



Financial Reporting Council

Feedback Statement and Impact Assessment

*Amendments to FRS 102 **The Financial Reporting Standard applicable in the UK and Republic of Ireland** and FRS 101 **Reduced Disclosure Framework***

**International tax reform –
Pillar Two model rules**

July 2023

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Executive Summary

- (i) The Financial Reporting Council's (FRC) overriding objective in setting accounting standards is to enable users of accounts to receive high-quality understandable financial reporting proportionate to the size and complexity of the entity and users' information needs.
- (ii) In July 2023, the FRC issued *Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 101 Reduced Disclosure Framework – International tax reform – Pillar Two model rules*. This Feedback Statement and Impact Assessment accompanies those amendments.
- (iii) In April 2023, the FRC issued FRED 83 *Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 101 Reduced Disclosure Framework – International tax reform – Pillar Two model rules*, which proposed to introduce a temporary exception to the accounting for deferred taxes arising from the implementation of the OECD's Pillar Two model rules, alongside targeted disclosure requirements.
- (iv) We received ten responses to FRED 83. Most respondents generally agreed with our proposals, with some providing suggestions to improve the clarity of the requirements. As FRED 83 was based on the IASB's Exposure Draft ED/2023/01 *International Tax Reform—Pillar Two Model Rules – Proposed amendments to IAS 12* we committed to considering the IASB's final amendments to IAS 12 *Income Taxes* as part of our redeliberations. In its final amendments the IASB has changed its approach to disclosure requirements in periods before Pillar Two legislation is effective from that set out in its Exposure Draft, instead introducing an objective-based disclosure requirement. Most respondents agreed that the FRC should take that approach too.
- (v) Having considered consultation responses, and the IASB's final amendments, we have finalised the amendments, which are an IFRS-based solution with appropriate changes and simplifications. Overall, the FRC believes that the amendments will have a positive impact on financial reporting that is expected to exceed the costs of applying the new requirements.

Introduction and Background

1. The FRC's overriding objective in setting accounting standards is to enable users of accounts to receive high-quality understandable financial reporting proportionate to the size and complexity of the entity and users' information needs.
2. In December 2021, the Organisation for Economic Co-operation and Development (OECD) published its Pillar Two model rules.¹ The rules are part of a two-pillar solution to address the tax challenges arising from the digitalisation of the economy.
3. The Pillar Two model rules:
 - (a) aim to ensure that large multinational groups pay a minimum amount of tax on income arising in each jurisdiction in which they operate; and
 - (b) would achieve that aim by applying a system of top-up taxes that results in the total amount of taxes payable on profit in each jurisdiction representing at least the minimum rate of 15%.

In general, the rules are intended to apply to multinational groups with revenue of over €750 million, subject to certain exclusions.

4. The FRC issued FRED 83 on 5 April 2023 for a comment period that closed on 24 May 2023. There are implications for income tax accounting resulting from jurisdictions implementing the Pillar Two model rules and FRED 83 proposed to introduce a temporary exception to the accounting for deferred taxes arising from the implementation of those rules, alongside targeted disclosure requirements. The proposals were based on similar proposals to amend IFRS Accounting Standards, issued by the IASB in Exposure Draft IASB/ED/2023/1 *International Tax Reform—Pillar Two Model Rules – Proposed amendments to IAS 12*.
5. The table below shows the number of respondents and analyses them by category.

Table 1: Category of Respondent

Category of Respondent	Number
Accounting firms	6
Professional bodies	4
Total	10

¹ OECD (2021), *Tax Challenges Arising from the Digitalisation of the Economy – Global Anti-Base Erosion Model Rules (Pillar Two): Inclusive Framework on BEPS*, OECD Publishing, Paris, <https://doi.org/10.1787/782bac33-en>.

Feedback Statement

6. The invitation to comment on FRED 83 posed six questions. The feedback and the FRC's response are summarised below.

Question 1

Do you agree that the proposed definition of the term 'Pillar Two legislation' would capture all transactions that are relevant to this topic? If not, please provide examples to support your view.

Table 2: responses to Question 1

Category of response	Number
Agreed	9
Agreed with reservations	1
Disagreed	-
Total	10

7. Most respondents agreed that the proposed definition of the term 'Pillar Two legislation' would capture all transactions that are relevant to this topic, with some minor drafting notes. Two of those respondents said they thought that it was important to fully align the definitions to those used by the IASB.

FRC response

8. We have made some changes to defined terms to refer to 'tax' rather than 'taxes', consistent with the rest of Section 29 *Income Tax*. Otherwise, our final definitions are the same as those proposed, and are aligned with those used by the IASB.

Question 2

Do you agree with the proposed amendments to FRS 102 that introduce mandatory temporary exceptions to recognising or disclosing information about deferred tax assets and liabilities related to Pillar Two income tax (proposed paragraph 29.2B), and to taking the effects of Pillar Two legislation into account when measuring deferred tax assets and liabilities (proposed paragraph 29.12)? If not, why not?

Table 3: responses to Question 2

Category of response	Number
Agreed	10
Disagreed	-
Total	10

9. All respondents agreed with the proposed amendments to introduce mandatory temporary exceptions (proposed paragraphs 29.2B and 29.12A). Some respondents suggested the temporary exception be kept under review by the FRC by monitoring the ongoing development of IFRS Accounting Standards.

FRC response

10. As proposed, the final amendments introduce a mandatory temporary exception to the accounting for deferred tax arising from the implementation of the Pillar Two model rules. As a temporary exception, it will be reviewed as appropriate.

Question 3

Do you agree with the proposed amendments to FRS 102 that require an entity to disclose:

- (a) the fact that it expects to fall within the scope of Pillar Two legislation (proposed paragraph 29.28);
- (b) the current tax expense related to Pillar Two income taxes (proposed sub-paragraph 29.26(g)); and
- (c) information that will enable users of financial statements to understand a group's potential exposure to paying top-up tax, when Pillar Two legislation has been enacted or substantively enacted but is not yet in effect (proposed paragraph 29.29)?

If not, why not?

Table 4: responses to Question 3

Category of response	Number
Agreed	3
Agreed with reservations	7
Disagreed	-
Total	10

11. Most respondents agreed with the proposed amendment to require an entity to disclose the fact that it expects to fall within the scope of Pillar Two legislation (proposed paragraph 29.28) and the proposed amendment to require an entity to disclose the current tax expense related to Pillar Two income tax (proposed sub-paragraph 29.26(g)).
12. The proposals in FRED 83 were based on similar proposals published by the IASB; we committed to considering the IASB's final amendments to IAS 12 *Income Taxes* when finalising our proposals. Most respondents agreed that the FRC should take the same approach as the IASB and replace the specific detailed requirements in proposed paragraph 29.29 with an objective-based disclosure requirement that is still intended to help users of financial statements understand potential exposure to paying top-up tax.

FRC response

13. Our approach to this matter remains an IFRS-based solution. Therefore, in finalising the amendments, a number of changes have been made to the proposals in FRED 83 to reflect the changes the IASB made to its proposals in finalising them, as well as respondents' detailed comments. This includes replacing proposed paragraph 29.29, which would have required disclosure of specific detailed information, with a requirement for an entity to disclose known or reasonably estimable qualitative and quantitative information that helps users of the financial statements understand the entity's exposure to Pillar Two income tax.

Question 4

Do you agree with the proposal to exempt qualifying entities, as defined in FRS 102 or FRS 101, from the disclosures that would otherwise be required by proposed paragraph 29.29 of FRS 102 and proposed² paragraph 88C of IAS 12 *Income Taxes* respectively? If not, why not?

Table 5: responses to Question 4

Category of response	Number
Agreed	7
Disagreed	3
Total	10

14. Most respondents supported the proposal to exempt qualifying entities from the detailed quantitative disclosure requirements proposed in FRED 83 (paragraph 29.29 of FRS 102), and the equivalent disclosure requirements in IAS 12 for FRS 101 preparers). However, some respondents thought that the disclosures could nevertheless be useful for users of qualifying entities' financial statements whilst Pillar Two legislation is not universally enacted, and in the case when the qualifying entity is an intermediate parent.
15. In the final amendments to IAS 12 the IASB has altered the disclosure requirements compared with the proposals in its exposure draft, by introducing a disclosure objective and removing the proposed detailed quantitative disclosures. In this context, some respondents suggested that an exemption in FRS 101 was no longer necessary.
16. As set out in relation to Question 3 above, respondents agreed with the FRC following the IASB in altering the disclosure requirements for FRS 102. Three respondents said that, if we did so, an exemption for qualifying entities in FRS 102 would not be necessary because the objective-driven disclosure requirements would allow entities to tailor their disclosures to meet the needs of their users in any case. However, two respondents said they would still support an exemption for qualifying entities if the disclosure requirements were amended.

FRC response

17. The final amendments make an exemption available to qualifying entities as defined in FRS 102 from the disclosures that would otherwise be required by paragraphs 29.28(b) and 29.29, provided that equivalent disclosures are included in the consolidated financial statements in which the entity is included.
18. A similar exemption is made available to qualifying entities as defined in FRS 101 from the disclosures that would otherwise be required by paragraphs 88C and 88D of IAS 12.
19. This approach provides a proportionate solution to users' information needs because top-up taxes are determined on a group basis and therefore users of financial statements will be able to

² Proposed in IASB/ED/2023/1 International Tax Reform—Pillar Two Model Rules – Proposed amendments to IAS 12, available at <https://www.ifrs.org/projects/work-plan/international-tax-reform-pillar-two-model-rules/exposure-draft-and-comment-letters/>.

obtain useful information about exposure to paying top-up taxes from the consolidated financial statements of the group in which the entity is consolidated.

Question 5

Do you agree with the proposed effective dates for these amendments? If not, what difficulties do you foresee?

Table 6: responses to Question 5

Category of response	Number
Agreed	5
Agreed with reservations	5
Disagreed	-
Total	10

20. All respondents broadly agreed with the proposed effective dates for the amendments. However, five respondents thought that proposed paragraph 29.12A (the temporary exception to considering the effects of Pillar Two legislation on the measurement of recognised deferred tax balances) should also be effective immediately and retrospectively, like proposed paragraph 29.2B. One respondent suggested that an entity should only be required to apply the exceptions from the date the Pillar Two legislation is enacted or substantively enacted, not the date the amendments are issued.
21. Three respondents thought that some disclosures should not be required for entities preparing interim financial statements in accordance with FRS 104 *Interim Financial Reporting* for periods ending on or before 31 December 2023.

FRC response

22. We agree that paragraph 29.12A should apply immediately and have made that change in the final amendments. The exceptions would only have effect once Pillar Two legislation has been substantively enacted, but we think it is clearer for the requirements to apply immediately upon issue of the amendments rather than the effective date being tied to an external event that may differ by jurisdiction.
23. The final amendments do not amend FRS 104. The disclosure requirements in paragraphs 29.28 and 29.29 of FRS 102 only require an entity to disclose known or reasonably estimable information, which we think would make them proportionate to apply if an entity preparing interim financial statements were to make those disclosures.

Question 6

In relation to the consultation stage impact assessment, do you have any comments on the costs and benefits identified? Please provide evidence to support your views.

Table 7: responses to Question 6

Category of response	Number
Did not comment ³	5
Commented in agreement	3
Commented with concerns	2
Total	10

24. Of those respondents commenting, three agreed that, whilst it is difficult to assess the costs and benefits of the proposals, the benefits would outweigh any potential costs of implementation.
25. Two respondents said that one of the reasons they thought we should amend proposed paragraphs 29.29(b) and (c) was because the additional costs of preparing the disclosures would outweigh the benefits to users.

FRC response

26. We have significantly altered paragraph 29.29, which should reduce the costs of preparing the disclosures. Overall, we continue to believe that the final amendments will have a positive impact on financial reporting that is expected to exceed the costs of applying the new requirements. The final impact assessment for these amendments is set out on pages 10 and 11.

³ Includes those respondents that stated that they had no comments in relation to Question 6 and those who did not address Question 6.

Impact Assessment

Introduction

27. The FRC is committed to a proportionate approach to the use of its powers, making effective use of impact assessments and having regard to the impact of regulation on small enterprises.

Amendments to FRS 102 and FRS 101

28. *Amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and FRS 101 Reduced Disclosure Framework – International tax reform – Pillar Two model rules* was issued in response to the expected enactment of tax law that implements the Pillar Two model rules into domestic legislation.

29. The amendments will affect entities applying FRS 102 and FRS 101 that are, or expect to be, within the scope of Pillar Two legislation. The high-level scope of the OECD's Pillar Two model rules is relatively clear, but the final approach taken may differ in practice in different jurisdictions.

30. We expect that, as set out in the high-level scope of the OECD's Pillar Two model rules, entities in scope will include those that are members of corporate groups with revenue in their consolidated financial statements exceeding €750 million in at least two of the four preceding fiscal years, but will exclude government entities, international organisations, non-profit organisations, pension funds, investment funds or real estate funds. Only some such entities will apply FRS 102 or FRS 101 and be affected by these amendments; some entities may instead, for example, apply adopted IFRS Accounting Standards.

31. OECD statistics⁴ indicate that there are 387 Multinational Enterprises (MNEs) which have headquarters in the UK, and 61 MNEs which have headquarters in the Republic of Ireland, with consolidated revenues of at least €750 million. The UK government estimates that the number of MNEs with consolidated revenues of at least €750 million which have operations in the UK but are headquartered outside the UK is 4,000.⁵ Each MNE may include a number of entities preparing financial statements. However, even taking this into account, we expect that the amendments will affect only a small proportion of the entities that apply FRS 102, which we estimate to be 1,767,465 entities in total.⁶

32. The amendments provide a temporary exception to certain aspects of recognition and measurement of deferred taxes, and require certain disclosures relating to Pillar Two income tax. They are not expected to affect an entity's exposure to tax.

⁴ The fourth edition of the Corporate Tax Statistics database available at <https://www.oecd.org/tax/beps/corporate-tax-statisticsdatabase.htm>.

⁵ Written question, 31 January 2023, UIN 136517 available at <https://questions-statements.parliament.uk/written-questions/detail/2023-01-31/136517>.

⁶ Tables 1 and 2 of the Consultation Stage Impact Assessment accompanying FRED 82 Draft amendments to FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland and other FRSs, available at <https://www.frc.org.uk/fred82>.

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33. Because the application of the principles and requirements in Section 29 *Income tax* of FRS 102 in the absence of these amendments could be inconsistent, it is difficult to assess the impact that the amendments will have. However, in general, we expect that they will:
- (a) respond to the information needs of users of financial statements by requiring entities to provide targeted disclosures about exposure to Pillar Two income tax;
 - (b) for FRS 102:
 - (i) allow in-scope entities to avoid costs that they would otherwise have incurred in recognising and disclosing information about deferred tax assets and deferred tax liabilities related to top-up taxes; and
 - (ii) introduce limited additional costs, which would be less than the costs avoided, because the new disclosure requirements in:
 - I. paragraphs 29.26(g) and 29.28(a) are readily determinable from the analysis a group will carry out to comply with Pillar Two legislation;
 - II. paragraphs 29.28 and 29.29 only require disclosure of known or reasonably estimable information; they do not require an entity to prepare new information; and
 - III. paragraphs 29.28(b) and 29.29 would not apply to qualifying entities, as defined in FRS 102, provided that equivalent disclosures are included in the consolidated financial statements in which the qualifying entity is included; and
 - (c) for FRS 101, provide a proportionate solution to users' information needs by making a disclosure exemption available to qualifying entities, provided that equivalent disclosures are included in the consolidated financial statements in which the qualifying entity is included.

Conclusion

34. Overall, the FRC believes that the amendments will have a positive impact on financial reporting that is expected to exceed the costs of applying the new requirements.

Appendix

List of respondents to the Consultation:

- Chartered Accountants Ireland
- Deloitte LLP
- Ernst & Young LLP
- ICAEW
- ICAS
- CPA Ireland
- KPMG LLP
- Mazars LLP
- PricewaterhouseCoopers LLP
- RSM UK Tax and Accounting Limited



Financial Reporting Council

**Financial
Reporting Council**

8th Floor
125 London Wall
London EC2Y 5AS
+44 (0)20 7492 2300

www.frc.org.uk

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