Accounting for Income Taxes Bulletin

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About this Publication

This publication is issued by KPMG's Accounting for Income Taxes group in Washington National Tax to highlight developments and other items of interest to professionals involved with accounting for income taxes matters.

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Featured items

Simplifications to accounting for income taxes

As part of the Financial Accounting Standards Board's (FASB or the Board) simplification initiative, Accounting Standards Update (ASU) No. 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*, was issued in December 2019. The objective of this element of the initiative is to simplify the accounting for income taxes by removing certain exceptions to general principles in ASC 740 and by clarifying and amending guidance that already exists within US generally accepted accounting principles (US GAAP). Upon adoption, the changes in the ASU include the following:

- Eliminates the exception to intraperiod tax allocation when there is a loss from continuing operations and income outside of continuing operations
- Eliminates exceptions that apply when an investment changes from an equity method investment to a subsidiary or from a subsidiary to an equity method investment
- Eliminates the exception to the general methodology for calculating income taxes in an interim period when a year-to-date loss exceeds the anticipated loss for the year
- Requires an entity recognize a franchise (or similar) tax that is partially based on income in accordance with ASC 740 and account for any incremental amount as a non-income-based tax

- Requires an entity evaluate when a step up in the tax basis of goodwill should be considered part of a business combination
- Specifies that an entity is not required to allocate the consolidated amount of current and deferred tax expense to a legal entity that is not subject to tax in its separate financial statements but may elect to do so for a disregarded entity
- Requires an entity reflect the effect of an enacted change in tax laws or rates in the annual effective tax rate computation in the interim period that includes the enactment date
- Makes minor Codification improvements for income taxes related to employee stock ownership plans and investments in qualified affordable housing projects

The amendments are effective for public business entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020, and for all other entities for fiscal years beginning after December 15, 2021, and interim periods within fiscal years beginning after December 15, 2022. Early adoption of the amendments is permitted for periods for which financial statements have not yet been issued or made available for issuance, including early adoption in an interim period.

Refer to the Defining Issues for further information on the changes included in the ASU.

Updates to KPMG's Accounting for Income Taxes handbook

KPMG recently updated its Accounting for Income Taxes Handbook to add interpretive guidance on several income tax matters and forthcoming ASUs.

The updates in the October 2019 edition include, but are not limited to, the following:

- Updates to interpretive guidance on changes in tax status in connection with transactions with shareholders, business combinations and common control mergers
- Additional guidance on intercorporate tax allocation and presentation of deferred tax assets and liabilities in separate financial statements
- Additional guidance on evaluating changes in estimates and error corrections
- Updates for the forthcoming ASU on simplifying the accounting for income taxes
- Removal of Appendix D: Tax Reform Supplement

The publication includes a brief summary of the significant revisions since the May 2019 edition.

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Updates on accounting matters

AICPA Q&A on section 163(j)

In December 2019, the AICPA posted a Technical Question and Answer (TQA), Q&A Section 3300.01 and .02, *Revised Section 163(j) Limitation and Evaluation of the Realizability of a Section 163(j) Carryforward*, in response to an inquiry on assessing the realizability of existing deferred tax assets related to disallowed interest carryforwards under section 163(j), when an entity has reversing deferred tax liabilities and expects to generate future disallowed interest deductions. The TQA indicated that entities should consider the sources of income listed in ASC 740-10-30-18 incrementally to determine the amount of valuation allowance needed, if any. Further, ASC 740 states that if one or more sources of income are sufficient to support a conclusion that a valuation allowance is not necessary, other sources need not be considered. As such, if the reversal of existing taxable temporary differences is sufficient to support the realization of deferred tax assets, then there is no need to consider remaining sources of taxable income.

Conversely, if the reversal of existing taxable temporary differences is not sufficient to realize existing deferred tax assets, then additional sources of taxable income, such as projections of future taxable income exclusive of reversing temporary differences and carryforwards, would be considered. In these situations, future limitations, such as those arising from section 163(j), would be relevant and need to be considered in the projections in assessing the realizability of any remaining deferred tax assets. Ultimately, future income projections may represent an incremental source of taxable income for purposes of realizing those deferred tax assets but would not affect the assessment of deferred tax assets already deemed realizable as a result of the reversal of existing taxable temporary differences.

Critical audit matters (CAM) update

The Public Company Accounting Oversight Board adopted an auditing standard that requires auditors to include in the auditor's report a discussion of the critical audit matters (CAMs), which are intended to make the auditors' report more informative and relevant for the financial statement users. The communication of CAMs is effective for audits of fiscal years ending on or after June 30, 2019 for large accelerated filers, and audits of fiscal years ending on or after December 15, 2020 for all other companies.

CAMs are those matters arising from the financial statement audit that were communicated or required to be communicated to the audit committee related to material accounts or disclosures and involved especially challenging, subjective, or complex auditor judgment. The auditors' report will be tailored to identify the CAM, describe the principal considerations that led the auditor to determine the matter is a CAM and how the auditor addressed the CAM in the audit. Auditors are required to provide a draft of the auditor's report to, and discuss it with, the audit committee. In most situations, the auditor should be able draft the CAMs well in advance of the completion of the audit.

ESMA enforcement priorities for 2019

The European regulator, European Securities and Markets Authorities (ESMA), has issued a statement highlighting the common areas that European national securities regulators will be focusing on when reviewing listed companies' 2019 annual reports in order to promote the consistent application of IFRS Standards and other EU-specific reporting requirements. Income taxes are regularly featured on ESMA's agenda with specific areas of focus related to IAS 12, *Income Taxes*, including deferred tax assets on unused tax losses, tax consequences of dividends, and uncertain tax treatments under IFRIC 23. Refer to the KPMG International Standards Group (ISG) article for additional information.

IFRS updates

KPMG LLP has released the following update that may impact tax professionals working on accounting for income taxes matters under International Financial Reporting Standards (IFRS).

- KPMG's ISG has published *Guides to IFRS financial statements*, based on standards in issuance as of August 31, 2019 that are required to be applied by a company in accordance with IFRS with annual reporting period beginning on January 1, 2019. The Guides include annual illustrative disclosures and a companion annual disclosure checklist and are available.

KPMG's DPP quarterly releases

KPMG's DPP published the following accounting and financial reporting developments releases:

- Quarterly Outlook – December 2019

Remember recent pronouncements

Professionals should be mindful of certain recently updated US GAAP standards, listed by order of required application.

Updated Standard	Brief Description of Standard	Public Business Entities Effective Date	Other Entities Effective Date
ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities	The evaluation of a valuation allowance on deferred tax assets related to available for sale securities is performed along with the entity's other deferred tax assets	Fiscal years beginning after December 15, 2017, including interim periods within those fiscal years	Fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019
ASU 2016-16, Intra-Entity Transfers of Assets Other Than Inventory	Requires an entity to recognize the income tax consequences of an intra-entity transfer of assets other than a transfer of inventory, when the transaction occurs	Annual reporting periods, including interim reporting periods in those annual reporting periods, beginning after December 15, 2017	Annual reporting periods beginning after December 15, 2018, and interim reporting periods within annual reporting periods beginning after December 15, 2019
ASU 2017-15, Codification Improvements to Topic 995, U.S. Steamship Entities	Eliminates an exception for steamship entities on the recognition of deferred taxes related to certain statutory reserve deposits	Fiscal years and first interim periods beginning after December 15, 2018.	Fiscal years and first interim periods beginning after December 15, 2018.
ASU 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income	Requires disclosure of an entity's policy for releasing stranded tax effects and allows entities to elect to reclassify certain stranded tax effects from AOCI to retained earnings	Fiscal years beginning after December 15, 2018, and interim periods within those fiscal years	Fiscal years beginning after December 15, 2018, and interim periods within those fiscal years
ASU 2018-09, Codification Improvements	Clarifies, corrects errors in, and makes improvements to several income taxes related matters	Generally, fiscal years beginning after December 15, 2018	Generally, fiscal years beginning after December 15, 2019

ASU 2017-04, Simplifying the Test for Goodwill Impairment	Provides guidance, amongst others, on the income tax effects from tax deductible goodwill when measuring goodwill impairment loss	Annual and interim impairment tests for periods beginning after December 15, 2019 for SEC filers, and after December 15, 2020 for other public business entities	Annual and interim impairment tests for periods beginning after December 15, 2021
ASU 2019-12, Simplifying the Accounting for Income Taxes	Removes specific exceptions to the general principles of ASC 740 and improves financial statement preparers' application of income tax-related guidance and simplifies GAAP for certain income tax items	Fiscal years beginning after December 15, 2020, and interim periods within those fiscal years	Fiscal years beginning after December 15, 2021, and interim periods within fiscal years beginning after December 15, 2022

Professionals should be mindful of the recently updated IFRS standards.

Updated Standard	Brief Description of Standard	Effective Date
IFRIC 23: Uncertainty over Income Tax Treatments	Addresses how to reflect uncertainty in accounting for income taxes	Annual periods beginning on or after January 1, 2019
Annual Improvements to IFRS Standards 2015-2017 Cycle	Clarifies recognition of income tax consequences of dividends, including payments on financial instruments	Annual periods beginning on or after January 1, 2019

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On the horizon

Proposed ASU on codification improvements

On November 26, 2019, the FASB issued a proposed ASU, *Codification Improvements*, to further clarify and conform the Codification or correct unintended consequences that are not expected to have a significant effect on current accounting practices. The amendments in this proposed ASU would effect a wide variety of Codification Topics, including, but not limited to:

- Adding and moving guidance to the disclosure section of Codification that already exists in other areas of Codification around income tax expense (benefit) in other comprehensive income,
- Removing outdated terminology around income taxes, and
- Correcting references and adding headings to the income tax related matters in ASC 830.

No transition guidance is proposed as the changes are not expected to change current practice. The comment period for the exposure draft ended December 26, 2019 and the project is currently in the redeliberations stage. Refer to the comment letter to learn more about KPMG's feedback.

FASB projects

The Board issued a revised proposed ASU in March 2019 on its disclosure framework project related to income taxes, which is currently in the exposure draft redeliberations stage.

The Board's disclosures by business entities about government assistance project is in the exposure draft redeliberations stage.

The Board continues its project on backwards tracing to consider whether changes should be made to the prohibition on backwards tracing and may consider alternatives to backwards tracing. The project is in the research stage.

Multiple tax consequences of recovering an asset under IFRS

The IFRS Interpretations Committee (the Committee) received a submission regarding IAS 12, which requested guidance on how an entity should account for deferred taxes when the recovery of the carrying amount of an asset gives rise to multiple tax consequences. In some tax jurisdictions, the manner in which an entity recovers the carrying amount of an asset determines the tax consequences that follow from such recovery. For example, the manner of recovery of an asset (either through use or through sale) may affect the applicable tax rates and the tax base attributed to that asset. Paragraph 51 of IAS 12 requires an entity to measure deferred tax assets and liabilities reflecting the tax consequences that would follow from the manner in which the entity expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

The submission describes a situation in which the expected manner of recovery of an asset's carrying amount gives rise to two distinct tax consequences, which arise under two different tax regimes, even though there is only one expected manner of recovery. The submitter asks how an entity determines the tax base of the asset and, consequently, how it accounts for deferred tax in this situation. Based on its analysis, the Committee tentatively concluded that, in the fact pattern described in the submission, IAS 12 requires an entity to reflect separately the distinct tax consequences of recovering the asset under both tax regimes.

Further, the Committee tentatively decided not to add this matter to its standard-setting agenda, and instead published a draft agenda decision that outlines how the existing applicable requirements in IAS 12 apply to the fact pattern described in the submission. The tentative agenda decision is open for comment through February 14, 2019. See the IASB project page for additional information.

KPMG comments on the IASB exposure draft on amendments to IAS 12 regarding the initial recognition exemption

KPMG's ISG submitted a response to the IASB's exposure draft, *Deferred Tax related to Assets and Liabilities arising from a Single Transaction - Proposed amendments to IAS 12*, which proposes to narrow the initial recognition exemption in IAS 12. KPMG believes that limiting the application of IAS 12's initial recognition exemption will improve comparability across IFRS financial statements. However, KPMG did note concerns about the clarity of the proposals and potential application issues. Refer to the comment letter to learn more about KPMG's feedback.

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Other items of interest

Section 987 Regulations

On December 6, 2019, the IRS issued Notice 2019-65, which further defers the applicability date of the 2016 regulations (and certain related and temporary regulations) as well as certain of the 2019 final regulations under section 987 by an additional year. Taxpayers should continue to consider the financial statement impact and tax implications when accounting for QBUs.

Refer to the KPMG Insights article for further information. A 2017 What's News in Tax article summarizes the current accounting for income taxes implications of the future adoption of the regulations.

Updated executive view: Up-C structures

KPMG has updated its Executive View on Up-C structures to include additional accounting considerations when determining how a company should present the noncontrolling interest of shares of the flow-through entity retained by the original owners in its financial statements.

Private business owners of a flow-through entity are often using an Up-C structure to conduct an initial public offering via a newly formed C Corporation which ultimately holds only an equity interest in the flow-through entity. KPMG's Executive View (the View) Unlocking Value Beyond a Traditional IPO describes a typical Up-C structure and highlights relevant accounting considerations and SEC filing requirements.

KPMG learning – executive education self-study courses

KPMG offers digital self-studies, which are mobile-friendly and easily accessible at the learner's convenience. Our CPE-eligible curriculum cover current and emerging technical accounting topics, including accounting for income taxes, to build skills and confidence in a variety of areas of accounting. View the catalog of KPMG's digital self-studies.

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Resources

- KPMG's Accounting for Income Taxes Publication
- Financial Reporting View

- TaxNewsFlash
- Chief Tax Officer Insights
- KPMG Executive Education
- KPMG U.S.
- Insights into IFRS
- IFRS compared to U.S. GAAP

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