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International Accounting Standards Board (IASB)
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Berne, 10 March 2023

International Tax Reform: Pillar Two Model Rules – proposed amendments to IAS 12

Dear Madam, dear Sir

SwissHoldings, the Swiss Federation of Industrial and Services Groups in Switzerland, represents 61 Swiss groups, including most of the country's major industrial and commercial enterprises. We very much welcome the opportunity to provide comments to this Exposure Draft (ED). Our detailed response (in the appendix) has been prepared in conjunction with our member companies.

The temporary exemption for the application of IAS 12 in respect of the Pillar Two requirements is a welcome and necessary step. We agree with the IASB's thinking and conclusion on this.

On the other hand, the disclosure requirements in the ED will be misleading to readers and commercially damaging to companies. Readers are given a picture of the impact of the Pillar Two requirements which is knowingly incomplete and inaccurate. Moreover they create many precedents, by requiring disclosure in financial statements of legislative developments and the provision of financial information that is not relevant to the current year results, but which is rather designed to allow forward-looking modelling of future events. These requirements should be deleted in their entirety, and companies should rather be encouraged to discuss the impact of the Pillar Two requirements in their Management Discussion & Analysis.

We would also like to highlight that the Financial Accounting Standards Board (FASB) issued a tentative decision on 1 February 2023 that the Pillar Two minimum tax is an alternative minimum tax per ASC 740 and therefore the existing requirements of ASC 740 would apply without additional burden to companies. We believe there is little benefit in the IASB developing different solutions to this topic compared to the FASB. We do not see why readers of IFRS financial statements require these additional disclosures described in the ED, while apparently readers of US GAAP financial statements do not need them. In addition to that, the FASB clarified that under the existing ASC 740 rules for deferred tax balance recognition and measurement, deferred tax balances would not be recognized or adjusted for the effect of OECD Pillar Two global minimum taxes. We would encourage the IASB considering this FASB approach for deferred tax balance recognition and measurement when it develops a framework for deferred tax accounting for the Pillar Two global minimum taxes that would supersede the temporary exception of pp4A and pp88A.

We would remind the IASB that in Switzerland, and many other jurisdictions, listed companies have the option to apply local GAAP or US GAAP instead of IFRS. The issuing of misleading and commercially damaging disclosure requirements, is not conducive to the wider adoption of IFRS.

SwissHoldings

Yours sincerely,

SwissHoldings

Federation of Industrial and Service Groups in Switzerland

Dr Gabriel Rumo
Director

Denise Laufer
Member Executive Committee

APPENDIX

QUESTIONS FOR RESPONDENT

Question 1 - Temporary exception to the accounting for deferred taxes (paragraphs 4A and 88A):

a) IAS 12 applies to income taxes arising from tax law enacted or substantively enacted to implement the Pillar Two model rules published by the OECD, including tax law that implements qualified domestic minimum top-up taxes described in those rules.

b) The IASB proposes that, as an exception to the requirements in IAS 12, an entity neither recognise nor disclose information about deferred tax assets and liabilities related to Pillar Two income taxes.

c) The IASB also proposes that an entity disclose that it has applied the exception.

d) Paragraphs BC13–BC17 of the Basis for Conclusions explain the IASB's rationale for this proposal.

e) Do you agree with this proposal? Why or why not? If you disagree with the proposal, please explain what you would suggest instead and why.

Answer to Question 1

The proposed temporary exemption is both welcome and necessary. We support this proposal.

We support the concerns noted in BC 10 about the uncertainties of how to apply the top-up taxes to the calculation of deferred taxes, and also those noted in BC 11 about the usefulness to readers of such information.

Furthermore we support the remarks in BC 17 that "further work is needed to determine how entities apply the principles and requirements in IAS 12 to account for deferred taxes related to Pillar Two income taxes" and would encourage the IASB to treat this matter with priority in the immediate future.

We would also encourage the IASB to align with the FASB and other standard setters, so that there is a uniform global approach. In this respect it is noteworthy to consider the most recent FASB announcement around deferred tax accounting for Pillar Two global minimum taxes. Consistent with that announcement and given the complexities, high level of judgment required around assessing the implications of future events and the time and effort that will be involved with respect to deferred tax accounting for Pillar Two, we believe a permanent exception could be a reasonable option as well. Therefore, we encourage the IASB to consider such a scenario of a permanent exception for deferred tax accounting as a viable option within the overall context and theoretical framework of deferred tax accounting.

We believe that pp88A is unnecessary and should be deleted. We believe this proposal now creates a precedent to disclose that mandatory requirements have been implemented. We note that recent IASB initiatives about "disclosure overload" have actually been moving in the opposite direction by, for example, encouraging that simply restating the requirements from the standards in the accounting policies is unnecessary.

Various jurisdictions intend to introduce a domestic minimum top-up tax. There are uncertainties as to whether these national taxes will be classified ultimately as qualified domestic minimum top-up tax (QDMTT) described in the model rules. It is possible that the uncertainties regarding classification of national taxes as QDMTT will remain until the beginning of 2024. In this case, the temporary exemption to the accounting for deferred taxes intended by the ED could be ineffective for the financial year 2023. An entity would have to assess whether the new domestic top-up tax create additional temporary differences and how to measure deferred taxes. The information that would result from recognizing deferred taxes related to not yet qualified top-up tax is not useful for investors. We encourage the IASB to examine whether the scope of the temporary exemption to the accounting for deferred taxes should be extended to enacted or substantively enacted non-qualifying top-up taxes that have materially the same financial impact as a QDMTT.

Question 2 - Disclosure (paragraphs 88B–88C)

The IASB proposes that, in periods in which Pillar Two legislation is enacted or substantively enacted, but not yet in effect, an entity disclose for the current period only:

a) information about such legislation enacted or substantively enacted in jurisdictions in which the entity operates.

b) the jurisdictions in which the entity's average effective tax rate (calculated as specified in paragraph 86 of IAS 12) for the current period is below 15%. The entity would also disclose the accounting profit and tax expense (income) for these jurisdictions in aggregate, as well as the resulting weighted average effective tax rate.

c) whether assessments the entity has made in preparing to comply with Pillar Two legislation indicate that there are jurisdictions:

i. identified in applying the proposed requirement in (b) but in relation to which the entity might not be exposed to paying Pillar Two income taxes; or

ii. not identified in applying the proposed requirement in (b) but in relation to which the entity might be exposed to paying Pillar Two income taxes. The IASB also proposes that, in periods in which Pillar Two legislation is in effect, an entity disclose separately its current tax expense (income) related to Pillar Two income taxes. Paragraphs BC18–BC25 of the Basis for Conclusions explain the IASB's rationale for this proposal.

Do you agree with this proposal? Why or why not? If you disagree with the proposal, please explain what you would suggest instead and why.

Answer to Question 2

<u>Paragraph 88B</u>

We believe that pp88B is unnecessary, is too loosely defined and will be confusing to readers.

In practical terms, the implementation of the Pillar Two reforms can be expected to increase the effective tax rates for many companies. This will occur because of a combination of:

- "Low-tax" jurisdictions increasing their tax rates and/or changing their rules of which items are taxable or tax-deductible; and
- The "Top-up taxes" will be levied.

We read pp88B as requiring disclosure only of the "Top-up taxes", although this is unclear from the ED and should in any case be clarified in the final standard. However, disclosing only this tells an isolated part of the impact of the Pillar Two reforms and on its own is not meaningful, and indeed potentially misleading. A company may well end up paying more income taxes as a result of the Pillar Two reforms due to changes in local tax rates/regulations, but a relatively minor amount of "Top-up taxes". In this case the company will disclose this relatively minor amount and the reader is almost invited to jump to the entirely wrong conclusion that the Pillar Two reforms have only a relatively minor impact on the company.

Furthermore we believe this proposal now creates a precedent to breakdown the income tax expense.

Implementing this change will require system changes to collect this information, and will add to the (already substantial) cost of implementing the Pillar Two reforms.

In our view there is no need for such specific disclosure requirement of 88B, because under the general disclosure requirements of pp79 (in combination with pp80) major components of tax expense shall be disclosed separately. Consequently, in case the additional Pillar Two tax expense would have a significant impact to the effective tax rate it will be disclosed separately anyway.

Paragraph 88C

BC 19 states that "users of financial statements need information to help them assess an entity's exposure to paying top-up tax". In our view this is incorrect. What we believe users need is "information to help them assess an entity's exposure to paying additional taxes following the Pillar Two reforms" – and that investors are not so concerned about whether this mechanically is incurred as "top-up tax" or whether it occurs because of changes in local tax rates/regulations.

Therefore, we believe the disclosure proposals are fundamentally addressing the wrong question. We note that there are no disclosure requirements relating to changes in local tax rates or local tax rules that would have been driven or influenced by the Pillar Two reforms, although it is of course judgmental about which changes were driven by Pillar Two and which would have occurred regardless.

Moreover, we believe that the disclosure proposals are directly written to require quantitative forward-looking information. BC23 makes it clear that this is what is behind the proposal. But as pointed out by the dissenting Board members in BC22, the forward-looking information required will actually confuse and mislead readers.

We note that nowhere else in IAS 12 are companies required to quantify the future impact on earnings of any tax rate changes that are not yet in effect and that these proposals create a new precedent.

Instead companies should be encouraged to inform readers about the potential and on-going impacts of the Pillar Two reforms on their effective tax rate and tax payments through the Management Discussion and Analysis (as outlined by pp18 of the IFRS Practice Statement 1: Management Commentary). Nevertheless, companies should not be required to provide forward-looking information.

We also believe that all such information is not necessary in the stand-alone IFRS financial statements of fully owned subsidiaries, and will add substantially to the burden of producing such financial statements. We encourage the IASB to consider and clarify this in the final standard.

Specifically to the requirements:

Paragraph 88C (a)

We believe that pp88C (a) is unnecessary. It should be replaced by more targeted and meaningful disclosure.

We do not consider that financial statements should provide a running commentary on the development of tax (or any other) legislation. Such information is already in the public domain. The requirement to include this in financial statements will result in a large volume of boiler-plate disclosures, as the information about each tax jurisdiction will be the same for each company.

The disclosure requirement is unclear about which jurisdictions should disclosures be made for, and for many preparers this could be in the tens or hundreds of jurisdictions. As an example in Switzerland alone there are 26 Kanton (State) tax jurisdictions as well as the Bund (Federal) level.

Moreover, such legislation is dynamically evolving as the Pillar 2 requirements are implemented globally, and any such information will need to be constantly updated by the company prior to the approval of the financial statements, and will quickly become out of date after they are published.

We note that nowhere else in IAS 12 are companies required to comment on the development of tax legislation, and that these proposals create a new precedent.

More helpful to readers would be for companies to list the major tax jurisdictions in which they are active. The reader can then get up-to-date information themselves for their own specific needs. Of course much of this information is already available through the disclosures required by IAS 1 pp138, IFRS 8 pp33 and IFRS 12 pp10.

Paragraph 88C (b)

We believe that pp88C (b) is poorly drafted, and would require companies to provide information which they know to be misleading to readers and which would be commercially damaging. It should be deleted in its entirety.

We understand that it attempts to provide the reader with forward-looking information about the impact of tax changes in future reporting periods. We note that nowhere else in IAS 12 are companies required to quantify the impact on earnings of any tax rate changes that are not yet in effect, and that these proposals create a major new precedent. We observe this with great concern and do not believe it appropriate that such changes are made with such accelerated comment and review periods.

Furthermore, tax expense (income) presented in the financial statements by applying IAS 12, as required by pp 88C(b), is just the starting point for Pillar Two purposes and must be adjusted for several items, resulting in that those numbers differ significantly from each other.

For example, dividend income is part of the accounting profit, whereas dividends must be eliminated for the calculation of the GloBE Profit or Loss. The elimination of dividends may have a material impact on the calculation of the ETR and the Top-up Tax for Pillar Two purposes. This clearly shows that the required information would not achieve the objective of providing useful information for users of financial statements.

In the example below, the IAS 2 and Pillar 2 ETR differs substantially due to these adjustments:

	ETR as per	
Company -XYZ	**IAS -12**	**Pillar -2**
Operating profit	2,000	2,000
Impairment of goodwill (asset deal)	-100	-100
Profit on disposal of a business (asset deal)	400	400
A)	**2,300**	**2,300**
From foreign subsidiaries *		
IG dividend income from all foreign subsidiaries	10,000	
Impairment of participation in SUB X	-1,000	
Profit on disposal of participation in SUB Y	2,000	
B)	**11,000**	**0**
Profit before taxes (A+B)	**13,300**	**2,300**
Taxes (15%) on A	-345	-345
Effective tax rate	**2.6%**	**15.0%**

* Dividends/ participations are excluded from Pillar 2 calculations

Turning to the disclosure itself, we interpret the proposal to require that in their 2023 annual financial statements, companies should include a statement, for example, that "In tax jurisdictions A, B and C, the average effective tax rate, as calculated according to IFRS, is below 15%. The combined IFRS income tax expense in these tax jurisdictions was LC 1,000, the combined IFRS accounting profit before tax was LC 20,000, and the resulting weighted average effective tax rate was 5%". In any event, if contrary to our proposal it is decided to keep the disclosure requirement of pp88C(b), a clarification is needed of how 'accounting profit for these jurisdictions' is defined.

More specifically it needs to be clarified if this accounting profit includes or excludes intercompany expense and profit components that are eliminated in consolidation.

Obviously, the reader is then expected to conclude that, once the minimum 15% rate is rolled out globally, the company will have to pay an additional LC 2,000 in tax in future periods.

We can also expect that media, political and other interested parties in tax jurisdictions A, B and C will also read these disclosures. This will then create a narrative that the company is either "avoiding tax" or "not paying its fair share". This can be commercially and reputationally damaging for the company concerned.

We can further expect that the tax authorities in tax jurisdictions A, B and C will read these disclosures, and these may result in challenges to the company's tax reporting in these places.

All of this would be entirely erroneous:

- The application of the Pillar Two rules will not use the full unadjusted IFRS profit. Far from it.
- Neither will it use the full unadjusted IFRS income tax expense. Far from it.
- The rules in place at the end of 2023 will not necessarily be the final rules that will apply, and they will evolve during 2023 and further into 2024.
- The company's results and the breakdown of profit and tax expense in future years will in any case be different to that of 2023.
- As noted in BC 22 at least some IASB members are fully aware of all of this, and we endorse their opposition to these disclosures, and we strongly encourage the other members of the board to reconsider their views noted in BC 23, for the reasons we described above.

This proposed disclosure has no relevance for the current year results, and is included solely to allow forward-looking projections. It creates a new precedent in that respect, and such precedent-making should be done (if done at all) through the usual considered standard setting process, and not added onto the urgently needed amendments in pp4A with limited time for review and discussion.

Finally, we are not aware that the FASB, or other accounting standard setters will require such information from companies, and therefore this will put IFRS preparers at a disadvantage.

Paragraph 88C (c)

We read pp88C (c) as being ancillary to pp88C (b) and consider it should also be deleted in its entirety, especially considering that companies first have to disclose under pp12.88C(b) information that would be misleading and that subsequently under IAS 12.88C(c) this (misleading) information should be put into context. When preparing the 2023 financial statements, the implementation of the Pillar Two requirements will be work-in-progress for companies, and moreover we can expect that the tax rates/regulations will continue to evolve during 2023 and 2024.

The users of the accounts would be confused if misleading information required under pp88C(b) is then "corrected" by narrative disclosure under pp88C(c). Any company which is in a position to make the disclosures required by pp 88C(c) would likely be able to directly disclose the expected impact if material. On the other hand, companies which do not have the information to estimate the impact of the GLoBE rules will hardly be able to make the disclosures required in pp88C(c) either.

Many companies may not able to make any firm conclusions as imagined by pp88C (c) and will be reluctant to make any premature public statements, for the reasons outlined previously.

Question 3 - Effective date and transition (paragraph 98M)

The IASB proposes that an entity apply:

- ***a) the exception — and the requirement to disclose that the entity has applied the exception — immediately upon issue of the amendments and retrospectively in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors; and***
- ***b) the disclosure requirements in paragraphs 88B–88C for annual reporting periods beginning on or after 1 January 2023.***

Paragraphs BC27–BC28 of the Basis for Conclusions explain the IASB's rationale for this proposal.

Do you agree with this proposal? Why or why not? If you disagree with the proposal, please explain what you would suggest instead and why.

Answer to Question 3

We agree that the exception in the amendment to pp4A should be available for immediate application, notably in 30 June 2023 Interim Financial Statements.

We do not agree to the proposals in pp88B and pp88C. Any disclosure thought necessary should be covered in the Management Discussion and Analysis, as would usually be the case, and is outside the scope of IAS 12.