Accounting for Income Taxes Bulletin

Issue 13 | April 01, 2020

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.

Featured items

Impact of CARES Act on accounting for income taxes

In response to the economic impacts of the COVID-19 outbreak, President Trump signed the Coronavirus Aid, Relief, and Economic Security Act (CARES Act or the Act) into law on March 27, 2020. The Act provides relief to corporate tax payers by permitting a five year carryback of 2018-2020 net operating losses (NOLs), removing the 80 percent limitation on the carryback of 2018-2020 NOLs, increasing the 30 percent limitation on interest expense deductibility to 50 percent of adjusted taxable income for 2019 and 2020, and accelerates available refunds for minimum tax credit carryforwards, amongst other provisions. These changes in tax law lead to a number of accounting for income taxes considerations.

The tax effects of retroactive changes in tax laws or rates on income taxes receivable (payable) for a prior year are recognized in income tax expense (benefit) from continuing operations as of the date of enactment. To the extent a retroactive change impacts income taxes receivable (payable) of the current year, such impacts are recognized in the estimated annual effective tax rate beginning in the interim period which includes the enactment date.

Deferred tax assets (liabilities) are remeasured to reflect the effects of enacted changes in tax laws as of the date of enactment. The impact of the remeasurement, if any, is reflected entirely within the interim period that includes the enactment date and allocated directly to income tax expense (benefit) from continuing operations.

Net operating loss carrybacks

Companies carrying back losses from the 2018 to 2020 tax years will need to consider the impact of tax rates in the carryback year to which the losses are applied. For example, a NOL from 2018 that would have previously created a deferred tax asset measured at 21 percent, under the Act could be carried back to offset taxable income from 2013 that would have been taxed at a 35 percent federal income tax rate. As such, the refund receivable would be measured at the 35 percent rate applicable to the carryback year.

Revisions on the limitations on interest carryforwards

The increase in the limitation on the deductibility of interest expense may reduce interest carryforwards generated in these tax years and the related deferred tax assets. Consequently, existing valuation allowance judgments should be reassessed to determine the realizability of the remaining deferred tax assets. Companies may need to revise the scheduling of the reversal of temporary differences to appropriately determining the total amount of interest character deferred tax assets supported by reversing taxable temporary differences.

Alternative minimum tax

As remaining minimum tax credit carryforwards will be realized either as a reduction of income taxes payable or as a refundable amount, existing deferred tax assets related to minimum tax credit carryforwards may be reversed and an income taxes receivable recognized. Any income taxes receivable recognized is presented as a current receivable as expected timing of receipt is anticipated to be within 12 months or the operating cycle. If an entity previously recognized a noncurrent receivable for the portion of the minimum tax credit carryforward expected to be refunded in 2021, a reclassification should be made from noncurrent to current.

Summary

As noted above, this discussion highlights selective common areas of accounting for income taxes that may be impacted by the new laws included in the Act, but it is not all inclusive. An entity's specific facts and circumstances should be assessed in determining the accounting for income taxes impact upon the March 27, 2020 enactment date.

Refer to the Tax News Flash Tax provisions in the CARES Act (COVID-19 "phase 3" response): Preliminary analysis and observations for additional details.

Accounting for income taxes considerations of negative economic conditions

Negative economic conditions may have significant effects on many aspects of an entity's accounting and reporting of income taxes. In light of the evolving impact of current economic conditions on the US and global economies, below are some accounting for income taxes considerations to keep in mind when discussing potential financial reporting consequences.

Interim period considerations

If the annual effective tax rate cannot be reliably estimated, the actual effective tax rate for the year-to-date period may be the best estimate of the annual effective tax rate. Similarly, if an entity is unable to reliably estimate individual items within ordinary income or loss, the tax expense (benefit) related to those items would be recognized in the interim period in which the items are reported. If an entity is unable to estimate an annual effective tax rate in a foreign jurisdiction or is otherwise unable to make a reliable estimate of its ordinary income in a jurisdiction, the entity excludes that jurisdiction from its estimated annual effective tax rate. Additionally, entities should consider whether tax benefits recognized in interim periods are limited due to the restrictions that apply when interim period losses exceed the anticipated ordinary loss for the year prior to the adoption of ASU 2019-12. See Section 10, *Interim Period Tax Calculations,* of KPMG's Accounting for Income Taxes publication for additional considerations.

Valuation allowances

Negative economic conditions may have significant effects on an entity's assessment of the realizability of its deferred tax assets, including whether reliance may be placed on estimates of future taxable income. Whether a valuation allowance is recorded may affect the interaction between intraperiod tax allocation and changes in a valuation allowance. Further, a valuation allowance may affect the determination of the carrying amount of a reporting unit when evaluating impairment of goodwill. Companies may also disclose the significant assumptions leading to a conclusion that deferred tax assets would be realized and therefore a valuation allowance is not required for all or a portion of the deferred tax assets and the potential for those assumptions changing. Refer to Section 4, *Valuation of Deferred Tax Assets,* of KPMG's Accounting for Income Taxes publication for additional detail.

Indefinite reinvestment assertion

As a reminder, the transition of the United States to a hybrid territorial system did not eliminate the need for a US taxpayer to consider its assertion regarding the indefinite reinvestment of investments in foreign subsidiaries. A US taxpayer should continue to evaluate its ability to assert indefinite reinvestment to avoid recognizing a deferred tax liability for items that trigger a tax effect on repatriation (including, but not limited to, section 986(c) currency gains on previously taxed earnings and profits (PTEP), section 965(b) PTEP without tax basis, foreign withholding taxes, and state income taxes).

As economic conditions change or as new transactions are planned as a result of changing economic conditions, an entity may reevaluate its global cash needs and revise its plans for repatriating or reinvesting foreign earnings. Changes in repatriation plans should be evaluated based on the specific facts and circumstances to determine how those changes affect the recognition and measurement of income tax liabilities and whether those changes in plans affect an entity's ongoing assertions related to the indefinite reinvestment of basis differences.

A change of plans related to the indefinite reinvestment of basis differences caused by a change in previously unforeseen circumstances generally would not raise questions about the original application of the exception and would not necessarily taint the continuing application of the indefinite reinvestment assertion to the remaining taxable outside basis difference or future earnings. A one-time plan to repatriate existing funds from the foreign subsidiary that will result in recognizing previously unrecognized taxes in the parent's tax jurisdiction would not prohibit applying the exception to the remaining undistributed earnings or basis difference if management has sufficient evidence of specific plans to continue reinvesting the foreign subsidiary's remaining undistributed earnings. In evaluating whether the entity's plans can support continued application of the exception, the entity should consider the facts and circumstances that caused the change in conditions, the likelihood of those facts and circumstances recurring, the entity's expected actions if those facts and circumstances were to recur, and its specific plans to continue reinvestment.

Refer to KPMG's recently issued Hot Topic for additional information. KPMG has a number of

resources that can assist professionals as they face the challenges of changing economic conditions, including the below webpages:

- Financial reporting impacts of coronavirus
- COVID 19: Insights on tax impacts
- COVID 19 | Financial reporting resource centre (IFRS)

Reminder on early adoption of ASU 2019-12

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).

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.

An entity that elects to early adopt the amendments in an interim period should reflect any adjustments as of the beginning of the annual period that includes that interim period of adoption. Additionally, an entity that elects early adoption must adopt all the amendments in the same period. In the period of adoption, an entity must disclose the nature of and reason for the change in accounting principle, the transition method, and a qualitative description of the financial statement line items affected by the change.

Entities are reminded that they have the option to early adopt the ASU and that Securities and Exchange Commission (SEC) registrants should disclose the date the registrant plans to adopt the standard. Refer to the Defining Issues for further information on the changes included in the ASU.

Brexit reminder

On January 31, 2020, the United Kingdom (UK) formally separated from the European Union (EU), referred throughout as Brexit. Immediately following Brexit, an 11-month transition period began during which the UK and EU must agree to the terms of its future relationship. Until the transition period ends on December 31, 2020, the UK will continue to follow all of the EU's rules and its trading relationships will remain the same. At that time, existing relationships, including tax treaties between the UK and the EU, will no longer be effective.

As reported in KPMG's Defining Issues No. 17-10, we believe companies should recognize in the financial statements the estimated changes to income tax accounts resulting from Brexit in the period that includes January 31, 2020 (the date that withdrawal occurred). Companies will need to determine what effect the expiration of the current tax treaties on December 31, 2020 will have on current and deferred income taxes. Those amounts due or expected to reverse after December 31, 2020 will need to be remeasured assuming the UK is no longer a member of the EU. If new treaties or arrangements are executed, companies will account for them in the reporting period(s) in which they are enacted. Professionals can find relevant guidance beginning in paragraph 5.008 in KPMG's Accounting for Income Taxes publication.

Updates on accounting matters

SEC comments on accounting for income taxes

A *What's News in Tax* article from the Accounting for Income Taxes group in Washington National Tax (WNT) provides examples of comments about accounting for income taxes recently issued by the US Securities and Exchange Commission to registrants. Recent comments from regulators and standard setters may help issuers identify areas for improvements in existing income taxes disclosures in order to provide more robust and relevant information to investors.

The selection of SEC comment letters specific to income taxes are provided to illustrate areas in which the SEC staff questioned whether the disclosures provided adequate insight for investors to understand a company's income taxes environment or when the SEC staff wanted a better understanding of the basis for management's judgments. The examples involve comments related to the effective tax rate reconciliation, valuation allowances, investments in subsidiaries, unrecognized tax benefits, changes in tax law, tax credits, and the adoption of new accounting standards.

KPMG's DPP quarterly releases

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

- Quarterly Outlook – March 2020

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 other than smaller reporting companies	Annual and interim impairment tests for periods beginning after December 15, 2022
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 certain 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

On the Horizon

FASB discusses income taxes disclosures

The Board discussed comment letters received on its revised proposed ASU, *Income Taxes (Topic 740): Disclosure Framework—Changes to the Disclosure Requirements for Income Taxes* during a February meeting. The proposed ASU was issued as part of the Board's project Disclosure Review: Income Taxes. The discussion focused on whether additional disaggregation of items, including pretax income, income tax expense and income taxes paid, would provide more useful information to investors and how much information should be disclosed, amongst other topics.

The Board directed the staff to perform research and additional outreach on potential alternatives to disclose certain disaggregated income taxes information and to perform additional research on other proposed amendments. It was suggested that a workshop with preparers, users, and other interested parties should occur as way to bridge the gap on how much disaggregated information should be disclosed. The staff will present the findings to the Board at a later date.

FASB projects

The Board's codification improvements project that includes moving guidance, removing outdated guidance and correcting references and headings is 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.

IFRIC discusses deferred tax related to a subsidiary's undistributed profits

During a recent meeting, the IFRS Interpretations Committee (IFRIC or the Committee) discussed accounting for deferred tax related to an investment in a subsidiary when the subsidiary operates in a jurisdiction in which profits are taxable to the subsidiary only when distributed. In the fact pattern discussed, the conditions for applying the exception from recognizing a deferred tax liability associated with investments in subsidiaries were not satisfied, and the entity expected to recover the investment through distributions.

The Committee observed that the future taxation to the subsidiary creates a taxable temporary difference associated with the entity's investment in the subsidiary and tentatively concluded that the entity recognizes a deferred tax liability for that taxable temporary difference.

The Committee also observed that guidance around recognizing the income tax consequences of dividends when it recognizes a liability to pay a dividend and guidance around measuring deferred taxes at the undistributed rate does not apply in the fact pattern described.

As the principles and requirements in IAS 12 provide an adequate basis for an entity to account for deferred tax in the fact pattern, the Committee tentatively decided not to add this item to its standard-setting agenda.

KPMG comments on multiple tax consequences of recovering an asset

KPMG has commented on the IFRIC's tentative agenda decision on multiple tax consequences of recovering an asset. KPMG disagreed with the Committee that IAS 12 is clear about whether there can be more than one tax base for a single asset or liability. KPMG also disagreed that the tax base of the asset in the scenario was not immediately apparent and urged the Committee to carry out a broader analysis of the issue.

IFRIC projects

The International Accounting Standards Board (IASB) project on Deferred Tax Related to Assets and Liabilities Arising from a Single Transaction (Amendments to IAS 12) is currently in the exposure draft feedback stage.

Other Items of Interest

SEC proposes disclosures on payments to governments

The SEC has proposed rules on disclosing payments to foreign governments and the US federal government by extractive industry issuers that are required to file an annual report on Form 10-K, Form 20-F or Form 40-F. The proposed rules would require disclosure of payments made to any government, foreign (including national, state, or provincial) or US federal (excluding state or county), to further the commercial development of oil, natural gas or minerals, and which are not de minimis. Such payments include those associated with taxes.

KPMG learning – executive education live courses

The following Accounting for Income Taxes Executive Education classes will be offered:

— Las Vegas, Nevada – June 2 – 3, 2020

— Chicago, Illinois – June 22 – 23, 2020

— New York, New York – August 17 – 18, 2020

— Chicago, Illinois – September 24 – 25, 2020

This two-day seminar is designed to help participants understand and apply the income tax accounting guidance in ASC 740. It provides a conceptual foundation of accounting for income taxes. Relevant aspects of the new tax reform will be discussed throughout the seminar. This seminar explains how to reconcile differences between four sets of flows: cash flows, US GAAP income, taxable income, and more likely than not taxable income. It will also cover valuation allowances, unrecognized tax benefits, interim tax allocations, business combinations, and stock compensation.

Additionally, the following Advanced Accounting for Income Taxes Executive Education classes will be offered:

— Las Vegas, Nevada – June 4 – 5, 2020

— Chicago, Illinois – June 24 – 25, 2020

This two-day seminar looks beyond the fundamentals of ASC 740 to examine some of the major implementation challenges that arise in applying the standard. It covers complex areas such as quarterly disclosures, intercompany transactions and equity investments.

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.

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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