



**IASB PUBLISHES EXPOSURE DRAFT -  
INTERNATIONAL TAX REFORM -  
PILLAR TWO MODEL RULES**  
INTERNATIONAL FINANCIAL REPORTING BULLETIN

2023/02



## BACKGROUND

In December 2021, the Organisation for Economic Co-operation and Development (OECD) published *Tax Challenges Arising from the Digitalisation of the Economy - Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS* (Pillar Two model rules). In March 2022, the OECD released commentary and illustrative examples that elaborate on the application and operation of the rules and clarify certain terms.

The Pillar Two model rules aim to ensure that large multinational groups (generally with revenue exceeding €750 million) pay a minimum amount of tax on income arising in each jurisdiction in which they operate. This would be achieved 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%.

Stakeholders raised concerns with the IASB about the potential implications on income tax accounting, especially accounting for deferred taxes, arising from the Pillar Two model rules. The stakeholders emphasised an urgent need for clarity given the imminent enactment of tax law to implement the rules in some jurisdictions.

In response to stakeholder concerns, the IASB has proposed amendments to IAS 12 *Income Taxes*. It issued Exposure Draft [International Tax Reform—Pillar Two Model Rules \(Proposed Amendments to IAS 12\)](#) on 9 January 2023. The proposed amendments provide an exception to entities from recognition and disclosure of information about deferred tax assets and liabilities related to Pillar Two model rules.

The Exposure Draft is open for comments until 10 March 2023.

**STATUS**  
Exposure Draft

**ACCOUNTING IMPACT**  
The proposed amendments create a temporary exception to the requirements of IAS 12 *Income Taxes* from recognition and disclosure of information about deferred tax assets and liabilities related to Pillar Two income taxes. The Exposure Draft also proposes additional disclosure requirements with respect to an entity's exposure to Pillar Two income taxes.

### Which entities will benefit from the proposed amendments?

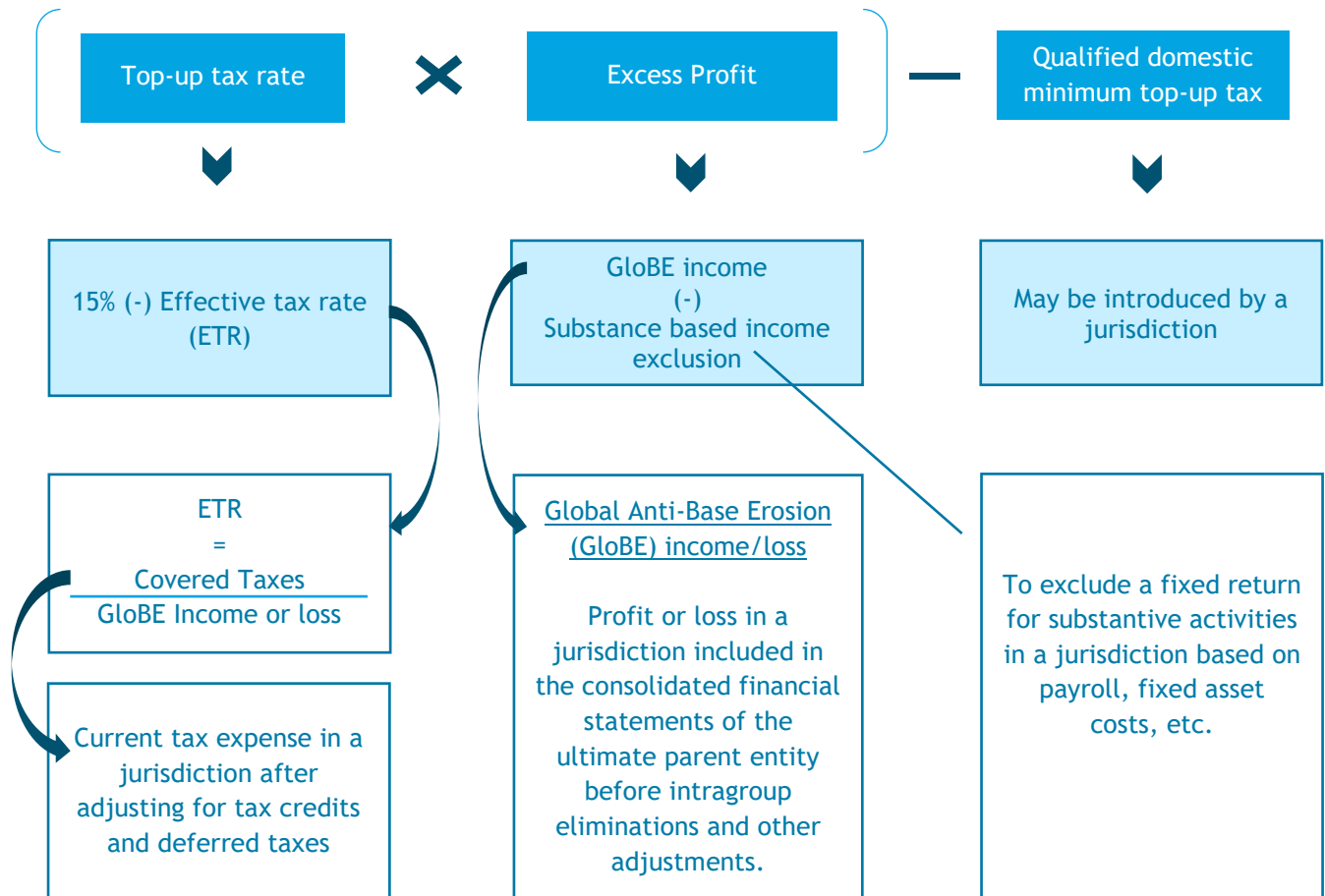
Pillar Two model rules generally apply to multinational groups with revenue in their consolidated financial statements exceeding €750 million in at least two of the four preceding fiscal years. These entities will benefit from the relief provided by the proposed amendments.



## PILLAR TWO MODEL RULES

The Pillar Two model requires payment of top-up tax by multinational entities within its scope.

Top-up tax is calculated as below:



### What were the concerns raised with respect to the accounting implications?

The following are some of the main concerns raised by stakeholders about the implications for income tax accounting of Pillar Two income taxes:

- Scope of IAS 12:

The stakeholders noted that it was not clear whether top-up tax is an income tax in the financial statements of a group's subsidiaries. For example, if an entity is liable to pay such tax with respect to profits of entities that are not part of its reporting group (for example, with respect to a fellow subsidiary's profits).

- Lack of clarity on deferred tax accounting, for example:

- Whether the Pillar Two model rules create additional temporary differences?
- Whether to remeasure deferred taxes recognised under domestic tax regime to reflect potential top-up tax payable?

- Tax rate to be used to measure deferred taxes: The tax rate that will apply to an entity's excess profit in future periods depends on a number of factors that are difficult to forecast reliably.

As some jurisdictions are expected to enact laws to implement the Pillar Two model rules in the first half of 2023, the stakeholders highlighted an urgent need for clarity on these issues.

In response to stakeholder concerns, the IASB issued the Exposure Draft of the proposed amendments on 9 January 2023, with a short (60 day) comment period.

## THE PROPOSED AMENDMENTS

The Exposure Draft proposes amendments to the scope of IAS 12 and additional disclosure requirements.

### Proposed amendment to the Scope of IAS 12

The proposed amendments have inserted paragraph 4A in the scoping requirements of IAS 12 as below:

#### IAS 12.4A (as proposed)

This Standard applies to income taxes arising from tax law enacted or substantively enacted to implement the Pillar Two model rules published by the Organisation for Economic Co-operation and Development, including tax law that implements qualified domestic minimum top-up taxes described in those rules. Such tax law, and the income taxes arising from it, are hereafter referred to as 'Pillar Two legislation' and 'Pillar Two income taxes'. As an exception to the requirements in this Standard, an entity shall neither recognise nor disclose information about deferred tax assets and liabilities related to Pillar Two income taxes.

The following are some key points to note with regards to the proposed amendments:

1. Pillar Two income taxes scoped in:

The proposed amendments bring Pillar Two income taxes within the scope of IAS 12.

2. Temporary exception created to the accounting for deferred tax:

The IASB has proposed to introduce a temporary exception to the requirements in IAS 12 by which entities will not be required or permitted to recognise and disclose information about deferred tax assets and liabilities related to Pillar Two income taxes.

This exception would provide affected entities with relief from accounting for deferred tax assets and liabilities in relation to Pillar Two income taxes to be enacted in a short period of time. The exception would also avoid inconsistent application of the requirements of IAS 12.

3. Mandatory application of the exception:

The exception is proposed to be mandatory, which would result in greater comparability between financial statements and eliminate the risk of entities inadvertently developing accounting policies that are inconsistent with the requirements of IAS 12.

4. Duration for the exception not specified:

The Exposure Draft does not specify an end date to the exception.

As noted by the IASB in the Basis for Conclusions (BC17) to the Exposure Draft, at present, it is not possible to determine how much time will be required to complete the work needed to determine

how entities apply the principles and requirements of IAS 12 to account for deferred taxes related to Pillar Two income taxes. Therefore, the IASB has proposed not to specify the duration of the exception.

## Proposed disclosure requirements

The Exposure Draft requires an entity to disclose that it has applied the exception to recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes.

### **Disclosure requirements when Pillar Two legislation is in effect:**

In periods when Pillar Two legislation is in effect, the proposed amendments require an entity to disclose separately its current tax expense (income) related to Pillar Two income taxes.

### **Disclosure requirements when Pillar Two legislation is enacted or substantively enacted but not yet in effect:**

In periods in which Pillar Two legislation is enacted or substantively enacted, but not yet in effect, the proposed amendments require the following disclosures **for the current period only**:

- information about such legislation enacted or substantively enacted in jurisdictions in which the entity operates;
- the jurisdictions in which the entity's average effective tax rate (calculated as specified in IAS 12.86) for the current period is below 15% and the tax expense (income) and accounting profit for these jurisdictions in aggregate, as well as the resulting weighted average effective tax rate;
- Whether the entity's assessment (if any has been made) indicates that there are jurisdictions:
  - i. Where the entity's effective tax rate is below 15% but in relation to which the entity might not be exposed to paying Pillar Two income taxes; or
  - ii. Where the entity's effective tax rate is above 15% but in relation to which the entity might be exposed to paying Pillar Two income taxes.

It should be noted that the effective tax rate specified in the disclosure requirements above is required to be calculated in accordance with IAS 12 and not in accordance with the requirements of Pillar Two legislation.

The Pillar Two model rules include specific requirements that differ from those in IAS 12 in relation to calculating an effective tax rate. However, preparing information in accordance with IAS 12 requirements would be less costly than preparing it in accordance with Pillar Two legislation. As observed by the IASB in the Basis for Conclusions, such information would still be useful in providing an indication of an entity's potential exposure to paying top-up tax and the jurisdictions where in which such exposure might exist.

If an entity's assessment indicates that there are additional or fewer jurisdictions in which the entity might be exposed to paying Pillar Two income taxes as compared to those with average effective tax rate of less than 15%, the Exposure Draft requires disclosure of these jurisdictions. However, this disclosure is required only if the entity has carried out such an assessment. The proposed amendments do not mandatorily require an entity to carry out this assessment.



The following example illustrates the disclosure requirements:

Fact pattern:

A multinational entity operates in jurisdictions A, B, C, D, E and F. The entity's annual reporting year end is 31 December.

At 31 December 2023, enactment of the Pillar Two legislation in the above jurisdictions is at various stages as below:

Jurisdiction A: Pillar Two legislation enacted and in effect from July 2023. Entity A will be required to pay Pillar Two income taxes in Jurisdiction A.

Jurisdiction B: Pillar Two legislation enacted in November 2023, but not yet in effect. The entity's average effective tax rate as per IAS 12 requirements is below 15% in this jurisdiction.

Jurisdiction C: Pillar Two legislation substantively enacted by December 2023, but not yet in effect. The entity's average effective tax rate as per IAS 12 requirements is below 15% in this jurisdiction.

Jurisdiction D: Pillar Two legislation substantively enacted by December 2023, but not yet in effect. The entity's average effective tax rate as per IAS 12 requirements is below 15% in this jurisdiction. However, based on the entity's assessment of its Pillar Two exposure, the entity might not be exposed to paying Pillar Two income taxes for Jurisdiction D.

Jurisdiction E: Pillar Two legislation substantively enacted by December 2023, but not yet in effect. The entity's average effective tax rate as per IAS 12 requirements is above 15% in this jurisdiction.

Jurisdiction F: Pillar Two legislation not substantively enacted by 31 December 2023.

What are the disclosure requirements in accordance with the Exposure Draft?

The entity is required to disclose the following with respect to Pillar Two taxes in the financial statements for the year ended 31 December 2023:

- The fact that the entity has applied the exception to recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes.
- Separate disclosure of current tax expense/ (income) related to Pillar Two income taxes for jurisdiction A.
- For jurisdictions B, C, D and E where Pillar Two legislation is enacted or substantively enacted, but not yet in effect:
  - Information about the legislation.
  - Disclosure of jurisdictions B, C and D as jurisdictions in which the entity's average effective tax rate is below 15%. Aggregate tax expense (income), accounting profit and weighted average effective tax rate for jurisdictions B, C and D. *(It should be noted that although as per the entity's assessment it might not be exposed to paying Pillar Two income taxes in jurisdiction D, for this disclosure jurisdiction D will be included).*
  - The fact that the entity's assessment indicates that there are jurisdictions where the entity's effective tax rate is below 15% but in relation to which the entity might not be exposed to paying Pillar Two income taxes.

No disclosures relating to Jurisdiction F are required because the Pillar Two legislation has not been substantively enacted as at 31 December 2023.

## Effective date and transition

The Exposure Draft proposes that the scope exception and disclosure of the fact of application of the exception would be applicable immediately upon issue of the amendments and retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Other disclosure requirements are proposed to be applicable for annual reporting periods beginning on or after 1 January 2023.

As the amendments on scope exception are proposed to be effective retrospectively, an entity would apply the exception even if the date Pillar Two legislation is enacted or substantively enacted is before the date on which the IASB issues final amendments.

### Example of retrospective application of the exception:

An entity's annual reporting period end is 31 March. In one of the jurisdictions that the entity operates in, Pillar Two legislation is enacted in March 2023.

Assume that the final amendments are issued in May 2023.

By May 2023, the entity is yet to issue its annual financial statements for the year ended 31 March 2023.

As the amendments are effective retrospectively, the entity would apply the scope exception in its annual financial statements for the year ended 31 March 2023 and disclose that fact. The entity would not be required to make the other disclosures as they are only required for annual reporting periods beginning on or after 1 January 2023.

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