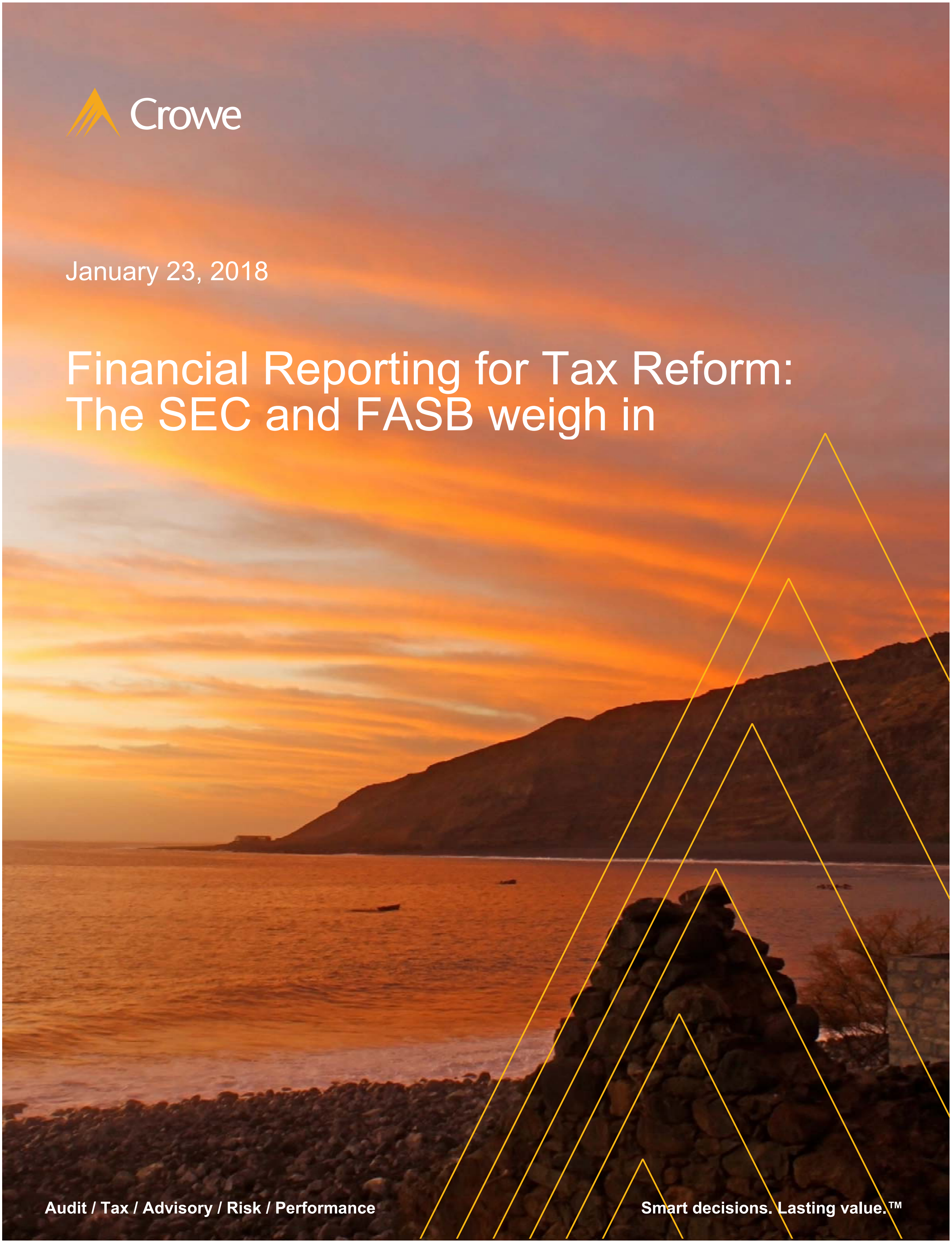

Crowe

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Financial Reporting for Tax Reform: The SEC and FASB weigh in

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President Donald Trump signed into law H.R. 1, commonly referred to as the *Tax Cuts and Jobs Act*, which could have significant income tax accounting implications for entities. Under U.S. generally accepted accounting principles (GAAP), entities are required to account for the effects of this change in the period of enactment, which was Dec. 22, 2017.

Acknowledging the possible financial reporting implications, the Securities and Exchange Commission (SEC) and the Financial Accounting Standards Board (FASB) have been fielding implementation questions and providing guidance. The SEC issued guidance on Dec. 22, 2017, and the FASB addressed six implementation questions at its meeting on Jan. 10, 2018. Most recently, the FASB's Emerging Issues Task Force (EITF) discussed drafts of the FASB Staff Q&As on various implementation questions at its Jan. 18, 2018, meeting.

Addressing the Uncertainty

The combination of H.R. 1 and accompanying conference report is in excess of 1,100 pages. Given its magnitude, evaluating tax law changes and accompanying financial reporting impacts will take time for some entities, particularly those with foreign operations. The SEC provided guidance to registrants on how to address the unknown effects, and the FASB has clarified the SEC guidance also is available to private companies and not-for-profit entities.

SEC Registrants

On Dec. 22, 2017, the same day the law was enacted, the SEC's Office of the Chief Accountant (OCA) and Division of Corporation Finance (Corp Fin) staff issued interpretive guidance for public companies, auditors, and other stakeholders to consider as they contemplate the accounting impacts of the tax reform law and related disclosures to investors.

The staff expects entities to make a good faith effort to determine the financial reporting impact; however, it acknowledges the uncertainty. To that end, the staff guidance addresses the various levels of uncertainty in measuring the impact and how an issuer should evaluate those situations; it also provides a period of time, not to extend beyond one year, to refine provisional amounts.

The interpretive guidance includes a new SEC Staff Accounting Bulletin (SAB) and a new Compliance and Disclosure Interpretation (C&DI).

SAB 118

SAB No. 118 (codified in SAB Topic 5.EE) provides the following measurement model and disclosure considerations:

Measurement

The SAB addresses three categories of accounting for the effects of the act. In scenarios where an entity's measurement of accounting for changes in tax laws is:

- Complete (in whole or in part): The effects should be recorded in the reporting period.
- Incomplete, but can be reasonably estimated: The provisional effects (or changes in the provisional effects) should be recorded in the reporting period.
- Incomplete and cannot be reasonably estimated: The entity should not record provisional amounts based on the act and should continue to record the effects based on the tax laws that were in effect immediately prior to the act being enacted. For those income tax effects for which an entity is not able to determine a reasonable estimate, the entity should record the effects in the first reporting period in which a reasonable estimate can be determined.

The provisional amount should be adjusted during the measurement period "upon obtaining, preparing, or analyzing additional information about facts and circumstances that existed as of the enactment date that, if known, would have affected the income tax effects initially reported as provisional amounts."

Disclosures

Supplemental disclosures should be provided about the material financial reporting effects of the act for which the accounting is incomplete, including:

- Qualitative disclosure of the areas for which the accounting is incomplete
- Items recorded as provisional amounts
- Current or deferred tax amounts for which the income tax effects have not been completed
- Reasons for the incomplete accounting

- Additional information or analysis that still needs to occur, and other information relevant to why the registrant was not able to complete the accounting
- Nature and amount of measurement period adjustments recognized in the reporting period
- Effect of measurement period adjustments on the effective tax rate
- When the accounting for the income tax effects of the act is completed

C&DI

One open question was whether or not the impact of the tax effects would require a registrant to file a Form 8-K, "Current Report." The SEC answered the question with the interpretation, question 110.02 related to Item 2.06 ("Material Impairments") on Form 8-K, noting that remeasurement of a deferred tax asset (DTA) in order to incorporate the effects of the newly enacted tax rates or other provisions of the tax reform law is not an impairment under GAAP and, therefore, does not trigger a Form 8-K filing requirement.

The staff observed the act could have other financial statement implications, including whether it is more likely than not that the DTA will be realized, which would be an impairment under GAAP. However, if this amount is determined in connection with preparing the annual or interim financial statements, it may be disclosed in the next periodic filing. A Form 8-K would not be required.

If using the measurement period approach in SAB 118, the impairment, or a provisional amount with respect to that possible impairment, may be disclosed in the next periodic report (rather than in Form 8-K).

Private Entities and Not-for-Profit Entities

As already described, SAB 118 provides guidance on how preparers should evaluate situations of uncertainty, recognizing that it may take a period of time to determine all of the impacts. Recognizing such guidance might be helpful to private companies and not-for-profits, the FASB staff view is those entities may elect, but are not required, to apply the provisions of SAB 118 in their financial statements. In particular, private entities with more complex operations or complex federal income tax calculations may benefit from being able to elect to apply SAB 118 to their 2017 annual financial statements.

If a private company or a not-for-profit entity applies SAB 118, the FASB staff believe all relevant aspects of the SAB should be applied, including the financial statement disclosures listed in SAB 118, and the limitation of up to one year for measurement period adjustments.

The FASB Staff Q&A, "Topic 740, No. 1, Whether Private Companies and Not-for-Profit Entities Can Apply SAB 118," was issued on Jan. 12, 2018.

Implementation Questions

Reclassification of Disproportionate Tax Effects

The FASB received several requests, primarily from banks and insurers, requesting the FASB permit a reclassification from accumulated other comprehensive income (AOCI) to retained earnings for "stranded tax effects." Current GAAP requires deferred tax assets and liabilities to be adjusted for the effect of a change in tax laws or rates – and the effect is recorded in income from continuing operations in the reporting period that includes the enactment date of the change – which is the fourth quarter of 2017. For items presented in AOCI (for example, securities classified as available for sale (AFS)), the original tax effects are recorded in AOCI, but the adjustment to the related deferred tax assets or liabilities is recorded in earnings – thus leaving tax effects "stranded" in AOCI.

On Jan. 18, 2018, the FASB issued a proposed Accounting Standards Update (ASU), "Income Statement – Reporting Comprehensive Income (Topic 220), Reclassification of Certain Tax Effects From Accumulated Other Comprehensive Income," to require reclassification from AOCI to retained earnings.

The FASB decided to limit the reclassification only to the rate differential between the prior corporate tax rates and the new 21 percent corporate tax rate in H.R. 1.

The board proposes the following transition disclosures:

1. The nature and reason for the change in accounting principle
2. A description of the prior-period information that has been retrospectively adjusted
3. The effect of the change on affected financial statement line items

The amendments would be effective for fiscal years beginning after Dec. 15, 2018, and interim periods within those fiscal years. For calendar year-ends, the ASU would be effective for the first quarter of 2019. Early adoption would be permitted for periods for which financial statements have not yet been issued or have not yet been made available for issuance.

Comments are due Feb. 2, 2018. The FASB expects to issue a final ASU in February.

The board added a research project on the accounting for subsequent effects of changes in deferred tax liabilities and assets that were originally charged or credited directly to equity ("backwards tracing").

For Banks: Guidance From the Federal Banking Agencies

On Jan. 18, 2018, the federal banking agencies issued guidance, "Interagency Statement on Accounting and Reporting Implications of the New Tax Law." One of the key provisions addresses the reclassification. Recognizing the fourth-quarter call report is due Jan. 30, 2018, prior to issuance of the final ASU, the agencies permit banks to record the tax effects (as proposed in the ASU for the various items reported net of deferred tax effect in AOCI) in their Dec. 31, 2017, call reports. In order to maintain consistency, banks electing to record in their fourth-quarter call report will need to early adopt the ASU for financial statement purposes.

Measurement of Alternative Minimum Tax (AMT) Credit Carryforwards

H.R. 1 repeals the AMT for corporations and provides a path to realize AMT credit carryforwards by allowing them to reduce regular tax liability. Any AMT credit carryforwards remaining after reducing regular taxes to zero are eligible for a 50 percent refund in 2018, 2019, and 2020 and a 100 percent refund in 2021. (Entities with AMT credits subject to limitation under Sec. 382 should consider the impact of those limitations on recovery of those credits.) Stakeholders questioned whether those amounts should be discounted.

The FASB staff view is these amounts should not be discounted. The staff noted that an entity should continue to disclose the amounts of AMT carryforward credits whether presented as a deferred tax asset or a tax receivable. The board concurred with the staff view.

The staff drafted a FASB Staff Q&A, which was discussed at the Jan. 18, 2018, EITF meeting. The staff noted it received minor wording changes. The final FASB Staff Q&A, "Topic 740, No. 3: Whether to Discount Alternative Minimum Tax Credits That Become Refundable," was issued on Jan. 22, 2018.

International

Base Erosion Anti-Abuse Tax (BEAT)

The BEAT is a tax that is paid if it is greater than an entity's regular tax liability. Stakeholders asked whether deferred tax assets and liabilities should be measured at the regular tax rate or the lower BEAT tax rate if the entity expects to owe BEAT in future years.

The FASB staff view is entities subject to BEAT in future years should record it as an incremental tax when paid (that is, as a period cost). As such, the entity should continue to record deferred tax assets and liabilities at the regular statutory rate, even if it expects to be subject to BEAT indefinitely. The board concurred with the staff view.

The staff drafted a FASB Staff Q&A, which was discussed at the Jan. 18, 2018, EITF meeting. The staff noted it received minor wording changes. The final FASB Staff Q&A, "Topic 740, No. 4: Accounting for the Base Erosion Anti-Abuse Tax," was issued on Jan. 22, 2018.

Global Intangible Low-Taxed Income (GILTI)

H.R. 1's GILTI provisions impose a tax on a U.S. shareholder's total net foreign income in excess of a deemed tangible return on its foreign business investments. Stakeholders have questioned if deferred tax assets and liabilities should be recognized for temporary basis differences expected to reverse as GILTI in future years or if the tax on GILTI should be included in the period in which it is incurred.

Based on outreach by the FASB staff, there is support for both views depending on the facts and circumstances present. As such, the staff's view is to allow a policy choice of whether to recognize deferred taxes for basis differences expected to reverse as GILTI in future years. Entities should disclose the policy elected. The board concurred with the staff view.

The staff plans to monitor this particular matter over the next few quarters to determine if any additional guidance is necessary.

The staff drafted a FASB Staff Q&A, which was discussed at the Jan. 18, 2018, EITF meeting. The staff noted it received minor wording changes. The final FASB Staff Q&A, "Topic 740, No. 5: Accounting for Global Intangible Low-Taxed Income," was issued on Jan. 22, 2018.

Deemed Repatriation

H.R. 1 taxes entities on undistributed and previously untaxed post-1986 foreign earnings and profits. Given the deemed repatriation tax may be paid over an eight-year period, stakeholders questioned whether the liability should be discounted.

The FASB staff view is the tax liability recorded for the deemed repatriation of foreign earnings and profits, which can optionally be paid over eight years, should not be discounted. The board concurred with the staff view.

The staff drafted a FASB Staff Q&A, which was discussed at the Jan. 18, 2018, EITF meeting. The staff noted it received minor wording changes. The final FASB Staff Q&A, "Topic 740, No. 2: Whether to Discount the Tax Liability on the Deemed Repatriation," was issued on Jan. 22, 2018.

Learn More

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