



Income Tax

April 2009

**COMMENTS TO THE IASB AND THE AcSB
MUST BE RECEIVED BY
JULY 31, 2009**

This Exposure Draft of proposed accounting standards is issued by the Accounting Standards Board. The Board is composed of persons knowledgeable in the preparation and use of financial statements who are drawn from public practice, business and academe. All members serve as individuals and not as representatives of their employers or organizations.

Individuals and organizations are invited to send written comments on the Exposure Draft proposals. Comments are requested from those who agree with the Exposure Draft as well as from those who do not.

Comments are most helpful if they are related to a specific paragraph or group of paragraphs, and, when expressing disagreement with the Exposure Draft, they clearly explain the problem, and include a suggested alternative supported by specific reasoning. All comments received will be available on the website at www.acsbcanada.org 10 days after the comment deadline, unless confidentiality is requested.

To be considered, comments to the AcSB must be received by July 31, 2009, addressed to:

**Peter Martin, CA
Director, Accounting Standards
Accounting Standards Board
277 Wellington Street West
Toronto, Ontario M5V 3H2**

For ease of handling, we prefer comments to be sent by e-mail (in Word format) to:
ed.accounting@cica.ca

“Standards need not be applied to immaterial items. While materiality is a matter of professional judgment in the particular circumstances, the Board believes that, as a general rule, materiality should be judged in relation to the significance of financial statement information to decision makers. An item of information, or an aggregate of items, is deemed to be material if it is probable that its omission or misstatement would influence or change a decision.”

(Introduction to Accounting Standards — CICA Handbook — Accounting)

Highlights

The Accounting Standards Board (AcSB) proposes, subject to comments received following exposure, to incorporate the final standard on income tax resulting from the exposure draft recently issued by the International Accounting Standards Board (IASB) into Canadian GAAP. The final standard will be part of the IFRSs to be adopted by publicly accountable enterprises in 2011. The proposed new standard would replace the income tax requirements in IAS 12, *Income Taxes*, SIC 21, “Income Taxes — Recovery of Revalued Non-Depreciable Assets,” and SIC-25, “Income Taxes — Changes in the Tax Status of an Enterprise or its Shareholders.”

Background

The AcSB’s strategy for publicly accountable enterprises is to adopt International Financial Reporting Standards (IFRSs) as Canadian GAAP for interim and annual financial statements related to fiscal years beginning on or after January 1, 2011.¹ The IASB has recently issued for comment its Exposure Draft, “Income Tax.” The AcSB intends to replace the income taxes requirements in IFRSs that were previously exposed in the April 2008 Exposure Draft, “Adopting IFRS in Canada,” with the revised IFRS on income tax.

The AcSB is developing a separate GAAP for private enterprises² that is expected to be completed before a final standard resulting from the IASB’s proposal on income tax is issued. In light of current work under way, the AcSB concluded that it will consider separately whether to adopt the new income tax standard for application by private enterprises. As the proposed standard might be applicable to private enterprises in the future, the AcSB encourages all entities to evaluate the proposals and provide comments.

IASB Exposure Draft

The IASB’s Exposure Draft, “[Income Tax](#)” is available on the IASB website.

Comparison of Income Tax ED to existing Canadian GAAP

The Income Tax Exposure Draft (the ED), IAS 12, US Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes*, and INCOME TAXES, Section 3465 of the CICA Handbook – Accounting, all share a common approach — the temporary difference approach. The objective of that approach is to recognize the income tax that would be payable or recoverable if an entity’s assets and liabilities were recovered or settled at their present carrying amount. However, the standards differ in a number of ways, including different exceptions to the temporary difference approach and differences relating to the recognition and measurement of deferred tax assets and liabilities, and the allocation of tax amounts to the components of comprehensive income and equity.

The proposed new standard is expected to improve financial reporting by clarifying various aspects of the requirements in IAS 12. It also eliminates a number of the

¹ The AcSB’s [Strategic Plan](#) and [Implementation Plan for Incorporating International Financial Reporting Standards into Canadian GAAP](#) are available on the AcSB’s website at www.acsbcanada.org.

² Additional information on the AcSB’s [strategy for Financial reporting by Private Enterprises](#) is available on the AcSB’s website at www.acsbcanada.org.

differences between the accounting for income tax under IFRSs and US GAAP. The FASB intends to issue the ED for comment and then decide whether to undertake a project that would eliminate the remaining differences in the accounting for income tax by adopting the IFRS.

The proposals in the ED apply to the accounting for all domestic and foreign taxes that are based on taxable profit. Income tax for a parent or an investor in an associate or joint venture also includes tax payable on distributions by the subsidiary on behalf of the parent, or by an associate or joint venture on behalf of the investor. The accounting for government grants and investment tax credits is excluded from the scope of the ED, but the accounting for temporary differences that arise from such grants or investment tax credits is included. The ED uses the terminology “deferred tax” rather than “future income tax”.

The principal differences between the proposals in the ED and existing Canadian GAAP include the following:

Scope

- Both the ED and Section 3465 exclude investment tax credits from their scope. The ED defines an investment tax credit as relating directly to the acquisition of depreciable assets while the existing Canadian GAAP definition includes all qualifying expenditures prescribed by tax legislation, whether or not they are made for depreciable assets.

Temporary differences

Exception from the temporary difference approach in Canadian GAAP that will be modified:

- The ED provides an exception from the temporary difference approach relating to a deferred tax asset or liability arising from an investment in a foreign subsidiary or joint venture that is essentially permanent in duration and it is apparent the temporary difference will not reverse in the foreseeable future. Section 3465 provides a similar exception for investments in all subsidiaries and interests in joint ventures.

Exceptions from the temporary difference approach in Canadian GAAP that will be removed:

- The ED does not provide an exception from the general requirement to recognize deferred tax amounts due to temporary differences arising:
 - from the difference between the historical exchange rate and the current exchange rate translations of the cost of non-monetary assets or liabilities of integrated foreign operations; and
 - in consolidated financial statements as a result of a difference between the tax basis of an asset in the purchaser’s tax jurisdiction and its cost recognized in the consolidated financial statements.
- The ED requires a deferred tax liability for temporary differences related to the liability component of a compound financial instrument to be recognized. Under Section 3465, when an enterprise is able to settle the instrument without the incidence of tax, no temporary difference is recognized.

Other changes to temporary differences:

- The ED requires assets and liabilities that have a tax basis different from their initial carrying amount to be disaggregated into an asset or liability excluding entity-specific tax effects and any entity-specific tax advantage or disadvantage.

The former would be recognized and measured in accordance with IFRSs and a deferred tax asset or liability would be recognized for the resulting temporary difference between the carrying amount and the tax basis available to the entity. If the consideration paid or received differs from the total recognized amounts of the acquired assets and liabilities (including deferred taxes), the difference is recognized as an allowance against, or premium on, the deferred tax asset or liability. Section 3465 uses a simultaneous equation method to determine the amounts to be recognized as assets and liabilities and future income taxes, which results in different amounts being recognized than the approach used in the ED.

Recognition and measurement

- The ED requires deferred tax assets to be recognized in full. However, the net carrying amount should equal the highest amount that is more likely than not to be realizable against taxable profit. A valuation allowance is established, if necessary, to record any difference between the full amount of the deferred tax asset and the net carrying amount. Section 3465 requires the recognition of a future income tax asset to the extent it is more likely than not to be realized and permits, but does not require, a separate valuation allowance. This difference is not expected to affect the net deferred tax asset recognized.
- The ED requires an acquirer to recognize its own pre-acquisition deferred tax asset against which a valuation allowance was provided if, as a result of a business combination, the deferred tax asset is considered more likely than not to be realized. The effect of the change is excluded from the accounting for the business combination. Therefore, recognition of such a deferred tax asset will not affect the determination of goodwill but will be recognized in income. Under Section 3465 an entity includes the future income tax asset when accounting for the business combination, which affects the amount of goodwill recognized.
- The ED requires current and deferred tax assets and liabilities to be measured using the probability-weighted average amount of all possible outcomes, assuming that the tax authorities will examine the amounts reported to them and have full knowledge of all relevant information. Section 3465 is silent on the treatment of uncertainty over tax amounts.
- The ED requires the use of average rates that are expected to apply to the expected taxable profit of the periods in which temporary differences are expected to reduce. Section 3465 is less specific.
- While both the ED and Section 3465 require the use of substantively enacted tax rates to measure income tax assets and liabilities, the ED includes more general guidance on when tax rates are substantively enacted and does not include guidance specific to Canadian legislative processes.

Other changes

- The ED specifically addresses deferred taxes resulting from share based payment transactions. Existing Canadian GAAP does not specifically address the future income tax effect of stock-based compensation and similar arrangements.
- The ED does not include guidance specific to the accounting for flow-through shares. Existing Canadian GAAP includes such guidance.

Presentation and disclosure

- The ED includes several presentation and disclosure requirements that differ from existing Canadian GAAP.

Timing of adoption in Canada

While the IASB has not yet determined the effective date of the proposed new IFRS, it currently expects to issue it in final form some time in 2010. Assuming this timetable is met, the AcSB intends to incorporate the new standard into Canadian GAAP as part of the IFRSs to be adopted by publicly accountable enterprises in 2011.

The IASB intends to permit first-time adopters of IFRSs with a transition date prior to the date the new IFRS is issued to apply the new IFRS to all periods presented in the year of adoption of IFRSs. This would allow Canadian entities that adopt IFRSs in 2011 to apply the new IFRS in preparing comparative financial information for 2010 rather than applying IAS 12 for that purpose.

Other material

The IASB has also published a Basis for Conclusions, a Draft Flow Chart and Illustrative Examples related to the proposed new standard. Although these documents are not part of the AcSB's Exposure Draft, constituents may wish to refer to them.

Comments requested

The AcSB encourages Canadian stakeholders to respond to the IASB on the ED since the proposed new IFRS will become part of Canadian GAAP for publicly accountable enterprises when finalized, and might also be applicable to private enterprises. Specific questions on which the IASB would like input are provided in the Invitation to Comment in the ED. The AcSB requests that comment letters be sent directly to the IASB with a copy to the AcSB.

The AcSB has identified additional questions regarding the proposed new standard on which it would like input from Canadian respondents.

1. The proposed new standard has been developed by the IASB for application by entities around the world. Assuming the ED proposals are approved by the IASB, do you believe that there are aspects of the proposed new standard that make some or all of it inappropriate for Canadian entities, even though it is appropriate for entities in the rest of the world? If so, please specify which aspects and what circumstances make the accounting requirements proposed in the ED inappropriate for Canadian entities.
2. The AcSB has determined that it will generally not issue application or interpretative guidance on IASB standards. An exception might be when an aspect of a standard needs interpreting in light of specific Canadian legal, tax, regulatory or other circumstances that do not apply in other countries and that therefore will not be addressed by the IASB. Do the proposals in the ED require such application or interpretative guidance? If so, please specify the issue giving rise to the need for additional material, and the nature of the material needed.
3. The AcSB expects to have developed a separate set of GAAP standards for private enterprises before the proposed new income taxes standard is issued, but concluded that it will consider, separately, whether to adopt the ED proposals in that set of standards. Therefore, it will be important for the AcSB to know

stakeholders' views on the matter. Are the proposals in the ED appropriate for Canadian private enterprises? If not, please specify why not.

Responses to these additional questions should be sent directly to the AcSB.

The deadline for commenting to the IASB on the ED and the deadline for responding to the AcSB on the additional questions set out above is July 31, 2009.