Amendments to HKAS 12 - Recognition of Deferred Tax Assets for Unrealised Losses

Introduction

The IFRS Interpretations Committee was asked to provide guidance on how to determine, in accordance with IAS 12 "Income Taxes", whether to recognise a deferred tax asset in relation to a debt instrument that is classified as an available-for-sale financial asset in accordance with IAS 39 "Financial Instruments: Recognition and Measurement". Practice differs because of divergent views on the recognition of deferred tax assets.

The Amendments to HKAS 12, following the IASB's equivalent amendments to IAS 12, clarify how to account for deferred tax assets related to debt instruments measured at fair value.

Effective Date

An entity shall apply the Amendments retrospectively for annual periods beginning on or after 1 January 2017. Earlier application is permitted. On initial application of the Amendments, the change in the opening equity of the earliest comparative period may be recognised in opening retained earnings (or in another component of equity, as appropriate), without allocating the change between opening retained earnings and other components of equity.

Summary of Amendments

01

Existence of a deductible temporary difference

HKAS 12 states that certain assets may be carried at fair value, or may be revalued, without an equivalent adjustment being made for tax purposes. A deductible temporary difference arises if the tax base of an asset exceeds its carrying amount. The Amendments add an example to illustrate the identification of a deductible temporary difference in the case of a fixed-rate debt instrument measured at fair value for which the principal is paid on maturity.

The example shows that the difference between the carrying amount of the asset measured at fair value and its higher tax base gives rise to a deductible temporary difference. The existence of the deductible temporary difference depends solely on a comparison of the carrying amount of the asset and its tax base at the end of the reporting period, and is not affected by possible future changes in the carrying amount. This applies irrespective of whether the debt instrument's holder expects to recover the carrying amount of the debt instrument by sale or by continuing to hold it, or whether it is probable that the principal will be recovered.

02

Recovering an asset for more than its carrying amount

Determining temporary differences and estimating probable future taxable profit against which deductible temporary differences are utilised are two separate steps. The carrying amount of an asset does not limit the estimation of probable future taxable profit. In the estimate of probable future taxable profit, an entity includes the probable inflow of taxable economic benefits that results from recovering the asset. This probable inflow of taxable economic benefits may exceed the carrying amount of the asset. However, sufficient evidence is required to base the estimate of probable future taxable profit.

The Amendments add a guidance to state that the estimate of probable future taxable profit may include the recovery of some of an entity's assets for more than their carrying amount if there is sufficient evidence that it is probable that the entity will achieve this.

03

Determining future taxable profit

Deductible temporary differences are utilised by deduction against taxable profit, excluding deductions arising from reversal of those deductible temporary differences. Taxable profit used for assessing the utilisation of deductible temporary differences is different from taxable profit on which income taxes are payable. If those deductions were not excluded, then they would be counted twice.

The Amendments add a guidance to state that in evaluating whether there will be sufficient taxable profit in future periods to utilise the deductible temporary differences, an entity shall compare the deductible temporary differences with future taxable profit that excludes tax deductions resulting from the reversal of those deductible temporary differences.

04

Combined versus separate assessment

Deferred tax assets are recognised only to the extent of probable future taxable profit against which the deductible temporary differences can be utilised. The deductible temporary differences are utilised when their reversal results in deductions that are offset against taxable profits of future periods.

The Amendments add a guidance to state that when an entity assesses whether taxable profits will be available against which it can utilise a deductible temporary difference, it considers whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. If tax law imposes no such restrictions, an entity assesses a deductible temporary difference in combination with all of its other deductible temporary differences. However, if tax law restricts the utilisation of losses to deduction against income of a specific type, a deductible temporary difference is assessed in combination only with other deductible temporary differences of the appropriate type.

Finally the Amendments add an example to illustrate the utilisation of deductible temporary differences because of the reversal of taxable temporary differences and future taxable profit.

CONTACT US

HONG KONG OFFICE
Unit 701-3 & 8, Citicorp Centre, 18 Whitfield Road, Causeway Bay, Hong Kong
Tel: (852) 2155 8288 | Fax: (852) 2564 2297

Email: info@zhcpa.hk | Web: www.zhcpa.hk www.zhtraining.com

If you have any comments or require further information, please feel free to contact:

Mr. Joel Chan
Quality Assurance Partner
ZHONGHUI ANDA CPA Limited
Email: joel.chan@zhcpa.hk

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