amount.

Current and deferred tax: capital gains

» Government specifies that:

- » Corporate normal tax rate = **30%**
  - » If the determination of taxable business income results in a loss in a tax period that loss may be set off against taxable income in the next five (5) tax periods, earlier losses being set off before later losses.
- » **Corporate capital gains** typically = 30%. However, building held for commercial purposes = **15%.**
  - » Capital losses may be carried forward indefinitely and offset against capital gains of the same class.

Source: Deloitte Guide to fiscal information | Key economies in Africa 2021, p87

Current and deferred tax: capital gains
Summary of class discussion

» Entity determines accounting profit for 2022 to be ETB900,000 (including accounting loss and tax loss on building held for commercial purposes = ETB100,000).

Entity's current tax for **2022** is? Choose one of: 1) ETB300,000 expense; 2) ETB285,000 expense; 3) ETB270,000 expense; 4) ETB300,000 income; 5) ETB285,000 income; 6) ETB270,000 income; or 7) nil.

Entity's deferred tax for **2022** is? Choose one or more of: 1) ETB30,000 expense; 2) ETB15,000 expense; 3) ETB30,000 income; 4) ETB15,000 income (if recoverable in full probable); or 5) nil (if recovery not probable).

Current and deferred tax: capital gains
Summary of class discussion

2022	Total	Trading	Capital
Accounting and tax profit/(loss) for 2022	**900,000**	**1,000,000**	**(100,000)**
Tax rate		30%	15%
Current tax expense for 2022	**300,000**	**300,000**	**Nil**

Note: tax capital loss carried forward = $100,000. Raise **deferred tax asset** to the extent that recoverability is probable (maximum = $15,000, using 15% tax rate because capital losses may be carried forward indefinitely and offset against capital gains of the same class, ie building held for commercial purposes).

Current and deferred tax

Deferred tax
definitions

» Deferred tax = income tax payable (recoverable) in respect of the taxable profit (tax loss) for future periods as a result of past transactions or events.

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

» Tax base = the tax base of an asset or a liability is the amount attributed to the asset or liability for tax purposes.

Deferred tax
example: definitions

- On 31 December 2023 a company buys a machine for ETB500,000.
- **Accounting:**
  - depreciate machine on straight-line method over 5 years to nil residual value
  - accounting profit = ETB300,000 per year (ie ETB400,000 less ETB100,000 machine depreciation)
- **Tax information:**
  - corporate tax rates: 30% on taxable profit (accounting profit less tax depreciation)
  - depreciate machine on straight-line method over 24 months to nil residual value

Continued…

Deferred tax
example: definitions

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability (30%)	Deferred tax expense (income)
31/12/2023	500,000	500,000	-	-	-
31/12/2024	400,000	250,000	150,000	45,000	45,000
31/12/2025	300,000	-	300,000	90,000	45,000
31/12/2026	200,000	-	200,000	60,000	(30,000)
31/12/2027	100,000	-	100,000	30,000	(30,000)
31/12/2028	-	-	-	-	(30,000)

Deferred tax, current tax and tax expense *example*

Date	Deferred tax liability	Deferred tax expense (income)[1]	Taxable profit[2]	Current tax expense[3]	Tax expense[4]
31/12/2024	45,000	45,000	150,000	45,000	90,000
31/12/2025	90,000	45,000	150,000	45,000	90,000
31/12/2026	60,000	(30,000)	400,000	120,000	90,000
31/12/2027	30,000	(30,000)	400,000	120,000	90,000
31/12/2028	-	(30,000)	400,000	120,000	90,000

[1] change in the deferred tax liability in the year (increase in liability = expense; decrease in liability = income)
[2] ETB400,000 accounting profit before accounting depreciation minus tax depreciation of ETB250,000 in 2024 & 2025)
[3] 30% of taxable profit
[4] current tax expense + deferred tax expense (absent permanent differences etc = 30% of ETB300,000 accounting profit)

50

Income Taxes
Mini-case studies

Mini-case studies

1. PPE revaluation model
2. Investment property
   » Scenario A: cost model and goodwill
   » Scenario B: fair value model
3. Multiple tax rates (various scenarios)

57

57

Objectives

Understand the judgements made to:

» classify tax assets and liabilities

» account for current and deferred tax assets and liabilities

» present and disclose income taxes in consolidated financial statements

58

58

Case study 1:
PPE revaluation model

Deferred tax
overview of the measurement requirements

» Measure deferred tax liability (asset) using
  » undiscounted amounts the entity expects to pay (recover)
  » substantively enacted tax rates that apply to undistributed profits reflecting the tax consequences that would follow from the manner in which the entity expects, at the reporting date, to recover the carrying amount of the asset/settle the liability
    » recovery of **revalued non-depreciable** items of **PPE** is through sale *(a principle)*
    » **rebuttable presumption** that **investment property** carried at fair value is recoverable through sale (rebutted if the **depreciable** and objective is to recover substantially all of its carrying amount through use) *(a rebuttable 'rule')*
  » (when **differential tax rates** apply) the average substantively enacted rate that is expected to apply to its taxable profits of the relevant future periods (for example, when the taxable temporary differences reverse)

Case study: revaluation model, depreciable machine
the facts

31 December 2020 Entity A buys a commercial building for ETB1 million.

» **Accounting**

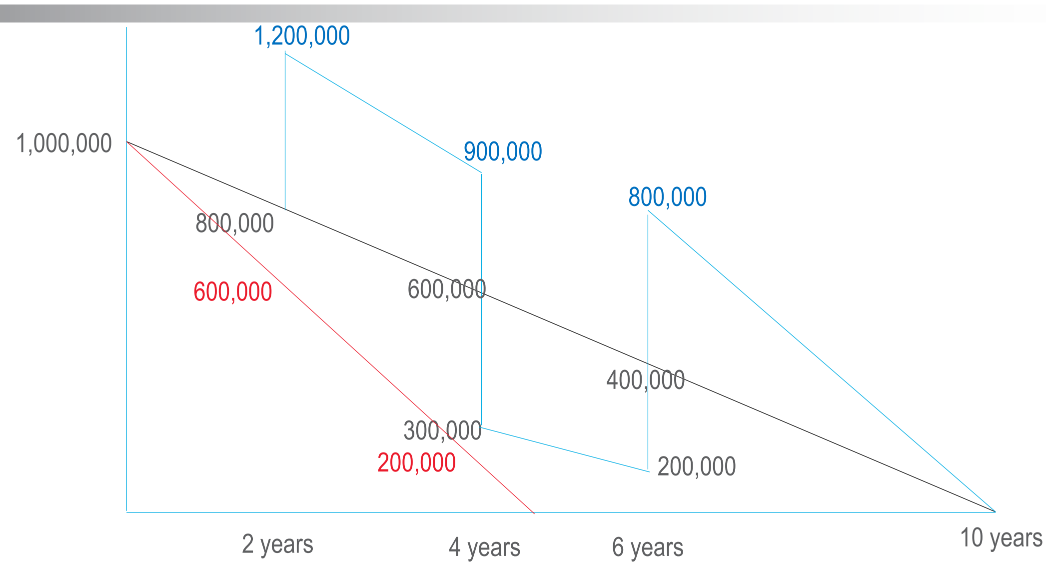
- » depreciation: straight-line to nil residual value over 10 years
- » revaluation model:
  - » **31/12/2022:** fair value = ETB1.2 million
  - » **31/12/2024:** recoverable amount (fair value less costs to sell) = ETB300,000
  - » **31/12/2026:** fair value = ETB800,000

Case study: revaluation model, depreciable machine
the facts

» **Tax**

- » depreciation: straight-line to nil residual value over 5 years
- » tax rates
  - » 30% on taxable income (including recoupment of past depreciation on sale of an asset but excluding capital gains)
  - » 15% on capital gains (for example, proceeds from sale of building less its original cost)

Case study: revaluation model, depreciable machine
the accounting and tax



Case study: revaluation model, depreciable machine
accounting for deferred tax

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2020	**1,000,000**	**1,000,000**	-	-	-
depreciation	(100,000)	(200,000)	100,000	30,000	30,000
31/12/2021	**900,000**	**800,000**	**100,000**	**30,000**	
depreciation	(100,000)	(200,000)	100,000	30,000	30,000
revaluation	400,000 OCI	-	400,000	120,000	120,000 OCI
31/12/2022	**1,200,000**	**600,000**	**600,000**	**180,000**	
depreciation	(150,000)	(200,000)	50,000	15,000	15,000
31/12/2023	**1,050,000**	**400,000**	**650,000**	**195,000**	

Case study: revaluation model, depreciable machine
accounting for deferred tax

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2023	**1,050,000**	**400,000**	**650,000**	**195,000**	
depreciation	(150,000)	(200,000)	50,000	15,000	15,000
revaluation decrease	(300,000) OCI		(300,000)	(90,000)	(90,000) OCI
impairment	(300,000)		(300,000)	(90,000)	(90,000)
31/12/2024	**300,000**	**200,000**	**100,000**	**30,000**	
depreciation	(50,000)	(200,000)	150,000	45,000	45,000
31/12/2025	**250,000**	**-**	**250,000**	**75,000**	

Case study: revaluation model, depreciable machine
accounting for deferred tax

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2025	**250,000**	**-**	**250,000**	**75,000**	
depreciation	(50,000)	-	(50,000)	(15,000)	(15,000)
reverse impairment	200,000	-	200,000	60,000	60,000
revaluation	400,000 OCI	-	400,000	120,000	120,000 OCI
31/12/2026	**800,000**	**-**	**800,000**	**240,000**	
depreciation	(200,000)	-	(200,000)	(60,000)	(60,000)
31/12/2027	**600,000**		**600,000**	**180,000**	

Case study: revaluation model, depreciable machine
accounting for deferred tax

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2027	**600,000**	**-**	**600,000**	**180,000**	
depreciation	(200,000)	-	(200,000)	(60,000)	(60,000)
31/12/2028	**400,000**	**-**	**400,000**	**120,000**	
depreciation	(200,000)	-	(200,000)	(60,000)	(60,000)
31/12/2029	**200,000**	**-**	**200,000**	**60,000**	
depreciation	(200,000)	-	(200,000)	(60,000)	(60,000)
31/12/2030	**-**	**-**	**-**	**-**	

Case study 2: investment property and goodwill
Scenario 1: cost model

Deferred tax
overview of the measurement requirements

- Measure deferred tax liability (asset) using
  - undiscounted amounts the entity expects to pay (recover)
  - substantively enacted tax rates that apply to undistributed profits reflecting the tax consequences that would follow from the manner in which the entity expects, at the reporting date, to recover the carrying amount of the asset/settle the liability
    - recovery of revalued non-depreciable items of PPE is through sale *(a principle)*
    - **rebuttable presumption** that **investment property carried at fair value** is recoverable through sale (rebutted if the **depreciable** and objective is to recover substantially all of its carrying amount through use) *(a rebuttable 'rule')*
  - (when **differential tax rates** apply) the average substantively enacted rate that is expected to apply to its taxable profits of the relevant future periods (for example, when the taxable temporary differences reverse)

Case study: investment property
the facts

- **31/12/2020** Entity A buys an investment property (building) cost = ETB1,000,000
- on **31/12/2024** impairment event
- on **31/12/2026** the condition that gave rise to the impairment reverses

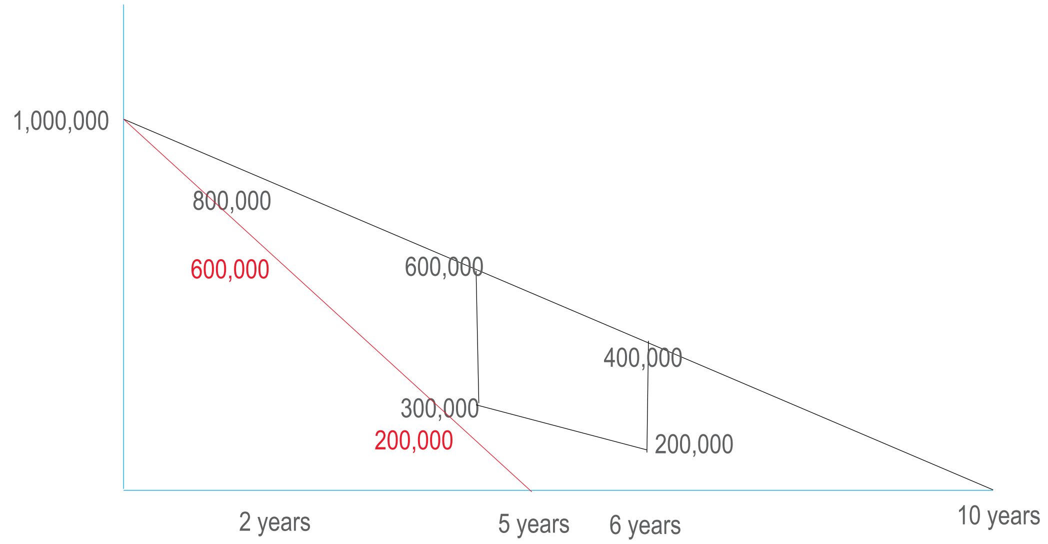
Case study: investment property
the facts

- **Tax**
  - depreciation buildings: straight-line to nil residual value over **5 years**
  - tax rates
    - **30%** on taxable income (including recoupment of past depreciation on sale of an asset but excluding capital gains)
    - **15%** on capital gains (for example, proceeds from sale of land less its original cost)

Case study: investment property
the facts

- **Accounting**
  - cost model
  - depreciation buildings: straight-line; nil residual value; 10 years
- on **31/12/2024 recoverable amount of** building = ETB300,000

Case study: investment property building cost model
the accounting and tax



Case study: investment property building cost model
accounting for deferred tax

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2020	**1,000,000**	**1,000,000**	-	-	-
depreciation	(100,000)	(200,000)	100,000	30,000	30,000
31/12/2021	**900,000**	**800,000**	**100,000**	**30,000**	
depreciation	(100,000)	(200,000)	100,000	30,000	30,000
31/12/2022	**800,000**	**600,000**	**200,000**	**60,000**	
depreciation	(100,000)	(200,000)	100,000	30,000	30,000
31/12/2023	**700,000**	**400,000**	**300,000**	**90,000**	

Case study: investment property building cost model *accounting for deferred tax*

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2023	**700,000**	**400,000**	**300,000**	**90,000**	
depreciation	(100,000)	(200,000)	100,000	30,000	30,000
impairment	(300,000)		(300,000)	(90,000)	(90,000)
31/12/2024	**300,000**	**200,000**	**100,000**	**30,000**	
depreciation	(50,000)	(200,000)	150,000	45,000	45,000
31/12/2025	**250,000**	**-**	**250,000**	**75,000**	

75

Case study: investment property building cost model *accounting for deferred tax*

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2025	**250,000**	**-**	**250,000**	**75,000**	
depreciation	(50,000)	-	(50,000)	(15,000)	(15,000)
reverse impairment	200,000	-	200,000	60,000	60,000
31/12/2026	**400,000**	**-**	**400,000**	**120,000**	
depreciation	(100,000)	-	(100,000)	(30,000)	(30,000)
31/12/2027	**300,000**		**300,000**	**90,000**	

76

Case study: investment property building cost model *accounting for deferred tax*

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2027	**300,000**	**-**	**300,000**	**90,000**	
depreciation	(100,000)	-	(100,000)	(30,000)	(30,000)
31/12/2028	**200,000**	**-**	**200,000**	**60,000**	
depreciation	(100,000)	-	(100,000)	(30,000)	(30,000)
31/12/2029	**100,000**	**-**	**100,000**	**30,000**	
depreciation	(100,000)	-	(100,000)	(30,000)	(30,000)
31/12/2030	**-**	**-**	**-**	**-**	

77

Case study 2: investment property
Scenario 2: fair value

Deferred tax
overview of the measurement requirements

- Measure deferred tax liability (asset) using
  - undiscounted amounts the entity expects to pay (recover)
  - substantively enacted tax rates that apply to undistributed profits reflecting the tax consequences that would follow from the manner in which the entity expects, at the reporting date, to recover the carrying amount of the asset/settle the liability
    - recovery of revalued non-depreciable items of PPE is through sale *(a principle)*
    - **rebuttable presumption** that **investment property carried at fair value** is recoverable through sale (rebutted if the **depreciable** and objective is to recover substantially all of its carrying amount through use) *(a rebuttable 'rule')*
  - (when **differential tax rates** apply) the average substantively enacted rate that is expected to apply to its taxable profits of the relevant future periods (for example, when the taxable temporary differences reverse)

Case study: investment property
the facts

- **31/12/2020** Entity A buys an investment property (buildings) for ETB1,000,000.

Case study: investment property
the facts

» **Tax**

» depreciation buildings: straight-line to nil residual value over **5 years**

» tax rates

» **30%** on taxable income (including recoupment of past depreciation on sale of an asset but excluding capital gains)

» **15%** on capital gains

81

Case study: investment property
the facts

» **Accounting** fair value model for the building.
» Management intend never to sell the building (rebut presumption).
» **Fair value** of the building:

Date	Fair value	Date	Fair value
31/12/2020	1,000,000	**31/12/2026**	800,000
31/12/2021	900,000	**31/12/2027**	600,000
31/12/2022	1,200,000	**31/12/2028**	400,000
31/12/2023	1,050,000	**31/12/2029**	200,000
31/12/2024	300,000	**31/12/2030**	-
31/12/2025	250,000		

82

Case study: investment property building fair value model *accounting for deferred tax*

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2020	**1,000,000**	**1,000,000**	**-**	**-**	**-**
2011	(100,000)	(200,000)	100,000	30,000	30,000
31/12/2021	**900,000**	**800,000**	**100,000**	**30,000**	
depreciation		(200,000)	200,000	60,000	60,000
fair value	300,000	-	300,000	90,000	90,000
31/12/2022	**1,200,000**	**600,000**	**600,000**	**180,000**	
2013	(150,000)	(200,000)	50,000	15,000	15,000
31/12/2023	**1,050,000**	**400,000**	**650,000**	**195,000**	

83

Case study: investment property building fair value model *accounting for deferred tax*

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2023	**1,050,000**	**400,000**	**650,000**	**195,000**	
depreciation		(200,000)	200,000	60,000	60,000
fair value	(750,000)		(750,000)	(225,000)	(225,000)
31/12/2024	**300,000**	**200,000**	**100,000**	**30,000**	
2015	(50,000)	(200,000)	150,000	45,000	45,000
31/12/2025	**250,000**	**-**	**250,000**	**75,000**	

84

Case study: investment property building fair value model accounting for deferred tax

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2025	**250,000**	**-**	**250,000**	**75,000**	
fair value	550,000	-	500,000	150,000	150,000
31/12/2026	**800,000**	**-**	**800,000**	**240,000**	
fair value	(200,000)	-	(200,000)	(60,000)	(50,000)
31/12/2027	**600,000**		**600,000**	**180,000**	

85

Case study: investment property building fair value model accounting for deferred tax

Date	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Deferred tax liability	Deferred tax expense (income)
31/12/2027	**600,000**	**-**	**600,000**	**180,000**	
fair value	(200,000)	-	(200,000)	(60,000)	(50,000)
31/12/2028	**400,000**	**-**	**400,000**	**120,000**	
fair value	(200,000)	-	(200,000)	(60,000)	(60,000)
31/12/2029	**200,000**	**-**	**200,000**	**60,000**	
fair value	(200,000)	-	(200,000)	(60,000)	(60,000)
31/12/2030	**-**	**-**	**-**	**-**	

86

Case study 3: multiple income taxes/tax rates

Deferred tax
overview of the measurement requirements

» Measure deferred tax liability (asset) using

» undiscounted amounts the entity expects to pay (recover)

» substantively enacted tax rates that apply to undistributed profits reflecting the tax consequences that would follow from the manner in which the entity expects, at the reporting date, to recover the carrying amount of the asset/settle the liability

» recovery of revalued **non-depreciable** items of **PPE** is through sale *(a principle)*

» **rebuttable presumption** that **investment property** carried at fair value is recoverable through sale (rebutted if the **depreciable** and objective is to recover substantially all of its carrying amount through use) *(a rebuttable 'rule')*

» (when **differential tax rates** apply) the average substantively enacted rate that is expected to apply to its taxable profits of the relevant future periods (for example, when the taxable temporary differences reverse)

Building
test your understanding

» 31/12/2000 Entity A buys a factory building for ETB1 million

» 31/12/2010 fair value of building is ETB1.2 million

» Depreciation

» **accounting** (when relevant): straight-line to nil residual value over 50 years

» **tax:** straight-line to nil residual value over 20 years

» Tax rates

» 30% on taxable income (including recoupment of past depreciation on sale of an asset but excluding capital gains)

» 15% on capital gains (for example, proceeds from sale of PPE less its original cost)

89

Fair value model investment property: presumption recover through sale (Scenario A: is inconsistent with nil residual value)
Summary of class discussion

The carrying amount of deferred tax at 31/12/2010 is?
Choose one of:

	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Applicable tax rate	Deferred tax liability
1)	1,200,000	1,000,000	200,000	30%	**60,000**
2)	1,200,000	1,000,000	200,000	15%	**30,000**
3)	1,200,000	500,000	700,000	30% on ETB300,000; 15% on ETB400,000	**120,000**
4)	1,200,000	500,000	700,000	30% on ETB500,000; 15% on ETB200,000	**180,000**

91

Fair value model investment property: rebutted presumption, ie intend to recover through use (Scenario B)

Summary of class discussion

The carrying amount of deferred tax at 31/12/2010 is?

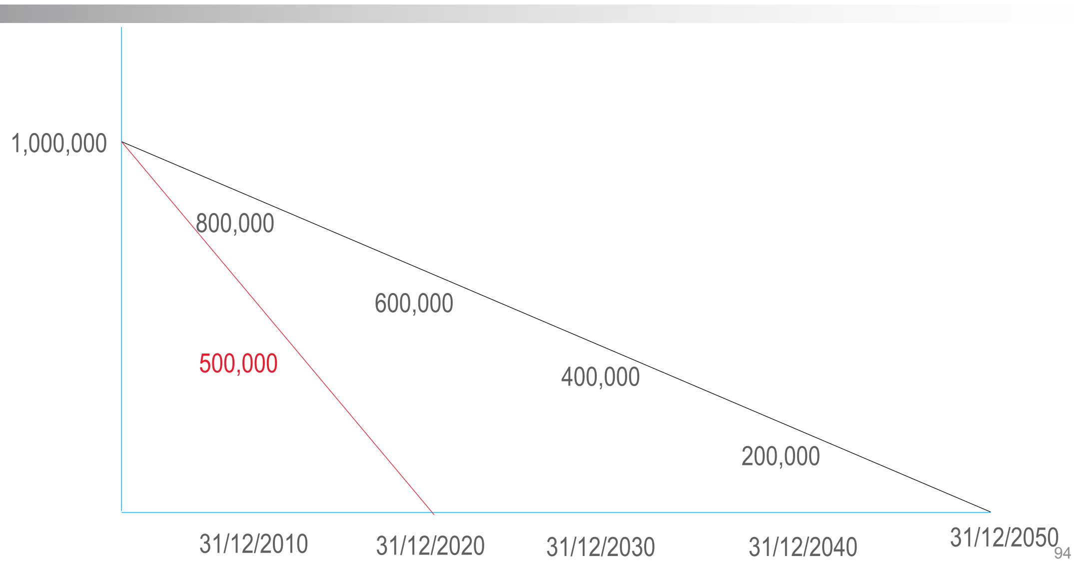
Choose one of:

	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Applicable tax rate	Deferred tax liability
1)	1,200,000	500,000	700,000	30%	**210,000**
2)	1,200,000	500,000	700,000	15%	**105,000**
3)	1,200,000	500,000	700,000	30% on ETB300,000; 15% on ETB400,000	**150,000**
4)	1,200,000	500,000	700,000	30% on ETB500,000; 15% on ETB200,000	**180,000**

93

Cost model (investment property and PPE) (Scenario C)

test your understanding (carrying amount and tax base)



94

Cost model (investment property and PPE) (Scenario C)
summary of class discussion

The carrying amount of deferred tax at 31/12/2010 is?

Choose one of:

	Carrying amount	Tax base (ie future tax deductions)	Temporary difference	Applicable tax rate	Deferred tax liability
1)	800,000	500,000	300,000	30%	**90,000**
2)	800,000	500,000	300,000	15%	**45,000**
3)	1,200,000	500,000	700,000	30% on ETB300,000; 15% on ETB400,000	**150,000**
4)	1,200,000	500,000	700,000	30% on ETB500,000; 15% on ETB200,000	**180,000**

96