



Accounting for deferred tax for an investment property business

FRS 102 is the financial reporting standard applicable to companies in the UK and the Republic of Ireland. This factsheet addresses how FRS 102 requires consideration of deferred tax. It should be noted that accounts prepared under FRS 105 (i.e. micro entities) will not require deferred tax disclosures.

What is deferred tax?

Deferred tax arises from differences between 'taxable profits' and 'accounting profits'. A simple way of understanding it is by considering capital expenditure. For tax purposes, 100% tax relief can be given in the year of acquisition, via capital allowances, whereas the cost of an asset is written off in the accounts over several years, via depreciation. In this case, there is a temporary timing difference between the taxable profits and the accounting profits. This is recorded in the accounts as a deferred tax liability because the tax relief has been given upfront and the accounts will take a few years to catch up!

You may also see a deferred tax asset. An example of this is if a company makes a loss and is able to carry forward the loss in order to reduce the taxable profits of future years. In this case, a deferred tax asset has been created and it should be shown in the accounts.

How is it calculated?

Deferred tax is calculated using the tax rates that have been substantively enacted for the balance sheet date for the accounting period in which the timing differences are expected to reverse. In the loss example above, the deferred tax asset would be calculated using the tax rate applicable for the accounting period in which the business expects to make a profit and offset the loss.

How is it disclosed in the accounts?

Deferred tax assets and liabilities should be calculated as at the balance sheet date and disclosed in the balance sheet, as appropriate.

Deferred tax assets should only be recognised in the accounts if it is probable (i.e. more likely than not) that they will be recovered.

Continuing our loss example, FRS 102 would require consideration as to whether the business is likely to make profits against which the loss could be offset. If future profits are not probable, the deferred tax asset should not be recognised.

Year on year changes to the deferred tax asset/liability are recognised as a deferred tax charge in the profit and loss account.

How does it apply to property investment companies?

FRS 102 requires investment properties to be revalued at their fair value on the balance sheet date and for deferred tax to be calculated in respect of any changes in value.

If a property's fair value were to increase by £20,000, this would mean that a company's taxable profits would be £20,000 higher should the property be sold. If the owner expected to pay corporation tax at 25% in the year of sale then a deferred tax liability of £5,000 (25% of £20,000) should be recorded.

To learn more about deferred tax, please speak to us - we will be happy to help!