Global minimum top-up tax

Relief from deferred tax accounting under IFRS® Accounting Standards

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Get ready for global minimum top-up tax

What's the issue?

To address concerns about uneven profit distribution and the tax challenges of the digitalised economy, various agreements have been reached globally. Many countries are now busy amending their local laws to introduce a global minimum top-up tax.

Implementing the new rules and determining their tax and accounting impacts may be challenging.

Stakeholders raised significant concerns about deferred tax accounting in relation to the new top-up tax under IFRS Accounting Standards. In response, the International Accounting Standards Board (IASB) **has amended IAS 12 *Income Taxes*.**

What's the impact?

The amendments to IAS 12 introduce a **temporary mandatory exception from accounting for deferred tax** related to top-up tax.

However, companies are required to provide **new disclosures** about their exposure to the top-up tax at the reporting date, particularly before the new tax rules come into effect.

What's next?

- Monitor the implementation of global anti-base erosion (GloBE) model rules into relevant jurisdictions' tax laws.
- Assess the potential impacts of the new tax rules.
- Engage with your users and determine which disclosures to provide.
- Collect appropriate information to provide the new disclosures about your potential exposure.

Relief from deferred tax accounting

Our guide explores the amendments to IAS 12 and will help you get ready to provide the new disclosures.

01 What is the global minimum top-up tax?

In October 2021, more than 135 jurisdictions – representing more than 90 percent of global GDP – agreed to a major international tax reform. This reform involves a two-pillar[1] solution.

There are four mechanisms under **Pillar Two** (referred to as a ‘global minimum top-up tax’ or ‘top-up tax’) that countries can adopt.

It is up to individual countries to decide how to implement Pillar Two using one or more of the four mechanisms.

Many jurisdictions are expected to enact changes to tax laws in 2023, with changes coming into effect from 2024.

[1] Pillar One aims to ensure a fairer distribution of profits and taxing rights among countries. Pillar Two aims to ensure that large multinational groups pay at least the minimum rate of 15 percent on income arising in each jurisdiction in which they operate.

In our view, **all** Pillar Two top-up taxes levied by tax authorities – i.e. IIR, UTPR and domestic minimum tax – are generally income taxes in the scope of IAS 12. This applies for **all financial statements**, including the consolidated financial statements of the ultimate parent company, separate financial statements of group companies and consolidated financial statements of a subgroup.

Pillar Two mechanisms

Subject to tax rule*

Payer collects top-up tax if recipient is not adequately taxed (<9%)

Domestic minimum tax

Local jurisdiction domestic minimum tax (based on the GloBE rules)

Income inclusion rule (IIR)**

Jurisdiction of ultimate parent generally collects top-up tax if overseas group companies are not adequately taxed (<15%)

Undertaxed payment rule (UTPR)**

Deductions denied or additional tax charged if ultimate parent does not collect top-up tax under IIR

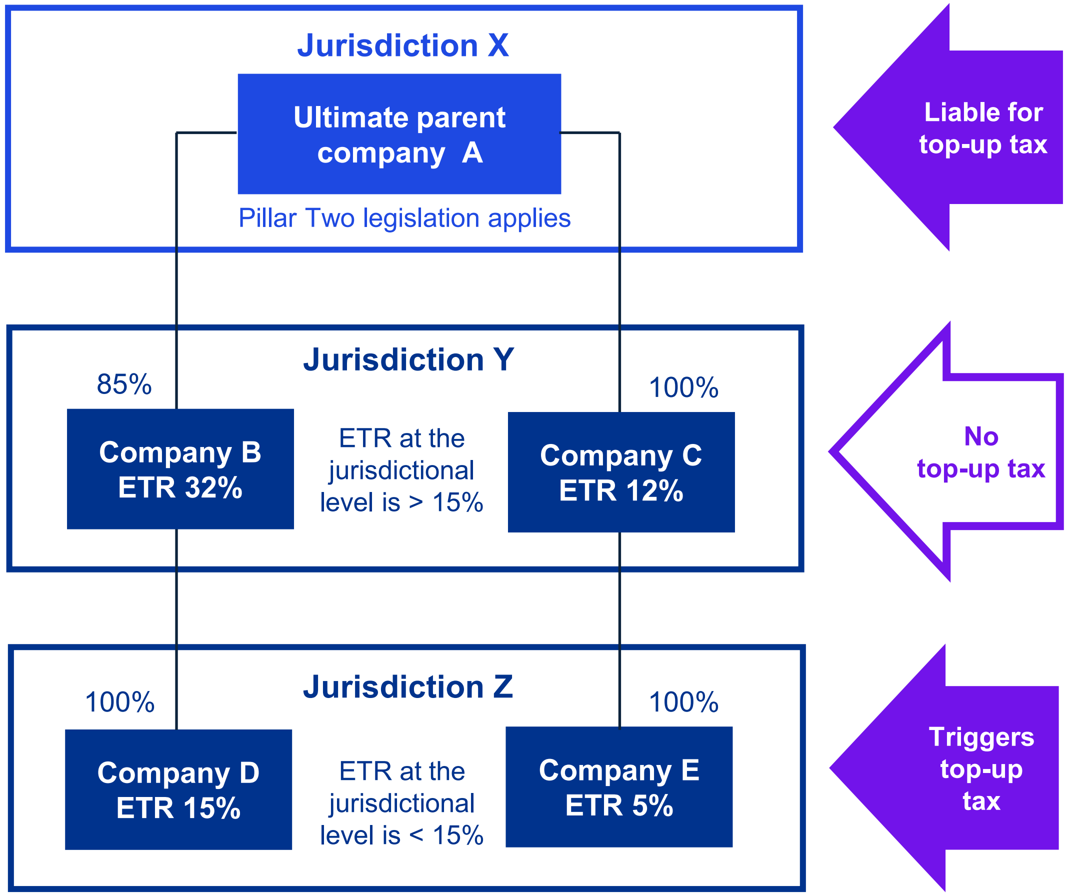
* In development

** Part of the GloBE rules

02 Who needs to pay it?

Pillar Two rules apply to multinational groups that have **consolidated revenues of EUR 750 million** or more in at least two of the last four years.

These groups will be required to calculate their effective tax rate (ETR) for each jurisdiction in which they operate under the GloBE rules. When this is **below the 15 percent minimum rate**, the group will be liable to pay a top-up tax for the difference.



In many cases, the group company liable for the top-up tax will differ from the group company that triggered it.

Typically the **ultimate parent** will be liable to pay top-up tax for its low-taxed subsidiaries and the parent's local tax authority will have a right to collect it. However, an intermediate parent or other group company can be liable for all or part of the top-up tax in some circumstances.

03 How is it calculated?

The company liable for the top-up tax will need to do the following.

1. **Determine qualifying (covered) taxes** for all group companies in the same jurisdiction.
2. **Determine the GloBE income** for all group companies in the same jurisdiction using the same accounting framework as the consolidated financial statements – e.g. US GAAP or IFRS Accounting Standards.
3. **Calculate the ETR** by dividing qualifying (covered) taxes by GloBE income.

If the ETR is less than 15 percent, then:

4. **Determine excess profit** as GloBE income minus qualifying deductions.
5. **Determine the top-up tax rate**, which is the minimum 15 percent rate minus the **ETR**.
6. **Calculate the top-up tax** by multiplying the excess profit by the top-up tax rate.

$$\frac{\textbf{Qualifying taxes}\ \text{(Step 1)}}{\textbf{GloBE income}\ \text{(Step 2)}} = \textbf{ETR}\ \text{(Step 3)}$$

If the ETR is less than 15%, then:

$$\textbf{Excess profit}\ \text{(Step 4)} \times \textbf{Top-up tax rate}\ \text{(Step 5)} = \textbf{Top-up tax}\ \text{(Step 6)}$$

The accounting framework will impact the amount of the top-up tax.

In addition, the ETR calculation differs under the GloBE rules and IAS 12.

04 Does it trigger deferred tax impacts and is there a relief?

Top-up tax differs from income taxes that arise under ‘traditional’ tax regimes. This has led to questions from stakeholders, particularly about the accounting for **deferred tax impacts** under IFRS Accounting Standards, including the following.

- What is the **tax base** of assets and liabilities for the purposes of the GloBE rules?
- Do the GloBE rules create **additional** temporary differences?
- Does a company need to **remeasure** its existing temporary differences in relation to deferred tax recognised?
- How will companies determine the **rate** for measuring the deferred tax impacts of top-up tax?

In response, the IASB has amended IAS 12 to provide a temporary relief.

IASB’s relief

Amendment to IAS 12

Temporary mandatory relief from accounting for deferred tax related to top-up tax.

The timing of the relief is critical. An entire group may be impacted as soon as a single jurisdiction in which it operates enacts or substantively enacts changes to its tax laws. Because many jurisdictions are expected to enact changes to tax laws in 2023, it is important that the relief is available beforehand.

05 When and how does the deferred tax relief apply?

23 May 2023

Amendments released.

The relief is effective **immediately** and applies **retrospectively** in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors.*

30 June 2023*

Companies provide the new disclosures on applying the relief.

Other disclosures are not required in interim periods ending on or before 31 December 2023.

31 December 2023*

The disclosures about the top-up tax exposure (in addition to those on applying the relief) apply for the financial statements of **calendar year companies**.

31 March 2024*

The disclosures about the top-up tax exposure (in addition to those on applying the relief) apply for financial statements of **non-calendar year companies**.

*The first date from which the new disclosure requirements apply

The relief is relevant only if changes to tax laws are enacted or substantively enacted. Pillar Two tax laws are complex and may require the release of **multiple pieces** of legislation **over a period of time**.

Judgement will be required to determine whether a specific piece of legislation results in enactment or substantive enactment of a tax law.

06 What disclosures does a company provide before and after top-up tax applies?

The new disclosure requirements (other than the disclosure on applying the relief) apply from **31 December 2023**. Companies are not required to provide the new disclosures in interim periods ending on or before 31 December 2023. However, **investors may expect disclosures** about the potential impacts **before** then, particularly from group companies that expect to be liable for the top-up tax.

Once tax law is enacted but before top-up tax applies

- Companies need to provide information that is known or can be reasonably estimated and helps users of the financial statements to understand the company's **exposure** to Pillar Two income taxes **at the reporting date**.
- Information does not need to reflect all of the specific requirements in the legislation and can be provided as an indicative range.
  - ***Qualitative information:*** How the company is affected by Pillar Two taxes and in which jurisdictions the exposure arises – e.g. where the top-up tax is triggered and where it will need to be paid.
  - ***Quantitative information:*** The proportion of profits that may be subject to Pillar Two income taxes and the average ETR applicable to those profits, or how the average ETR would have changed if Pillar Two legislation had been effective.
- If information is not known or cannot be reasonably estimated at the reporting date, then a company discloses a statement to that effect and information about its progress in assessing the Pillar Two exposure.

After top-up tax applies

- **Current tax expense** related to top-up tax.

In the separate financial statements, do the disclosures focus on the group's or the company's own exposure?

In a nutshell – the company's own exposure.

In our view, in determining which disclosures to provide, a company should consider the information relevant to the users of a specific set of financial statements to understand the company's potential exposure as a result of the Pillar Two tax laws.

For example, information about an individual company's exposure may be relevant if it expects to be liable for, or to trigger, top-up tax.

07 What are your next steps?

01 Monitor the changes to tax laws

- Monitor the implementation of GloBE model rules into relevant jurisdictions' tax laws.

02 Assess the impacts of GloBE model rules

- Engage with tax specialists to assess the impacts.
- Determine whether the group may potentially be subject to the top-up tax.

03 Determine which disclosures to provide

- Engage with your users to determine which disclosures to provide at 31 December 2023 and which disclosures may be relevant in interim periods before that date.

04 Get ready to provide the new disclosures

- Collect appropriate information to provide the new disclosures about your potential exposure.

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