European Securities and Markets Authority

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PUBLIC STATEMENT

Accounting for Income Tax consequences of the United States Tax Cuts and Jobs Act under IFRS[1]

1. The United States Tax Cuts and Jobs Act (hereinafter 'the Act') was signed into law on 22 December 2017 and introduces significant changes in US tax laws taking effect on 1 January 2018. The European Securities and Markets Authority (ESMA) has become aware of concerns expressed by EU issuers (whether Foreign Private Issuers in the US (FPIs)[2] or any issuers having material subsidiaries in the US) with respect to the accounting for the effects of the Act in their IFRS financial statements. Particularly, some EU issuers and their auditors have expressed concerns with respect to their ability to complete fully the accounting under IAS *12 Income Taxes* for the effects of the Act in their 2017 annual financial statements due to the short time available to assess the accounting consequences of the Act and the lack of information on their tax position.

2. Therefore, in order to avoid the risk of inconsistent application of IFRS in the European Union, ESMA decided to publish this Public Statement to provide clarifications on accounting for the income tax consequences of the Act under IFRS. ESMA notes that, according to paragraphs 46 and 47 of IAS 12, current and deferred tax assets and liabilities shall be measured based on tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period. ESMA highlights that under IFRS there is no relief from these requirements, even to deal with circumstances in which complex legislation is substantively enacted shortly before the year-end.

3. Consequently, in ESMA's view, for reporting periods that include 22 December 2017, IAS 12 requires issuers that are affected by changes in US tax legislation introduced by the Act to measure current and deferred taxes based on the newly enacted tax law. Furthermore, ESMA reminds issuers that paragraph 61A of IAS 12 requires recognition of current and deferred tax outside profit or loss if the tax relates to items that are recognised, in the same or a different period, outside profit or loss (backward tracing).

4. ESMA acknowledges that a complete understanding of the implications of the Act may take some time. For example, application questions related to the provisions of the Act to the specific circumstances of the issuer may arise or be answered only in subsequent periods. ESMA expects EU issuers to be able to make a reasonable estimate of the impact of the material aspects of the Act on their current and deferred tax

[1] The Act amends the US Internal Revenue Code to reduce tax rates and modify policies, credits, and deductions for individuals and businesses and was signed into law as "An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018". The Act can be found here: https://www.congress.gov/115/bills/hr1/BILLS-115hr1enr.pdf

[2] In response to the concerns raised by US issuers, the US Securities and Exchange Commission (SEC) has issued Staff Accounting Bulletin no. 118 (SAB 118) to provide clarification to address any uncertainty and diversity in practice that may arise in accounting for the effects of the Act in accordance with US GAAP and specifically ASC Topic 740 and giving issuers some relief from reflecting the effects of the Act in their 2017 financial statements. Footnote 6 in SAB 118 explains that SEC staff would not object to FPIs reporting under IFRS to follow the SAB 118 when accounting for the effects of the Act in their financial statements filed with the SEC. (https://www.sec.gov/interps/account/staff-accounting-bulletin-118.htm)

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assets and/or liabilities in their 2017 annual financial statements in line with the deadlines set out in Article 4 of the Transparency Directive, as transposed by the national law. ESMA acknowledges that these reported amounts may be subject to a higher degree of estimation uncertainty than usually the case and that measurement adjustments may need to be made in subsequent reporting periods as issuers get more accurate information on the impact of the Act and the modalities of its application.

5. ESMA highlights the need for transparent and informative disclosure both in relation to the amounts reported in the 2017 annual financial statements and on their subsequent re-measurement. ESMA draws attention to the disclosure requirements of paragraphs 80(d) and 81(d) of IAS 12, requiring disclosure of the amount of deferred tax expense/(income) relating to changes in tax rates or the imposition of new taxes and the explanation of changes in the applicable tax rate(s) compared to the previous accounting period.

6. ESMA also expects that, where material tax assets and/or liabilities are subject to increased estimation uncertainty, issuers give additional consideration to their entity-specific disclosure on those estimates and the judgements they have made in their determination, as well as the nature and sources of estimation uncertainty in line with paragraphs 122 and 125-129 of IAS 1 *Presentation of Financial Statements*. ESMA expects the level of disclosures provided to reflect the complexity of the estimate and the degree of the estimation uncertainty. ESMA stresses that any disclosures in accordance with IAS 1 or IAS 12 do not replace disclosure obligations of issuers under other EU legislation such as the Market Abuse Regulation, with regard to inside information.

7. Furthermore, taking into account the fact that new information on application of the Act to the specific circumstances of the issuer might become available only progressively, ESMA expects that, in line with paragraph 5 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, such adjustments in subsequent periods would in most cases constitute a change in accounting estimate where they result from a reassessment of the future expected benefits and obligations associated with the tax assets or liabilities. This is the case, if an issuer had used all information it reasonably could have been expected to obtain for its prior period estimates and is taking into account new information about the application of the Act to the specific circumstances of the issuer when that information becomes available.

8. At the same time, ESMA notes that issuers should carefully assess whether measurement adjustments are a change in estimates or represent a correction of an error as defined in paragraph 5 of IAS 8 (e.g. mathematical mistake, mistake in applying accounting policy, fraud or oversight or misinterpretation of facts).

9. Finally, ESMA expects this Public Statement to be taken into account and reflected in the 2017 annual financial statements as well as in any subsequent reporting periods in which material adjustments are made to the estimated effects of the Act on reported tax assets and liabilities, thereby enhancing the comparability of IFRS financial statements in the EU. ESMA together with National Competent Authorities will monitor the level of transparency that issuers provide in their financial statements about the accounting for the effects of the Act, changes in estimates resulting from its implementation and information relevant to assessing its possible impact on the issuers' future financial statements.