

EITF ABSTRACTS

Issue No. 99-15

Title: Accounting for Decreases in Deferred Tax Asset Valuation Allowances
Established in a Purchase Business Combination As a Result of a Change in Tax
Regulations

Date Discussed: November 17–18, 1999

References: FASB Statement No. 109, *Accounting for Income Taxes*
APB Opinion No. 16, *Business Combinations*

ISSUE

1. On June 25, 1999, new consolidated tax return regulations were issued that changed the rules for utilizing certain net operating loss carryovers and carrybacks (NOLCs) by eliminating the requirement to apply the limitations on the separate return limitation year losses to situations in which a change in ownership as defined in Section 382 of the Internal Revenue Code (Section 382) has occurred within six months of a target company becoming a member of a consolidated group. As a result of the new tax regulations, only the loss limitation of Section 382 applies in those circumstances. The change in tax regulations requires an entity to reevaluate the need for an existing valuation allowance for deferred tax assets relating to NOLCs acquired in a prior purchase business combination. In the event that the valuation allowance is reduced or eliminated, there appears to be conflicting guidance about whether the effect of the adjustment should be (a) included in operations (pursuant to paragraph 27 of Statement 109) or (b) applied first to reduce to zero any goodwill related to the acquisition, second to reduce to zero other noncurrent intangible assets related to the acquisition, and third to reduce income tax expense (pursuant to paragraph 30 of Statement 109).

2. The issue is whether the effect of a change in tax law or regulation that results in a decrease in a valuation allowance that initially was recorded in the allocation of the

purchase price in a purchase business combination should be included in income from continuing operations pursuant to paragraph 27 of Statement 109 or as an adjustment to the purchase price allocation pursuant to paragraph 30 of Statement 109.

EITF DISCUSSION

3. The Task Force reached a consensus that the effect of a change in tax law or regulation that results in a decrease in a valuation allowance that initially was recorded in the allocation of the purchase price in a purchase business combination should be included in income from continuing operations pursuant to paragraph 27 of Statement 109. The consensus applies to any reduction in the valuation allowance that otherwise would not have been recognized except for the change in tax law or regulation, regardless of whether the valuation allowance is reduced in the period of the tax law change or in a subsequent period.

STATUS

4. No further EITF discussion is planned.