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Technical Director  
Financial Accounting Standards Board  
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File Reference 1215-001 – Accounting for Uncertain Tax Positions

Dear Director:

I have read the Proposed Interpretation, “Accounting for Uncertain Tax Positions – an interpretation of FASB Statement No. 109,” and offer the following comments.

The Pronouncement Should Be An Amendment Rather Than An Interpretation

While it may not change the substance of any final pronouncement, I believe this document would more properly be characterized as an amendment of Statement No. 109 rather than an interpretation. According to my dictionary, an interpretation “explains the meaning of” something. I do not recall these matters being deliberated during the Board meetings that led to the issuance of Statement 109. Why imply that the new pronouncement explains what the Board members meant 13 years ago when none of the Board members are presently with the FASB or have been consulted (as far as I know)?

## The Pronouncement Is Not Consistent With The Board's Simplification Goal

One of the FASB's three strategic goals at present is simplification. I applaud that goal but observe that this exposure draft as well as the two other recent ones on business combinations accounting and "minority interests" move in the opposite direction. The positions expressed by two Board members in their Alternative Views (paragraphs B46-B47) are that the "... proposed Interpretation (a) would be unduly complex, (and) (b) would prove difficult to apply in practice...." My impression of the required accounting would lead me to reach a similar conclusion, although the Board should seek more specific comments from corporations who try to apply the proposed guidance to factual situations. The approach suggested by the two dissenting Board members would seem to achieve very similar financial reporting results in most cases at considerably less application cost.

## The Board Should Better Explain Why Fair Value Is Not Appropriate

Based on the positions the Board has taken on most recent projects, I had expected the Board to propose that assets or liabilities recorded for uncertain tax positions be measured at fair value. Thus, I was pleasantly surprised to see that the Board has "... concluded that uncertainty should be addressed using a recognition threshold" (paragraph B10), and measurement of uncertain tax positions should be based on a best estimate approach. However, I am disappointed that the sole argument for using a best estimate is that fair value would be akin to discounting of deferred taxes and Statement 109 specifically prohibits that approach.

Paragraph B9 notes that, "Fair value measurement can yield representationally faithful financial reporting even when there is a low probability of realization associated with the item being measured. Some Board members believe that fair value measurement is the most reliable alternative that incorporates uncertainty about possible outcomes into the measurement attribute" (does "some" mean less than a majority?). These statements are hardly strong endorsements of the fair value approach that the Board has used in many recent pronouncements such as Statements 143 and 146, Interpretations 45 and 47, and the business combinations exposure draft.

As I have stated in responses to some of these proposals, I disagree with requiring fair value “when there is a low probability of realization associated with the item being measured.” Implementing the Board’s fair value approach to the situations covered by the pronouncements mentioned in the preceding paragraph will be difficult and costly for corporations and will produce information of very questionable relevance to users, in my opinion. In the case of the Uncertain Tax Positions ED, I believe the Board has a responsibility to more thoroughly explain its thinking on the pros and cons of measuring these items at fair value. It is too easy of an “out” to say that fair value was rejected only because of the prohibition against discounting. Would the Board have required fair value if not for that prohibition?

### The Unit Of Account And Two-Step Process Illustration Is Not Clear

Paragraphs A2 through A11 are subtitled, The Unit of Account and Two-Step Process. I assume that the term “two-step process” is meant to refer to the steps of (1) recognizing amounts for uncertain tax positions based on probability of being sustained on audit by taxing authorities, and (2) measuring any amounts recognized based on the best estimate of the amount that will be sustained. However, I don’t believe the term “two-step process” is used in the Interpretation section of the proposal, and the subsequent illustrative guidance might be clearer if it were.

Paragraph 9 of the proposed Interpretation states that the appropriate “unit of account” for a tax position is a judgment that has to be made in light of all of the facts and circumstances. Yet the example in this section provides no insights on how the Board decided that the appropriate unit of account was the individual research project – it is simply asserted in footnote 6. Why wouldn’t the company aggregate all of its research projects and use its average experience? To be useful as Guidance For Applying The Interpretation, the illustrations should explain why the Board members reached a particular conclusion, even though it is still only a hypothetical situation.

For the R&D credit examples in paragraphs A2 through A11, a tax benefit would be recognized in the examples only for the two projects where it is assumed that 90% of the benefit will be sustained upon tax audit. For the other projects, it seems probable that a benefit will also be realized, albeit for only 10% of the total cost. I would have assumed that this company would take the position that at least some benefit would arise from each of its

projects so that the recognition condition is met for all four projects. Then it would measure the benefit and record the larger amounts for the first two projects and the smaller amounts for the other two projects. The Board should further explain why recognizing a 10% benefit for the other two projects is somehow not permitted under paragraph 11.

In addition to not understanding the mechanics of the illustration, how realistic is it that a company would have four R&D projects with such disparate expected tax consequences? In reality, I suspect that most companies would be able to do no better than review experience in recent tax audits and assume that on average for all projects approximately x% of claimed benefits are disallowed upon examination.

### Disclosures

Paragraph 18 of the proposal states that, “An enterprise shall disclose loss contingencies relating to previously recognized tax positions in accordance with paragraphs 9-12 of Statement 5.” As you know, paragraph 9 of Statement 5 states, “Disclosure of the nature of an accrual made pursuant to the provision of paragraph 8, and in some circumstances the amount accrued, may be necessary for the financial statements not to be misleading.” It is my long-standing understanding that relatively few disclosures have been in practice in response to this sentence, most likely because the “may be necessary” words have been interpreted as more of an encouragement than a requirement.

By using the “shall disclose” wording in paragraph 18 of the proposal, I believe that some will interpret the Board’s intent to now require disclosure about recorded accruals pursuant to Statement 5 rather than the encouragement implied by “may be necessary.” Rather than allow such an ambiguous situation to occur, I suggest the Board modify the language in any final pronouncement to make its intent clear.

### Other Comments

One of the examples of facts or circumstances that would demonstrate a probable level of confidence is, “An unqualified *should prevail* tax opinion from a qualified expert for which all conditions are objectively verifiable (paragraph 9b).” I’m concerned that the “for which all conditions are objectively verifiable” language may not be commonly understood. If the

Board has already vetted this language with appropriate tax specialists, that should be mentioned in the Basis for Conclusions. If not, such evaluation should be performed. While I have seen only a handful of these tax opinions in practice, it is my impression that they are often based on professional judgments and not on “objective conditions.”

I agree that interest should be accrued on any amounts accrued for uncertain tax positions. The need to consider the accrual of a penalty would seem to suggest such an unreasonable tax position that the full amount of tax involved should be accrued.

Please let me know if you have any questions about my comments.

Sincerely,

Dennis R. Beresford