AICPA

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Re: File Reference 2019-500

The Financial Reporting Executive Committee (FinREC) of the American Institute of Certified Public Accountants (AICPA) appreciates the opportunity to comment on the Financial Accounting Standards Board's (FASB or Board) March 25, 2019 Exposure Draft, *Income Taxes (Topic 740)—Disclosure Framework—Changes to the Disclosure Requirements for Income Taxes*.

FinREC supports the Board's intent to modify disclosure requirements to result in more effective, decision-useful information about income taxes. We generally believe that the proposed amendments will result in more effective disclosures by focusing on information that is important to the financial statement users. However, as discussed in the attached responses, we did note a few matters of particular concern.

Appendix A to this letter includes our responses to the questions for respondents raised in the proposed ASU. Representatives of FinREC are available to discuss our comments with Board members or staff at their convenience.

Sincerely,

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Appendix A

Responses to Questions for Respondents in the Proposed ASU

FinREC is pleased to provide responses to specific questions for respondents presented in the proposed ASU.

Question 1: Would the amendments in this proposed Update that add or modify disclosure requirements result in more effective, decision-useful information about income taxes? Please explain why or why not. Would the proposed amendments result in the elimination of decision-useful information about income taxes? If yes, please explain why.

We generally believe that the proposed amendments will result in more effective and useful information about income taxes except for the matters noted below.

- The proposed amendment in ASC 740-10-50-6A (a) would require public business entities (PBEs) to disclose a tax-effected table for carryforwards while private companies would be required to disclose carryforwards gross in accordance with ASC 740-10-50-8A. Although private companies often are exempted from certain disclosure requirements, it is unusual to have all companies subject to a disclosure requirement, with private companies using a different measurement. We believe this difference between the proposed public and private company disclosure may be confusing to the users of the financial statements.

- The proposed amendments in ASC 740-10-50-6B would require public business entities to disclose the amount of valuation allowance recognized and released during the period with an explanation for each. Chapter 8, *Notes to Financial Statements*, of Statement of Financial Accounting Concepts No. 8 indicates that the notes should provide information about specific line items when the amount and description do not give users enough information to assist in their decisions about whether to provide resources to an entity. We believe an explanation of year-over-year changes in the valuation allowance extends beyond the information necessary for a financial statement user to make resource decisions. We believe this disclosure is better placed in Management's Discussion and Analysis.

  However, if the Board decides to retain the disclosure requirement, we recommend the explanation of the material changes be required only as a result of changes in judgment. Often changes in the valuation allowance may be simply by-products of normal operations. For example, an entity with a full valuation allowance may continue to incur losses or have reversing deferred tax liabilities (DTLs) that mathematically cause a change in the valuation allowance with no real change in fact pattern or judgment. As such, this information would not seem relevant to the financial statement users.

- The proposed amendments in ASC 740-10-50-12 would require explanation of the year-over-year change in an amount or percentage of reconciling items in the rate reconciliation. For the same reasons noted above, we believe an explanation of year-over-year changes in reconciling items extends beyond the information necessary for a financial statement user to make resource decisions.

However, if the Board decides to retain the disclosure requirement, we recommend that the explanation of changes year over year should be as a result of significant changes in operations. Similar to changes in the valuation allowance, changes in the reconciling items will change annually due to the changes in income levels purely due to the mathematics. For example, a multinational entity experiences increased earnings all over the world so its incremental foreign tax expense reconciling item in the effective tax rate (ETR) grows in dollars but is not changing relative to the overall effective tax rate.

Overall, we believe the proposed amendment would not result in the elimination of any decision-useful information from a preparer/auditor perspective.

Question 2: Are the proposed disclosure requirements operable and auditable? If not, which aspects pose operability or auditability issues and why?

We generally believe the proposed disclosure requirements are operable and auditable except for the matters noted below.

- The proposed requirements of ASC 740-10-50-6A would require carryforwards to be disaggregated by time period of expiration along with the amount of the valuation allowance recognized for deferred tax assets for federal, state, or foreign carryforwards. The provisions of ASC 740 do not require companies to determine a valuation allowance on the basis of each underlying deductible temporary difference or to allocate the valuation allowance to specific deferred tax assets (DTAs) for deductible temporary differences and tax attributes. As such, any allocations made would likely be arbitrary and inconsistently performed. Further, the valuation allowance is generally not calculated or scheduled on a year-by-year basis. Companies generally would not have this data readily available.
- As discussed in our response to Question 1 above, we anticipate that there will be difficulties in, or lack of useful information associated with, providing a narrative related to the year-over-year changes in the valuation allowance and year-over-year change in an amount or percentage of reconciling items in the rate reconciliation. A likely component of the year-over-year changes would be simply math based on the changes in the deferred tax liabilities and/or changes in the level of income and as such would not provide useful information to the financial statement users. We recommend that the Board remove these proposed disclosures or require that they be provided only when the year-over-year change is due to a change in judgment, subjective reasons, or new information.
- We also believe that the proposed requirement of ASC 740-10-50-10A to disclose pretax book income before intra-entity eliminations disaggregated between domestic and foreign in certain instances could be inoperable or unauditable. Please see our response to Question 4 for a more detailed discussion.

Question 3: Would any of the proposed disclosures impose significant incremental costs? If so, please describe the nature and extent of the additional costs.

As discussed in our responses to Questions 1 and 2 above, the requirement to disaggregate the carryforwards by time period of expiration along with the amount of any associated valuation allowance recognized for these carryforwards would impose the most significant incremental costs for entities. In addition, the year-over-year changes required to be disclosed associated with the valuation allowance and reconciling items in the rate reconciliation, the carryforward table by time period of expiration, and pretax income before intra-entity transactions may require entities to capture different data, change internal processes and related controls, or reconfigure existing IT platforms in order to accurately capture and disclose the required information.

Question 4: One of the proposed amendments would require entities to disclose pretax income (or loss) from continuing operations before intra-entity eliminations disaggregated between domestic and foreign, which initial feedback indicated would reduce diversity in practice. Would this proposed amendment be operable? Should the Board specify whether the disclosed amounts should be before or after intra-entity eliminations? Why or why not?

We generally agree with the principle, but believe the guidance as written may not address the diversity in practice. For example, some companies record intra-entity transfers pretax and others do not. We understand that responses to the previous exposure draft discussed the need for clarity and definition related to the disclosure of domestic and foreign pretax income; however, some preparers may find that either there are difficulties in computing or tracking pretax income before intra-entity eliminations due to existing data used in internal reporting and compliance, or the measure of pretax income before intra-entity eliminations is less relevant due to beneficial tax structures. Additionally, the pre-elimination disclosure may not be reflective of an entity's global operations and income tax footprint. We suggest instead to require companies to disclose the methods and assumptions made in preparing the pretax income disclosure. An alternative may be to allow entities to either use preelimination or postelimination as the basis for disclosure and require disclosure of the method the entity is using.

Question 5: Would a proposed amendment to require disaggregation of income tax expense (or benefit) from continuing operations by major tax jurisdiction be operable? Would such a proposed amendment result in decision-useful information about income taxes? Why or why not?

We do not believe this requirement would be operable without additional guidance provided on the benchmark that should be used when evaluating "major." Would a U.S. parent with significant U.S. operations with a full valuation allowance on U.S. DTAs disclose the United States as a major jurisdiction even if the U.S. tax expense for the year was zero? In other words, what metric would a "major" jurisdiction be based upon: pretax income or loss, tax expense or benefit, net assets, or some other metric?

Although we are generally refraining from providing a user view in our response, we question whether this provides meaningful information, especially for entities in a full valuation allowance where income tax expense may not be overly meaningful on the whole, or for entities with tax-beneficial structures where tax expense is minimal even though the entity's presence in a jurisdiction may be significant.

Question 6: The proposed amendments would modify the existing rate reconciliation requirement for public business entities to be consistent with SEC Regulation S-X 210.4-08(h). That regulation requires separate disclosure for any reconciling item that amounts to more than 5 percent of the amount computed by multiplying the income before tax by the applicable statutory federal income tax rate. Should the Board consider a threshold that is different than 5 percent? If so, please recommend a different threshold and give the basis for your recommendation.

The scope of the proposed amendments is expanded from public entities as currently defined in ASC 740 to public business entities as defined in the Master Glossary. As such, this requirement would apply to preparers that meet the definition of a public business entity, but may not be required to file with the SEC. As such, we believe that using 5 percent of the expected tax expense (based on the statutory rate) may result in disclosure of many immaterial reconciling items, particularly given the 2017 reduction of the U.S. tax rate. In general, we agree with the notion of aligning SEC disclosures and US GAAP requirements; however, a bright-line requirement may not allow a public business entity to appropriately determine what information is material, relevant, and decision-useful.

If this concept is retained, the guidance should be consistent with existing SEC guidance or not specify a threshold at all.

Question 7: Are there any other disclosures that should be required by Topic 740 on the basis of the concepts in Chapter 8 of Concepts Statement 8, as a result of the Tax Cuts and Jobs Act, or for other reasons? Please explain why.

None noted.

Question 8: Are there any disclosure requirements that should be removed on the basis of the concepts in Chapter 8, as a result of the Tax Cuts and Jobs Act, or for other reasons? Please explain why.

None identified.

Question 9: The proposed amendments would replace the term public entity in Topic 740 with the term public business entity as defined in the Master Glossary of the Codification. Do you agree with the change in scope? If not, please describe why.

We agree with the change in scope to change the term public entity as defined in Topic 740 to public business entity as defined in the Master Glossary.

Question 10: Should the proposed disclosures be required only for the reporting year in which the requirements are effective and thereafter or should prior periods be restated in the year in which the requirements are effective? Please explain why.

We suggest requiring prospective application in the reporting year the requirements are effective with an option for retrospective application at the preparer's discretion. This would allow a preparer to choose prospective or retrospective using their judgment considering their financial statement users' needs and information available.

Question 11: How much time would be needed to implement the proposed amendments? Should the amount of time needed to implement the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities? Should early adoption be permitted? Please explain why.

For public business entities, we note that even though several of these requirements are consistent with current SEC regulations, not all public business entities as defined in the Master Glossary are SEC filers. As such, we believe that these entities may require more time to implement since this information previously was not required to be disclosed. In addition, we believe the five-year carryforward table with valuation allowance and pretax income before intra-entity eliminations requirements will require a significant amount of time for all public business entities regardless of whether they are an SEC registrant.

Lastly, we support allowing early adoption.