KPMG

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.

Featured items

Accounting for income taxes considerations of COVID-19

The COVID-19 outbreak is having a significant impact on global markets driven by a number of factors, many of which are negatively impacting companies' financial performance. These effects, and a company's actions in responding, may also impact a company's accounting for income taxes. Below are some possible accounting for income taxes considerations arising from the economic and financial markets effects of COVID-19.

Accounting for income taxes impact of coronavirus

KPMG has updated its guidance that addresses possible impacts to companies' accounting for income taxes from the economic effects of the pandemic. This update includes guidance on the effects of forecasted cumulative losses in recent years and going concern disclosures and how such matters would impact the valuation allowance assessment.

ASC 740 requires companies to consider all available evidence in determining whether it is more likely than not that all or some of its deferred tax assets will not be realized. The following are reminders of items that may be particularly relevant in light of COVID-19:

- A cumulative loss in recent years is a significant piece of negative evidence that is difficult to overcome when assessing the need for a valuation allowance. We believe a company that is not in a cumulative loss, but expects to be in the near term (due to the forecast of near-term losses), should consider that condition to also be a significant piece of negative evidence when evaluating the need for a valuation allowance.
- Substantial doubt about a company's ability to continue as going concern (as a result of covenant violations, or negative actual or forecasted operating results, amongst other relevant events) also raises doubt about the ability to generate taxable income. As a result, we believe substantial doubt disclosure generally necessitates a valuation allowance for all deferred tax assets that are not realizable through the reversal of existing taxable temporary differences or taxable income in carryback years.
- Sections 4 and 10 of KPMG's Handbook, Accounting for Income Taxes, discuss valuation allowances and changes in valuation allowances in interim periods, respectively, in additional detail.

Additional interim reporting considerations

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 for interim periods ending on or around June 30, 2020. Section 10 of KPMG's Handbook, Accounting for Income Taxes, discusses interim period tax calculations in additional detail.

Interim period losses

Companies that are experiencing unexpected ordinary losses due to COVID-19 may need to adjust the estimated annual effective tax rate, limit year-to-date tax benefits, or both, if the year-to-date ordinary loss exceeds the ordinary loss expected for the full fiscal year.

A company recognizes the tax effects of losses that arise in interim periods only if the benefits are more

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likely than not to be realized during the current year or recognizable as an asset at the end of the year. Further, prior to the adoption of Accounting Standards Update (ASU) 2019-12, if a company's year-to-date ordinary loss exceeds its expected annual ordinary loss, the year-to-date tax benefit for the interim loss is limited to the amount that would be recognizable if the year-to-date loss was the expected annual loss.

Interim period losses in only certain tax jurisdictions
Multinational companies may be experiencing losses due to COVID-19 in only some tax jurisdictions and may need to estimate a separate annual effective tax rate for those jurisdictions. A company subject to income taxes in multiple tax jurisdictions generally computes one overall annual effective tax rate. However, the ordinary loss and the related tax effect for a tax jurisdiction is excluded from its overall estimated annual effective tax rate if that jurisdiction experiences a year-to-date loss or anticipates an annual loss, for which no tax benefit can be recognized.

A separate estimated annual effective tax rate is computed for that jurisdiction and applied to the respective ordinary income.

Inability to make reliable estimates
Companies that are experiencing near break-even operations due to COVID-19 may conclude that they cannot reliably estimate the annual effective tax rate. If a company is unable to reliably estimate its annual effective tax rate, the actual effective tax rate for the year-to-date period may be used as the best estimate of the annual effective tax rate.

Alternatively, if a company is unable to reliably estimate individual items in consolidated ordinary income or the related income tax expense or benefit, the tax effect of those items should be recognized in the interim period in which the items are reported.

Goodwill impairments
The economic impact of COVID-19 increases the likelihood that a company's goodwill may be impaired. There are some unique aspects in the evaluation as to whether goodwill is impaired and the measurement of the impairment that may include tax considerations.

To determine the carrying amount of a reporting unit used in the measurement of an impairment, a company will need to assign deferred tax assets and liabilities to reporting units and will need to complete its valuation allowance assessment as part of that assignment. To determine the fair value of a reporting unit used in the measurement of an impairment, a company must determine whether a hypothetical disposition would be taxable or nontaxable. A company determines the fair value of a reporting unit based on which tax structure is feasible, results in the highest economic value, including consideration of the related taxes generated by the sale, and is consistent with the view of market participants.

An entity may elect to allocate any impairment loss between first and second component financial statement goodwill using one of two acceptable methods. One method allocates the impairment loss first to second component goodwill to the extent available and then to first component goodwill. The other method allocates the impairment loss on a pro rata basis to first component and second component financial reporting goodwill. If the reporting unit impairs first component goodwill subsequent to the adoption of ASU 2017-04, the final impairment loss and related deferred tax consequences may need to be determined using the simultaneous equation to adjust the carrying amount of a reporting unit by the deferred tax consequences.

Section 10 of KPMG's Handbook, Accounting for Income Taxes, discusses goodwill impairment in additional detail.

Accounting and reporting impact of the CARES Act
KPMG has released guidance on the accounting and reporting impacts of the Coronavirus Aid, Relief, and Economic Security (CARES) Act. The most recent version of the publication contains new guidance and significant updates, as well as changes to the Act resulting from the Paycheck Protection Program (PPP) Flexibility Act of 2020.

KPMG Financial Reporting Podcast: CARES Act
Additionally, specialists from KPMG's Government Affairs and DPP participated on a podcast to discuss some of the financial reporting implications of the CARES Act on income taxes, financial instruments and more. The podcast includes a discussion of key tax provisions and how they affect the accounting for income taxes.

Summary
The potential global and economic impacts of the coronavirus evolve rapidly, and companies should continue to monitor the situation. Companies are encouraged to maintain close communications with the board of directors, external auditors, legal counsel and other service providers as the circumstances progress. Stay informed of the financial reporting impacts of coronavirus.

Updates to KPMG's Accounting for Income Taxes handbook
KPMG recently updated its handbook, Accounting for Income Taxes, to add interpretive guidance on several income tax matters.

The April 2020 edition incorporates:

— Updates for ASU 2019-12, Simplifying the Accounting for Income Taxes,

— Guidance on accounting for the income tax implications of Brexit and the CARES Act, and

— Additional guidance on accounting for asset acquisitions.

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

Updates on Accounting Matters

IFRIC® finalizes agenda decision on multiple tax consequences

On May 6, the IFRS Interpretations Committee (the Committee) issued a final agenda decision addressing the accounting for deferred tax in a scenario in which the recovery of the carrying amount of an asset gives rise to multiple tax consequences. 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 asked how an entity determines the tax base of the asset and, consequently, how it accounts for deferred tax in this situation. The Committee noted that the recovery of the asset's carrying amount gives rise to two distinct tax consequences therefore, an entity reflects separately these two distinct tax consequences and identifies two separate temporary differences. See the IASB project page for additional information.

IFRIC finalizes agenda decision on deferred tax related to a subsidiary's undistributed profits

The Committee met on June 16 and issued a final agenda decision addressing 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 noted that a taxable temporary difference associated with the entity's investment in the subsidiary exists and concluded that the entity recognizes a deferred tax liability for that taxable temporary difference. The Committee also concluded that the entity uses the distributed tax rate to measure the deferred tax liability related to its investment in the subsidiary.

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 decided not to add this item to its standard-setting agenda. See the IASB project page 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 International Standards Group has issued its 2020 interim illustrative disclosures and companion interim disclosure checklist to help companies prepare condensed consolidated interim IFRS financial statements.

KPMG's DPP quarterly releases

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

— Quarterly Outlook – June 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	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	Annual reporting periods beginning after December 15, 2018, and interim reporting periods within annual reporting periods beginning after December 15, 2019

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Updated Standard	Brief Description of Standard	Public Business Entities Effective Date	Other Entities Effective Date
ASU 2017-15, Codification Improvements to Topic 995, U.S. Steamship Entities	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	Fiscal years and first interim periods beginning after December 15, 2018.
ASU 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income	Fiscal years and first interim periods beginning after December 15, 2018.	Fiscal years and first interim periods beginning after December 15, 2018.	Fiscal years beginning after December 15, 2018, and interim periods within those fiscal years
ASU 2018-09, Codification Improvements	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	Generally, fiscal years beginning after December 15, 2019
ASU 2017-04, Simplifying the Test for Goodwill Impairment	Generally, fiscal years beginning after December 15, 2018	Generally, fiscal years beginning after December 15, 2019	Annual and interim impairment tests for periods beginning after December 15, 2022
ASU 2019-12, Simplifying the Accounting for Income Taxes	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	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 projects

TThe Financial Accounting Standards Board's (FASB or the Board) Disclosure Review: Income Taxes project continues to be in the revised exposure draft redeliberations stage after the Board directed the staff in February 2020 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.

FASB's codification improvements project that includes moving guidance, removing outdated guidance and correcting references and headings is in the exposure draft redeliberations stage.

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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.

IASB projects
The International Accounting Standards Board (IASB) has discussed feedback on its Deferred Tax Related to Assets and Liabilities Arising from a Single Transaction (Amendments to IAS 12) project and is currently deciding on project direction.

Other Items of Interest

U.S. Supreme Court will not hear Altera
On June 22, 2020, the U.S. Supreme Court denied certiorari in Altera v. Commissioner, thus leaving intact the U.S. Court of Appeals for the Ninth Circuits's 2019 decision upholding the validity of the treasury regulations that require related parties to share the costs of stock-based compensation as a component of their intangible development costs in cost sharing aggangements. An entity may need to evaluate whether the denial impacts its tax positions taken and expected to be taken using the recognition and measurement guidance in ASC 740.

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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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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.

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