



Letter of Comment No: /
File Reference: FSPFAS109

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Mr. Lawrence W. Smith
Director—Technical Application and Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: Proposed FASB Staff Position No. 109-a, Application of FASB Statement No. 109, *Accounting for Income Taxes*, for the Tax Deduction Provided to U.S. Based Manufacturers by the American Jobs Creation Act of 2004 (FSP No. 109-a)

Dear Mr. Smith:

We appreciate the opportunity to comment on the referenced document.

In summary, we support the issuance of the Exposure Draft as a final FASB Staff Position (FSP), subject to our concerns about Example 4 in Appendix A. The remainder of the following comments seeks to clarify the guidance in the Exposure Draft.

Paragraph 2. We recommend that the wage limitation on the domestic manufacturing deduction referred to in paragraph 4 be articulated in paragraph 2.

Appendix A, all examples. The inference from the examples is that an expectation of future taxable income is sufficient to conclude that a valuation allowance is not required for deferred tax assets. However, Statement 109 requires enterprises to consider all positive and negative evidence when forming a conclusion about the need for a valuation allowance for deferred tax assets. In some situations, negative evidence of the type illustrated in paragraph 23 of Statement 109 will exist and will cause enterprises to conclude, notwithstanding the expectation of future taxable income, a valuation allowance is required for some or all of their deferred tax assets. We recommend that language be added to the examples cautioning readers to consider all evidence when forming a conclusion about the need for a valuation allowance.

Appendix A, all examples. Assumed facts should include expected wages for 2005, as expected wages can limit the amount of the domestic manufacturing deduction.

Appendix A, all examples. The computation of the domestic manufacturing deduction should be based on the tax law. That is, wages paid should be part of the equation and the taxable income limitation should be taxable income less operating loss carryforwards utilized, not just taxable income. The domestic manufacturing deduction amounts shown in Examples 2, 3, and 4 are not the amounts, based on the assumed facts, which would be expected to be claimed on the 2005 tax return.

Appendix A, Example 4. Although not clear from Example, 4, we understand that the FASB staff believes, in the situation illustrated in Example 4, the valuation allowance for the operating loss carryforward deferred tax asset should be computed on a "with-and-without" basis (that is, what would be the enterprise's future tax expense with and without the operating loss carryforward). This approach has the effect of recognizing a valuation allowance today for the fact that the future utilization of the operating loss carryforward will reduce the future domestic manufacturing deduction. Based on the facts assumed in Example 4, it is our understanding that the 2005 domestic manufacturing deduction on the 2005 tax return would be \$90 (taxable income of \$21,000 less operating loss carryforward utilized of \$20,000 or \$1,000 times 9 percent) and that none of the \$20,000 operating loss carryforward would expire unused.

In our view, paragraph 232 of Statement 109 instructs enterprises to consider the effect of future special deductions on an enterprise's forecast of future taxable income (a \$90 reduction in future taxable income in Example 4) when an enterprise assesses the need for a valuation allowance for deferred tax assets. We do not believe that paragraph 232 provides for the computation of a hypothetical future special deduction (\$1,890 in Example 4) or that the result of using the hypothetical future deduction results in more understandable results (as drafted, Example 4 reflects an expectation that a portion of an operating loss will expire unused, which is not true, and reflects the benefit of a larger domestic manufacturing deduction in 2005 than will actually be realized on the 2005 tax return).

We would be pleased to discuss our comments with the FASB or the FASB staff at your convenience.

Very truly yours,

Financial Reporting Advisors, LLC