March 28, 2007



LETTER OF COMMENT NO. /3

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Proposed FSP FIN 48-a Definition of Settlement in FASB Interpretation No. 48

Dear Mr. Smith:

We are pleased to comment on the Financial Accounting Standards Board's (FASB or the Board) FASB Staff Position FASB Interpretation No. 48-a, Definition of Settlement in FASB Interpretation No. 48 (Proposed Staff Position or PSP). We generally support the issuance of this Proposed Staff Position as we believe it will ease certain issues facing entities in the adoption of Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). We are, however concerned that the Proposed Staff Position, which was designed to address the limited population of tax positions that do not meet the initial recognition criteria of FIN 48 but have progressed in the audit process such that it is highly unlikely the tax authority would take issue with them, may be perceived as applying to more unrecognized tax positions than it actually may. In addition, while the PSP is consistent with FIN 48 in prohibiting detection risk from being factored in for purposes of initial recognition, it does introduce the concept of enforcement risk as a basis for recognition. We do believe that enforcement vs. detection needs to be discussed on an expanded basis in the PSP to explain why one is permitted in certain cases while the other is not. We also question the introduction of a new recognition threshold and term in the accounting literature - "highly unlikely". We have further elaborated on these comments as well as a few other matters below.

Limited Relief - While we understand that the purpose of the PSP is to both ease certain transition issues as well as to result in more timely adjustment of FIN 48 liabilities as the audit process of the taxing authority progresses, as a practical matter we expect the PSP to have the greatest impact on individually small, as opposed to larger, tax positions. For example, if a company on adoption of FIN 48 has several open tax years for which the taxing authority has completed their expected or required audit procedures, the PSP may reduce the need for an extensive analysis of the technical merits for many smaller tax positions as the taxing authority is "highly unlikely" to reexamine those positions even though they retain that right. On the other



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hand, if a company has a significant tax position related to those open years that is not more likely than not of being sustained, if that position ever becomes known (if not previously the focus of the exam) or receives additional scrutiny by the press or others (if it were previously examined), it generally would not be "highly unlikely" to be reexamined.

Our view as to limited relief may be illustrated by the application of U.S. Revenue Procedure 2005-32, 2005-23 IRB (May 20, 2005), which notes that the U.S. Internal Revenue Service will not reopen a case closed after examination (assuming a closing agreement is not issued) to make an adjustment unfavorable to the taxpayer unless:

- > There is evidence of fraud, malfeasance, collusion, concealment, or misrepresentation of material fact:
- > The closed case involved a clearly defined, substantial error based on an established Service position existing at the time of the examination; or
- > Other circumstances exist indicating that a failure to reopen the case would be a serious administrative omission.

Under the IRS rule, other circumstances indicating that a failure to reopen a case would be a serious administrative omission include cases with items or transactions that present significant potential for abuse for which a limited examination was performed. This third category would include many significant tax positions that are not more likely than not on their technical merits. In addition, since the decision to reopen a tax year (or position) once a certain portion of the audit process has been completed is often based on the taxing authorities' own policies and practices, it is unclear how statements by taxing authority personnel that they may (or are intending to) review those procedures and are considering revising them impacts the highly unlikely assessment – see example 2 of the PSP for an announced (versus potential) change.

Highly Unlikely

The Proposed Staff Position introduces the new term "highly unlikely" (we did not consider the inclusion of "highly unlikely" in the 2005 Invitation to Comment on Selected Issues Relating to Assets and Liabilities with Uncertainties to set a precedent for use of the term). While we understand that the use of that term is intended to significantly limit applicability of the PSP, we question whether a newly defined threshold of likelihood is needed. That is, practitioners and auditors are already using remote (as defined in FASB Statement No. 5, Accounting for Contingencies) to assess likelihood, and it would seem to be a term that would still significantly reduce the applicability of the PSP, without introducing another measurement threshold into the accounting model.



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Other Comments

Paragraph 5 of the PSP notes, "[I]f the taxing authority has specifically examined a tax position during the examination process, an enterprise shall consider this information in assessing the likelihood that the taxing authority subsequently would reexamine that tax position for the completed examination". It appears that the intent of this statement is that the taxing authority's likelihood of reexamination may, depending on the jurisdiction, be based in part on whether or not the specific position was examined previously. We would suggest clarifying this point.

Paragraph 7 notes "However, the effectively settled conditions in paragraph 5 of this FSP may not be the **sole** basis for the enterprise to change its assessment of the technical merits of any tax position in other periods". It is our understanding that the PSP and the related effectively settled criteria are meant to apply in assessing positions that are not more likely than not on their technical merits. As a result, the effectively settled criteria should not serve as **any** basis for assessing the technical merits of a position.

Consistent with FIN 48, the PSP is to be applied on a position-by-position basis. We would however note that in many jurisdictions (including the U.S.) that while a Notice of Proposed Adjustment may be issued on an item-by-item basis, it is a non-binding agreement and is rather nothing more than a memo of understanding. There is no impediment for the taxing authority to reopen that position prior to concluding on the entire year (e.g., An IRS Closing Letter from the Director of Field Operations accepting the Revenue Agent's Report is the document that triggers the re-opening procedure requirements of Rev. Proc 2005-32, and is issued covering one or multiple years). As a result, in many jurisdictions, while the individual position will be evaluated under FIN 48 and the PSP, a conclusion that a position is effectively settled is unlikely to occur until the entire year is completed.

Again, thank you for the opportunity to provide you with our comments on this important FASB Staff Position. We would be pleased to discuss our comments with you further at your convenience.

Very truly yours,

Ernet + Young LLP