



FRED 83 DRAFT AMENDMENTS TO FRS 102 AND FRS 101: INTERNATIONAL TAX REFORM - PILLAR TWO MODEL RULES

Issued 22 May 2023

ICAEW welcomes the opportunity to comment on the FRED 83 *Draft amendments to FRS 102 and FRS 101: International tax reform - Pillar Two model rules* published by the Financial Reporting Council in April 2023, a copy of which is available from this [link](#).

For questions on this response please contact the Corporate Reporting Faculty at crf@icaew.com quoting REP 45/23

We believe there continues to be significant uncertainty over the accounting for deferred taxes arising from the Pillar Two model rules. This uncertainty will undoubtedly result in differing interpretations arising in practice, with the resulting information likely to prove of limited use to users of the financial statements.

We support the proposed temporary exceptions to FRS 102, which we believe will provide an appropriate solution in these circumstances. However, we have concerns with the proposed disclosure requirements in paragraph 29.29(b) which we believe require further consideration before the amendments are finalised.

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KEY POINTS

BROADLY SUPPORTIVE

1. We believe there continues to be significant uncertainty over the accounting for deferred taxes arising from the Pillar Two model rules. This uncertainty will undoubtedly result in differing interpretations arising in practice, with the resulting information likely to prove of limited use to users of the financial statements.
2. While the accounting for deferred taxes arising from the Pillar Two model rules is clearly a complex matter requiring careful consideration, the imminent enactment of tax law to implement these rules necessitates urgent action now. We support the proposed temporary exceptions to FRS 102, which we believe will provide an appropriate solution in these circumstances.

DISCLOSURES

3. We have concerns with the proposed disclosure requirements in paragraph 29.29 which, in our view, could result in lengthy disclosures that do not provide meaningful information. We believe a better alternative would be to adopt a more principles-based approach which allows entities to assess and disclose how Pillar Two legislation might affect the tax charge in the future, both in terms of the amount and variability.
4. We raised similar concerns in our [response](#) to the IASB's recent proposed amendments relating to the Pillar Two model rules. Although at the time of writing the IASB amendments have not yet been finalised, we note the outcome of a recent [Supplementary IASB meeting](#), whereby the members tentatively agreed to move towards setting a disclosure objective. This approach would require entities to 'disclose information that helps users of financial statements understand the entity's exposure to Pillar Two taxes arising from the legislation' with further details to be provided on how to meet that objective.
5. We recommend that the FRC considers the IASB's recent tentative decisions on this matter when finalising its own amendments. At the very least we do not believe that the disclosure requirements under FRS 102 should be any more onerous or prescriptive than those to be eventually introduced by the IASB.

EFFECTIVE DATES

6. We support the proposed effective dates and, notwithstanding our concerns regarding the proposed disclosures, urge the FRC to finalise the amendments as quickly as possible to enable entities to take up the exception at the earliest opportunity. In our response to question 5 we have highlighted a potential issue regarding the proposed effective date for paragraph 29.12A, and the need for the FRC to consider the effective date of the proposed disclosures in interim financial statements.

ANSWERS TO SPECIFIC QUESTIONS

Question 1 Do you agree that the proposed definition of the term ‘Pillar Two legislation’ would capture all transactions that are relevant to this topic? If not, please provide examples to support your view.

7. Yes, we agree with the proposed definition of the term ‘Pillar Two legislation’ and believe it will capture all transactions that are relevant to this topic.

Question 2 Do you agree with the proposed amendments to FRS 102 that introduce mandatory temporary exceptions to recognising or disclosing information about deferred tax assets and liabilities related to Pillar Two income tax (proposed paragraph 29.2B), and to taking the effects of Pillar Two legislation into account when measuring deferred tax assets and liabilities (proposed paragraph 29.12)? If not, why not?

8. We support the proposed amendments to FRS 102 which will introduce mandatory temporary exceptions to recognising or disclosing information about deferred tax assets and liabilities related to Pillar Two income tax, and to taking the effects of Pillar Two legislation into account when measuring deferred tax assets and liabilities.
9. We agree with the FRC that the exceptions are necessary due to the risk that entities would otherwise apply the principles and requirements in Section 29 *Income Tax* inconsistently to account for deferred taxes related to Pillar Two legislation. In our view, the proposed temporary exceptions provide an appropriate solution in these circumstances.
10. We welcome this temporary exception being kept under review by the FRC. In particular, we believe it will be important for the FRC to monitor ongoing developments at the IASB and, when appropriate, for the FRC to consider how future relevant changes to IFRS Accounting Standards might be reflected in UK GAAP.
11. As a minor note, we believe there is a small error in paragraph 29.2B which should refer to ‘Pillar Two income taxes’.

Question 3 Do you agree with the proposed amendments to FRS 102 that require an entity to disclose: (a) the fact that it expects to fall within the scope of Pillar Two legislation (proposed paragraph 29.28); (b) the current tax expense related to Pillar Two income taxes (proposed sub-paragraph 29.26(g)); and (c) information that will enable users of financial statements to understand a group’s potential exposure to paying top-up tax, when Pillar Two legislation has been enacted or substantively enacted but is not yet in effect (proposed paragraph 29.29)? If not, why not?

12. We agree with the proposals to require an entity to disclose the fact that it expects to fall within the scope of Pillar Two legislation, and to disclose the current tax expense related to Pillar Two income taxes. To avoid any potential uncertainty, we believe it would be helpful if the amendments clarify that, for the purpose of the proposed current tax expense disclosure, all taxes arising from the Pillar Two model are considered income taxes.
13. We have some concerns regarding proposed paragraph 29.29. The disclosures proposed in paragraphs 29.29(b) and (c) would be based on the entity’s average effective tax rate, as opposed to the effective tax rate required in accordance with the Pillar Two model rules. We understand that there are significant differences between the two methodologies such that using the effective tax rate in accordance with FRS 102, as the basis for disclosure would result in disclosures which are not indicative of an entity’s exposure to top-up taxes.
14. Overall, we are concerned that the proposed disclosures in paragraphs 29.29(b) and (c) would cause confusion to preparers and could result in lengthy disclosures which have limited use to users of the financial statements.

15. We raised similar concerns in our [response](#) to the IASB's proposals which would have required an entity to disclose similar, very specific information on a jurisdiction by jurisdiction basis. In responding to the IASB we suggested that a better alternative would be to adopt a more principles-based approach which allows entities to assess and disclose how Pillar Two legislation might affect the tax charge in the future, both in terms of the amount and variability.
16. We are pleased to note that at the recent [Supplementary IASB meeting](#), the members tentatively agreed to move towards setting a disclosure objective which would require entities to 'disclose information that helps users of financial statements understand the entity's exposure to Pillar Two taxes arising from the legislation' with further details to be provided on how to meet that objective.
17. We believe that the FRC should also adopt a more principles-based approach when setting the disclosure requirements intended to demonstrate an entity's exposure to Pillar Two tax legislation. Although we do not have the benefit of having the IASB's final amendments available at the time of writing, we recommend that the FRC considers the IASB's recent tentative decisions on this matter. At the very least we do not believe that the disclosure requirements under FRS 102 should be any more onerous or prescriptive than those to be eventually introduced by the IASB.

Question 4 Do you agree with the proposal to exempt qualifying entities, as defined in FRS 102 or FRS 101, from the disclosures that would otherwise be required by proposed paragraph 29.29 of FRS 102 and proposed paragraph 88C of IAS 12 Income Taxes respectively? If not, why not?

18. We broadly agree with the FRC's assessment that the most useful information for users of financial statements about exposure to paying top-up taxes will be in the consolidated financial statements of the group in which the entity is consolidated. However, we believe there may be instances when information would also be helpful at an individual UK subsidiary level, for example, a qualifying entity which is a UK-based intermediate company owned by an overseas parent company and is liable to pay top-up taxes as a result of the Pillar Two model rules. While paragraph 29.25 of FRS 102 might potentially help in this respect for FRS 102 reporters, it may not go far enough in requiring relevant information on Pillar Two income taxes.
19. If the FRC decides to amend the disclosure requirements as proposed in paragraph 29.29(b) and (c) to follow a more principles-based approach, then we suggest that an exemption for qualifying entities as defined under FRS 102 or FRS 101 would not be necessary. This is because entities will be able to determine for themselves whether information on Pillar Two tax legislation is relevant within their individual financial statements and provide disclosures to meet the disclosure objective. Where information is not relevant at an entity level, then no disclosures would be made in the individual financial statements. In our view, this would ensure that all relevant entities are captured, with an appropriate level of disclosure imposed on individual entities across the group.
20. That said, if the FRC does not amend the proposed disclosure requirements we would support the proposal to exempt qualifying entities from the disclosures in proposed paragraph 29.29 of FRS 102 (and the proposed paragraph 88C of IAS 12 *Income Taxes* respectively) provided that equivalent disclosures are made in the consolidated financial statements in which the entity is included. We believe this would be necessary to avoid lengthy and potentially unhelpful disclosures in individual financial statements.

Question 5 Do you agree with the proposed effective dates for these amendments? If not, what difficulties do you foresee?

21. We agree with the FRC's proposal for immediate application of the exception in paragraph 29.2B. We think that immediate application of the measurement exemption is the most effective way to provide clarity and reduce diversity in accounting practice in this complex area.
22. We also believe that the proposed paragraph 29.12A, which introduces the exception from taking into account the effects of Pillar Two legislation when measuring deferred tax assets and liabilities, should be introduced with immediate effect. Currently it is proposed that this requirement would come into effect for accounting periods beginning on or after 1 January 2023.
23. We agree with the proposal for the effective date for the disclosures in 29.26(g), 29.28 and 29.29 to be accounting periods beginning on or after 1 January 2023. We agree that these should not become effective immediately as this would result in some entities having insufficient time to prepare.
24. We note that there is no reference to interim accounts in the exposure draft. We believe the FRC will need to specify the effective date of the proposed disclosure requirements for entities preparing interim reports in accordance with FRS 104. That is, to provide an exemption from certain disclosure requirements for interim periods ending on or before 31 December 2023.
25. It is also important to proceed as quickly as possible to reduce the risk of worse outcomes, such as entities reporting deferred tax for top-up taxes in one period, or making efforts to do so, and removing them in a subsequent period.

Question 6 In relation to the consultation stage impact assessment, do you have any comments on the costs and benefits identified? Please provide evidence to support your views.

26. We have no comments on the costs and benefits, over and above comments made elsewhere in this response.