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Ref: EFRAG's due process on the IASB's Exposure Draft International Tax Reform – Pillar Two Model Rules

Dear Dr Klinz, dear Wolf,

The European Securities and Markets Authority (ESMA) thanks you for the opportunity to contribute to EFRAG's due process with regards to Exposure Draft ED/2023/1 *Exposure Draft International Tax Reform – Pillar Two Model Rules*. We are pleased to provide you with the following comments with the aim of improving the consistent application and enforceability of IFRS in the European Union.

ESMA agrees with the IASB that entities need sufficient time to determine how to apply the principles and requirements in IAS 12 to account for deferred taxes related to top-up taxes resulting from the implementation of the OECD's Pillar Two model rules in different jurisdictions. ESMA therefore welcomes the initiative to introduce a temporary exception to the accounting for deferred taxes arising from the implementation of the Pillar Two model rules. ESMA supports the proposal to make the temporary exception mandatory, rather than optional, as this will improve the comparability of information between entities.

ESMA notes that the IASB has not specified how long the temporary exception would apply. While ESMA agrees that it is currently difficult to assess how much time will be needed for further work to determine how entities should apply the principles and requirements of IAS 12 to account for deferred taxes under the Pillar Two model rules, ESMA considers that the proposed exception constitutes a departure from the fundamental principles of IAS 12. Therefore, ESMA strongly encourages the IASB to closely monitor and analyse future developments related to the implementation of the Pillar Two model rules in different jurisdictions and replace the temporary exemption with a sustainable solution as soon as feasible. ESMA also encourages the IASB to engage with stakeholders on what actions are needed to support the consistent application of IAS 12, including providing any necessary guidance or illustrative examples as part of future standard-setting activities.

ESMA also supports the targeted disclosure requirements as well as the effective date and transition provisions proposed by the Board. In particular, ESMA agrees with the requirement in paragraph 88C(b) of the ED to disclose the jurisdictions in which the entity's average effective tax rate, calculated according to requirements of IAS 12, is below 15%, the tax

expense and accounting profit for those jurisdictions in aggregate and the resulting weighted average effective tax rate. EFRAG notes in its draft comment letter that it will seek views from its constituents on the usefulness of the proposed disclosures. Although the specific requirements with regards to the calculation of the effective tax rate included in Pillar Two model rules differ from those in IAS 12, ESMA considers that the proposed disclosures will provide useful indications of an entity's potential exposure to top-up taxes. ESMA also agrees with the separate disclosure of current tax expense related to Pillar Two income taxes as it would enable users to understand the magnitude of these taxes.

Taking into account that some jurisdictions are expected to enact tax law to implement the Pillar Two model rules in the first half of 2023 ESMA, like EFRAG, emphasises the importance of the timing of the publication of the amendment to IAS 12.

Finally, ESMA believes that convergence between IFRS and US GAAP in this area is of high importance and encourages the IASB to coordinate its future work regarding the impact of Pillar Two model rules on financial reporting with the FASB.

In case you have any questions or comments please do not hesitate to contact me or Isabelle Grauer-Gaynor, Head of the Corporate Finance and Reporting Unit (Isabelle.Grauer-Gaynor@esma.europa.eu).

Yours sincerely,

[signed]

Verena Ross