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Ind AS- 12
Income Taxes

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Introduction

- What is Income Tax (General Term)?
- The term **income tax** refers to a type of tax that governments impose on income generated by businesses and individuals within their jurisdiction.

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Scope & Objective

Ques. What is Income tax for the purpose of Ind AS-12?

Ans. Income tax for the purpose of this standard includes:

1. Income taxes include all domestic and foreign taxes which are based on taxable profits.
2. Also include taxes, such as withholding taxes, which are payable by a subsidiary, associate or joint arrangement on distributions to the reporting entity.

<u>OBJECTIVE:</u> To prescribe accounting treatment for Income tax.

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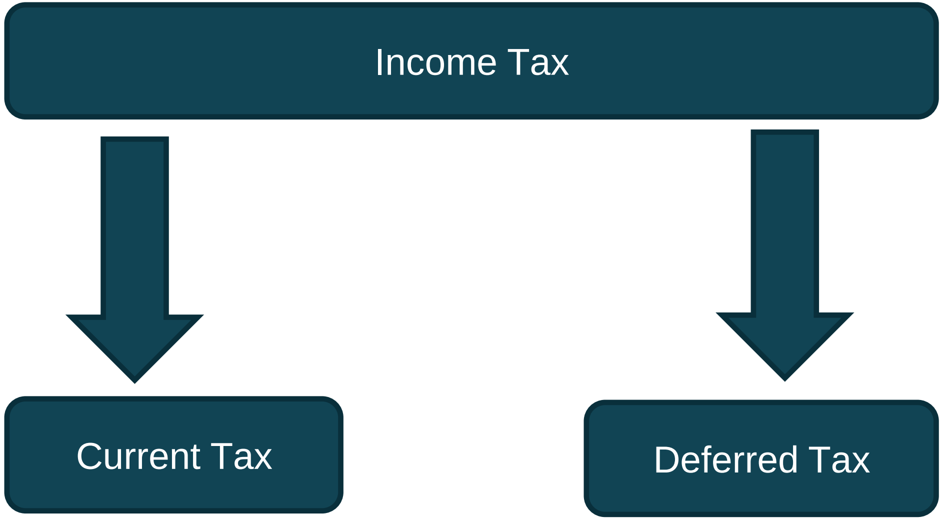
Continuation

Further, the Income tax for the purpose of this Standard could be classified as:



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Important Definitions

1. Accounting profit is profit or loss for a period before deducting tax expense.

2. Taxable profit (tax loss) is the profit (loss) for a period, determined in accordance with the rules established by the taxation authorities, upon which income taxes are payable (recoverable).

3. Tax expense (tax income) is the aggregate amount included in the determination of profit or loss for the period in respect of current tax and deferred tax.

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Important Definitions

4. Temporary differences are differences between the carrying amount of an asset or liability in the balance sheet and its tax base.

Temporary differences may be either:

(a) Taxable temporary differences (Results in DTL), are temporary differences that will result in taxable amounts in determining taxable profits of future periods. It arises DTL.

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Continuation

(b) Deductible temporary differences (Results in DTA), are temporary differences that will result in amounts that are deductible in determining taxable profits of future periods. It results in DTA.

Continuation

Current Tax: Is the amount of income taxes payable (recoverable) in respect of the taxable profit (tax loss) for a period.

Current Tax

Current tax Liability: Current tax for current and prior periods shall, to the extent unpaid, be recognised as a liability.

Current tax asset: If the amount already paid in respect of current and prior periods exceeds the amount due for those periods, the excess shall be recognised as an asset.

Continuation

Deferred Tax

Deferred Tax Liabilities: Are the amounts of income taxes payable in future periods in respect of taxable temporary differences.

Deferred Tax Assets: are the amounts of income taxes recoverable in future periods in respect of: (a) deductible temporary differences; (b) the carry forward of unused tax losses; and (c) the carry forward of unused tax credits.

When DTL is created?

The most common areas of taxable temporary differences giving rise to deferred tax liabilities are:

1. Timing differences – Timing difference arises when the recognition of certain item in the financial statements occurs in a different time than its recognition in tax return.

Continuation

2. **Business combinations** – In a business combination identifiable Assets and Liabilities can be revalued Upwards to Fair Value at the acquisition date, but no adjustment is made for Tax Purposes. As a result, Taxable Temporary Difference will arise.

3. **Assets carried at fair value** – When a company applies policy of revaluation (for example, revaluation model for property, plant and equipment in line with INDAS 16, 38, 116) and some assets are revalued upwards to their fair value, taxable temporary difference will arise through Revaluation Surplus (OCI)

When DTA is created?

The most common areas of deductible temporary differences giving rise to deferred tax liabilities are:

1. **Timing differences** – Timing difference arises when the recognition of certain item in the financial statements occurs in a different time than its recognition in tax return, for example, accrued expenses are tax deductible only when paid.

Continuation

2. <u>Business combinations</u> – In a business combination identifiable assets and liabilities can be revalued downwards to fair value at the acquisition date, but no adjustment is made for tax purposes. As a result, deductible temporary difference arises.

3. <u>Assets carried at fair value</u> – When a company applies policy of revaluation (for example, revaluation model for property, plant and equipment in line with Ind AS 16, 38, 116) and some assets are revalued downwards to their fair value, deductible temporary difference arises through P&L.

Exceptions

In almost all situations you would recognize deferred tax as an income or an expense in profit or loss for the period. There are just 2 exceptions of this rule:

1. An item of current tax or deferred tax pertaining to other comprehensive income should be recognized in other comprehensive income or directly in equity)
2. An item of current tax or deferred tax pertaining to Direct Equity should be directly in equity.

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Classification of Temporary Difference with the help of Matrix:

	For Assets	For Liabilities
If carrying amount > tax base	Taxable Temporary Difference ↓ Deferred Tax Liability (e.g. WDV as per books > WDV as per Income Tax)	Deductible Temporary Difference ↓ Deferred Tax Asset (e.g. Provision for Bonus as per books > Provision for Bonus as per IT)
If carrying amount < tax base	Deductible Temporary Difference ↓ Deferred Tax Asset (e.g. WDV as per books < WDV as per Income Tax)	Taxable Temporary Difference ↓ Deferred Tax Liability (e.g. Loan carrying amount as per books< Loan carrying amounts as per tax)
If carrying amount = tax base	No temporary difference	No temporary difference

Example of Taxable temporary difference (DTL)

An entity has acquired an asset for Rs 10,000. The depreciation as per Income tax is 40% on WDV Basis. In books of accounts, entity claims depreciation on SLM basis @ 16.21%. The profit before depreciation is Rs 20,000. Tax rate is 30%. Compute the amount of DTL or DTA.

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Continuation

Particulars	As per Income Tax	As per Books
PBDT	20,000	20,000
- DEP	(4000)	(1,621)
PBT	16,000	18,379
- TAX @ 30%	(4,800)	(5,514)
PAT	11,200	12,865

Tax Base= 10,000-4000= 6,000
Carrying Value= 10,000-1,621= 8,379
Temporary Difference= 2,379 (8,379-6,000)
DTL= 714 (2,379*30%)

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Tax Base: Tax base of an asset or liability is the amount attributed to that asset or liability for tax purposes.

The tax base of an asset is the amount that will be deductible for tax purposes against any taxable economic benefits that will flow to an entity when it recovers the carrying amount of the asset. If those economic benefits will not be taxable, the tax base of the asset is equal to its carrying amount.

The tax base of a liability is its carrying amount, less any amount that will be deductible for tax purposes in respect of that liability in future periods. In the case of revenue which is received in advance, the tax base of the resulting liability is its carrying amount, less any amount of the revenue that will not be taxable in future periods.

Example of Tax base (Asset)

A machine cost Rs. 100. For tax purposes, depreciation of Rs. 30 has already been deducted in the current and prior periods and the remaining cost will be deductible in future periods, either as depreciation or through a deduction on disposal. Revenue generated by using the machine is taxable, any gain on disposal of the machine will be taxable and any loss on disposal will be deductible for tax purposes. The tax base of the machine is Rs. 70.

Example of Tax base (Liabilities)

Current liabilities include accrued expenses with a carrying amount of Rs. 100. The related expense will be deducted for tax purposes on a cash basis. The tax base of the accrued expenses is nil.

Current liabilities include interest revenue received in advance, with a carrying amount of Rs. 100. The related expense will be deducted for tax purposes on a cash basis. The tax base of the accrued expenses is nil.

Deferred Tax- Its recognisation, measurement & presentation

STEPS

1. Compute carrying amount of A&L
2. Compute Tax Base
3. Compute Temporary Difference
4. Classify it into: Taxable or Deductible temporary difference
5. Identify Exceptions
6. Assess deductible temporary differences, tax loss & tax credit and determine tax rate
7. Calculate & Recognize Deferred Tax
8. Accounting of Deferred Tax
9. Offsetting DTA & DTL

Step 1

Calculate Carrying Amount

Example: An entity has acquired P&M as on 1st April 2021 for Rs 1,00,000. It is depreciated @10% on SLM Basis. For the year ended 31st March, 2022 it provides depreciation for Rs 10,000.

The carrying amount of an asset is Rs 90,000 (1,00,000-10,000)

Step 2

Compute Tax Base

Example: An entity has acquired P&M as on 1st April 2021 for Rs 1,00,000. It is depreciated @10% on SLM Basis. For the year ended 31st March, 2022 it provides depreciation for Rs 10,000.

As per income tax P&M is depreciated @30%p.a on WDV Basis. It would provide depreciation for Rs 30,000.

Thus the tax base of this item is Rs 70,000 (1,00,000-30,000)

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Step 3

Compute Temporary Difference

Value of P&M as per Books: 90,000 (Step 1)

Value of P&M as per IT Act: 70,000 (Step 2)

Temporary Difference is Rs 20,000 (90,000-70,000)

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Step 4

Classify into Taxable or Deductible Temporary Difference

When Carrying amount of an asset is more Tax Base= Taxable Temporary Difference.

Example: Carrying amount (90,000) > (70,000)

Thus, it is the case of Taxable Temporary Difference

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Step 5

Determine Tax Rate

Taxable temporary difference when multiplied with tax rate will result in DTL

Deductible temporary difference when multiplied with tax rate will result in DTA

Example: Tax rate is 30%

DTL= 6000 (20,000*30%)

Step 6

Disclosure: Accounting of Deferred Tax

Accounting entry:

Profit & Loss Account.........Dr 6,000

To DTL 6,000

DTA............................Dr

Profit & Loss Account.........Dr

Offsetting CTA & CTL

An entity shall offset current tax assets and current tax liabilities if, and only if, the entity:

(a) has a legally enforceable right to set off the recognized amounts; and

(b) intends either to settle on a net basis, or to realize the asset and settle the liability simultaneously.

Offsetting DTA & DTL

An entity shall offset deferred tax assets and deferred tax liabilities if, and only if:

(a) the entity has a legally enforceable right to set off current tax assets against current tax liabilities; and

(b) the deferred tax assets and the deferred tax liabilities relate to income taxes levied by the same taxation authority.

Exceptions

Exception 1 The initial reconginisation of goodwill in case of Business Combination

No DTL is recognised for taxable temporary differences arising on **Goodwill** arising on Business Combination in tax jurisdiction where such **goodwill is not deductible.**

In all other cases of Temporary differences either taxable or deferred, either DTL or DTA should be recognised in accordance with other provision of Ind AS.

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Example

An entity acquires a subsidiary and pays Rs. 1,00,000. The fair value of net identifiable assets is Rs. 65,000.

The following entry shall be made in the books:

Entry 1: Goodwill Dr. 35,000

Net Assets Dr. 65,000

To Consideration 1,00,000

The tax base of goodwill is Rs Nil. Hence the difference is Rs. 35,000. Assuming tax rate to be 30%, deferred tax liability of Rs. 10,500 needs to be created.

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Now because of recognition of this deferred tax liability, the following entry needs to be passed instead of the above entry:
Entry 2: Goodwill Dr. 45,500

Net assets Dr. 65,000

To Consideration 1,00,000

To Deferred tax liability 10,500

The difference now is Rs. 45,500 and not Rs. 35,000 and the resultant deferred tax liability should be Rs. 13,650 (45,500 x 30%) and not Rs. 10,500.

Continuation

- Thus, deferred tax liability in entry 2 should be increased by Rs. 3,150 which in turn will increase goodwill by a similar amount with consequent impact on taxable temporary difference and deferred tax liability. The circle goes on. Therefore, no deferred tax liability is to be recognised in the case of differences arising on the initial recognition of goodwill in a business combination in tax jurisdiction where such goodwill is not tax deductible

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Exceptions

Exception 2 The initial recognition of Asset or Liability in a transaction which either: 1. is not a Business Combination and 2. At the time of transactions neither affects accounting profit nor taxable profit (tax loss)

No deferred tax liability shall be recognized from initial recognition of any Asset or Liability in a transaction other than a Business Combination and at the time of the transaction it affects neither Accounting nor Taxable profit (loss). In this situation Tax Base will be assumed to be equal to the Carrying Amount.

Example

Entity A acquires a foreign made vehicle for Rs 1,00,000 directly from the vehicle manufacturer. The transaction is not a part of any business combination. The tax laws do not permit any depreciation thereon. Also, any profits at the time of sale are not taxable or losses are not tax deductible. This vehicle thus has a tax base of Rs Nil. There is a taxable temporary difference of Rs 1,00,000. Assuming a tax rate of 30%, the entity should create a deferred tax liability of Rs 30,000. But the Standard does not permit. Since it is a permanent difference and will never be reversed, hence we assumed the Tax Base as 1,00,000 so that difference should not arise

Difference between Ind AS-12 and AS-22

Particulars	Ind AS 12	AS 22
Approach for creating Deferred Tax	Ind AS 12 is based on balance sheet approach. It requires recognition of tax consequences of differences between the carrying amounts of assets and liabilities and their tax base.	AS 22 is based on income statement approach. It requires recognition of tax consequences of differences between taxable income and accounting income. For this purpose, differences between taxable income and accounting income are classified into permanent and timing differences.

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Recognition of Current and Deferred Tax	As per Ind AS 12, current and deferred tax are recognised as income or an expense and included in profit or loss for the period, except to the extent that	AS 22 does not specifically deal with this aspect.
	the tax arises from a transaction or event which is recognised outside profit or loss, either in other comprehensive income or directly in equity, in those cases tax is also recognised in other comprehensive income or in equity, as appropriate.	

Changes in Entities Tax Status or that of its Shareholders	Ind AS 12 provides guidance as to how an entity should account for the tax consequences of a change in its tax status or that of its shareholders.	AS 22 does not deal with this aspect.
Virtual Certainty	Since the concept of virtual certainty does not exist in Ind AS 12, this explanation is not included.	AS 22 explains virtual certainty supported by convincing evidence.
Guidance for Recognition of Deferred Tax in a Tax Holiday Period	Ind AS 12 does not specifically deal with these situations.	AS 22 specifically provides guidance regarding recognition of deferred tax in the situations of Tax Holiday under Sections 80-IA and 80-IB and Tax Holiday under Sections 10A and 10B of the Income Tax Act, 1961. Similarly, AS 22 provides guidance regarding recognition of deferred tax asset in case of loss under the head 'capital gains'

Disclosure

1. Components of TAX Expenses
2. Any Current Tax or Deferred Tax directly Charged to Equity/OCI (other than P&L)
3. Any Current Tax or Deferred Tax recognized in OCI (other than P&L)
4. A numerical Reconciliation between Tax Expense and the product of accounting profit multiplied by applicable tax rate.

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Example of Effective Tax Rate

An entity has made an accounting profit of Rs 1,00,000. The tax rate is 30%. In computing the accounting profit, a penalty of Rs 10,000 has been considered which is not tax deductible.

There are no other tax impacts. In this case, the taxable profits are Rs1,10,000 (Rs1,00,000 + Rs10,000) and tax expense @ 30% is Rs33,000.

Example of Effective Tax Rate

The two types of disclosures are as under:

Particulars	Amount (In Rs)
Accounting profit	1,00,000
Tax at the applicable tax rate of 30%	30,000
Tax effect of expenses that are not deductible in determining taxable profits:-	3,000
Penalties Tax expense	33,000

Example of Effective Tax Rate

The two types of disclosures are The effective tax rate is as per the national income-tax rate.

Particulars	%
Applicable tax rate	30
Tax effect of expenses that are not deductible in determining taxable profits:- Penalties	3
Average effective tax rate	33

The effective tax rate is as per the national income-tax rate.

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Thank You!!

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