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LETTER OF COMMENT NO. /

Via email

Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: Invitation to Comment - Proposed FASB Staff Position No. FIN
48-a, *Definition of Settlement in FASB Interpretation No. 48*

Wells Fargo & Company (Wells Fargo) is a diversified financial services company with over \$482 billion in assets providing banking, insurance, investments, mortgage and consumer finance services. We appreciate the opportunity to comment on the issues being considered by the Board to provide guidance on whether a tax position is effectively settled for the purpose of recognizing previously unrecognized tax benefits.

We believe that the proposed FASB Staff Position (FSP) as currently drafted detrimentally constrains the use of professional judgment in determining whether an effective settlement of tax positions has occurred and will produce financial reporting results which are misleading.

Accounting for income taxes is an area of accounting that by its very complex nature requires the use of professional judgment. Income tax accounting is characterized by the evolution of tax issues, which are ultimately settled, individually or as a group, with a taxing authority either through a negotiation process or through litigation. Given the complex and often judgmental nature of the merits supporting tax issues, income tax accounting cannot rely too heavily on the application of detailed formulas or mechanical rules. Significant professional judgment always must be applied in this area of accounting to ensure that the final result best reflects the economic reality of the tax process. Therefore, we agree with the Board that there needs to be general principles, not formulaic rules, established in this area to ensure that consistency and financial statement integrity are maintained. The importance of professional judgment in accounting for complex and interwoven tax positions needs to be at the forefront of any final guidance.

The accounting principle at the very core of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48) is that tax positions should be recognized when it is more likely than not that the position will be realized. This concept equates to a probability of 51% or greater of a tax matter being realized. FIN 48 contemplates that significant professional judgment must be employed in evaluating tax positions to determine whether and when they meet this more likely than not recognition threshold. In its proposed FSP FIN 48-a, however, FASB apparently would establish a bright-line rule that a tax position cannot be recognized until the period in which all administrative reviews are finally completed. We are troubled by the inconsistency where it is appropriate to apply professional judgment to evaluate whether it is 51% or more probable that a tax position will be realized, but prohibit any use of judgment related to the outcome of an administrative review. We believe that the taxpayer should be allowed to apply the same professional judgment to all facts and circumstances surrounding a tax position, including an evaluation of the expected outcome of any administrative reviews, in determining whether a tax position meets the recognition threshold. If a taxpayer believes that the likelihood of an administrative review resulting in changes to a tax settlement already agreed to by a taxpayer and the taxing authority is remote, we believe the tax positions should be recognized currently and not when the administrative review is completed.

We are therefore concerned with the proposed requirement in amended paragraph 10A.a. that would require that the taxing authority must have completed any administrative reviews that it is required or expected to perform for the tax position in order for effective settlement to have occurred.

In significant IRS refund situations, the Joint Committee on Taxation is required to perform an administrative review. In its Notice dated July 3, 2003, entitled *The Role of the Joint Committee on Taxation Under Section 6405*, the Office of the Chief Counsel of the Internal Revenue Service (IRS) describes the role of the Committee as follows:

“The express language of section 6405(a) only prohibits the Service from issuing a refund or credit during the 30-day period following the report to the Joint Committee. This “report and wait” period requirement allows the Joint Committee a limited period of time to consider and comment on the Service’s proposed refund or credit. It does not give the Joint Committee the authority to approve, disapprove, authorize, or, in any way, prohibit the Service from taking whatever action the Service determines is appropriate. The determination whether to issue or deny a refund or credit rests solely with the Commissioner, regardless of the Joint Committee’s favorable or unfavorable views on the Service’s proposed action.”

And further:

“Although the Joint Committee does not have the authority to approve or disapprove refunds or credits, the report to the Joint Committee is not a perfunctory gesture. The legislative history underlying section 6405 and its

predecessors establishes that Congress wanted the Joint Committee to review refunds and credits to monitor whether the Service's administration of the Internal Revenue Code is consistent with Congressional intent and without favoritism. The Service values the views of the Joint Committee and carefully considers those views before making a final determination on a refund or settlement."

The role of the Joint Committee on Taxation is therefore to collect and review tax refund information (and to express its views to the IRS on any matter submitted).

Given the high rate of interest charged by the IRS on tax deficiencies, it is not unusual for a taxpayer to elect to pay taxes assessed by the IRS related to issues raised during examination and pursue a refund claim to limit its exposure to interest (and penalties). In these circumstances, should the taxpayer prevail, the final settlement would be in the form of a refund and would therefore be subject to administrative review by the Joint Committee on Taxation. Application of the Board's proposed guidance appears to require that all tax positions included in the period under review could not be considered effectively settled until the administrative review is completed. In refund situations, the Board has therefore removed the ability for the taxpayer to apply its professional judgment to determine whether an effective settlement has occurred. However, the taxpayer is in the same substantive position as if no payment was made. Its IRS audit team has completed its on-site examination. Disagreed issues have been identified, escalated and resolved with the IRS office of appeals. Yet the FIN 48 administrative review recognition criteria as currently drafted requires the form of the transaction (a refund claim) to trump its substance. The requirement to have completed the Joint Committee on Taxation's administrative review treats the same substantive resolution of contested matters with the IRS differently, depending solely on whether the agreement results in a refund or a deficiency. Inclusion of the administrative review requirement results in no material difference between "ultimately settled" and "effectively settled" for tax positions subject to an administrative review as the Board has imposed a bright-line rule that must be met in order for the tax positions subject to a refund claim to be accounted for as settled.

Based on prior experience and the nature of a Joint Committee on Taxation administrative review, a taxpayer could easily determine that the likelihood that the Joint Committee on Taxation would not sustain a settlement agreement to be extremely remote for the following reasons:

1. The Joint Committee on Taxation does not reject settlement agreements. Rather, it has the ability to consider the refund and provide comment;
2. In the event that the Joint Committee on Taxation were to raise an issue, it would be limited to the issues identified in the settlement agreement, and
3. The IRS would need to address the Joint Committee on Taxation issue, but would not re-open its audit of the taxpayer/registrant to reconsider "other tax positions" that were no longer actively being reviewed.

We recommend that the Board allow the taxpayer to consider these circumstances in their evaluation of the tax positions rather than impose a rule (which overrides the fundamental accounting principle supporting FIN 48 – the "more-likely-than-not" criteria) requiring that

recognition not occur until completion of the administrative review (by the Joint Committee on Taxation for IRS refunds). We would even go so far as to suggest that applying judgment to the outcome of this type of an administrative review is probably less challenging than many of the other judgments already inherent in FIN 48.

Additionally, had the taxpayer not made the strategic decision to pay the tax and pursue settlement in the form of a refund, the final settlement would involve the exact same tax positions being settled via a payment to the IRS. As such, the settlement would not be subject to an administrative review. In these circumstances, the taxpayer would be able to apply professional judgment and could conclude that the exact same tax positions were effectively settled. We are concerned with the financial reporting inconsistency that inclusion of the administrative review rule may create. We do not think that including a specific rule that administrative reviews must be completed contributes to the Board's mission to make financial reporting meaningful.

Implications under Sarbanes – Oxley

The effectively settled administrative review criteria for recognizing tax benefits associated with refund claims on disputed tax matters as drafted in the FSP has identified a disconnect which we want to highlight. Our Chief Executive Officer is an engineer by training and uses these skills to very effectively lead our organization. He has always looked to the underlying principle/logic embedded in the applicable accounting standards to understand and deal with the numerous accounting issues and matters impacting our company. He has raised a very straight forward question as follows: **If the fundamental accounting principle underpinning our accounting for income taxes is the “more-likely-than-not” recognition criteria, why do we have to recognize the tax benefit of a tax strategy that only has a 51% possibility of being sustained, but for matters that have already been subject to IRS audit which are pending an administrative review characterized as highly probable of being approved (by both internal and outside counsel) we are restricted by the same accounting standard to not recognize the tax benefit associated with an item that has over a 90% probability of occurring?**

This disconnect has caused our CEO to raise concerns as to how he can “sign-off” under Sections 302, 404 and 906 of the Sarbanes–Oxley Act. Omitting the tax benefit associated with successfully concluding an IRS audit agreement that is highly probable of being administratively approved by the Joint Committee on Taxation is potentially misleading. In fact, the Sarbanes-Oxley Act certification requirements specifically exclude relying on GAAP as a defense to filing misleading financial statements when CEOs and CFOs “sign-off” each quarter. In the Final Rule implementing the Sarbanes-Oxley Act, *“Certification of Disclosure in Companies’ Quarterly and Annual Reports”* dated August 29, 2002, the SEC states:

The certification statement regarding fair presentation of financial statements and other financial information is not limited to a representation that the financial statements and other financial information have been presented in accordance with "generally accepted accounting principles" and is not otherwise limited by

reference to generally accepted accounting principles. We believe that Congress intended this statement to provide assurances that the financial information disclosed in a report, viewed in its entirety, meets a standard of overall material accuracy and completeness that is broader than financial reporting requirements under generally accepted accounting principles.

Conclusion

We encourage the Board to remove the requirement that administrative reviews must be completed in order for tax positions to be considered effectively settled. The substance of the tax positions evaluated using the taxpayer's professional judgment should determine whether the tax positions are effectively settled, not any administrative requirements of the tax settlement process. Income tax accounting is a very judgmental area of accounting. The proposed accounting guidance attempts to impose a level of precision in defining settlement that we do not believe is appropriate or necessary.

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We appreciate the opportunity to comment on the issues contained in the Board's invitation. If you have any questions, please contact me at (415) 222-3119.

Sincerely,

/s/ Richard D. Levy

Richard D. Levy
Executive Vice President & Controller