December 16, 2019

Mr. Shayne Kuhaneck  
Technical Director  
Financial Accounting Standards Board  
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Agenda request – Accounting for deferred tax assets and liabilities

Dear Mr. Kuhaneck,

I appreciate the opportunity to submit an agenda request to the FASB. I request that the FASB or Emerging Issues Task Force (EITF) address the accounting for uncertain tax positions, which is also known as FIN 48, under ASC Topic 740 (Income Taxes). Specifically, FASB or EITF should review the recognition and initial measurement of deferred tax assets and liabilities under the guidance in Accounting Standards Codification (ASC) 740-10-25-2 through 30-8.

I am making this request because the application of the more-likely-than-not criteria/threshold to a tax position produces DTAs and DTLs that are inconsistent with the definition of assets and liabilities in FASB’s Statement of Financial Accounting Concept 6 and other thresholds created by FASB. Furthermore, the measurement of deferred taxes does not reflect the financial concept of time value of money.

These issues have not been addressed or revisited since the establishment of FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes, in July 2006 in relation to the calculation of reserves for uncertain tax positions. However, I believe that these issues can be
solved in less than a year and that the solution provided in this agenda request would reduce the inconsistency of the relative guidance in relation to SFAC 6.

ASC 740-10-25-6 states that “An entity shall initially recognize the financial statement effects of a tax position when it is more likely than not, based on the technical merits, that the position will be sustained upon examination.” The more-likely-than-not term means that there is a likelihood of more than 50 percent.

FASB’s Statement of Financial Accounting Concept 6 as amended provides the following definitions of assets and liabilities:

- Assets are probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events.
- Liabilities are probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events

Under ASC Topic 310 (Receivables), ASC 450 (Contingencies), ASC 606 (Revenue from Contracts with Customers), and several others, the term “probable” is defined as “the future event or events are likely to occur”. In other words, under US GAAP, “probable” is interpreted as a high likelihood and its threshold is approximately between 75%-80%. This suggests that the

term “probable” is considered a much higher threshold than the more-likely-than-not criteria. Furthermore, the more-likely-than-not threshold is more common in IFRS.

ASC 740-10-25-6 permits entities to recognize deferred tax assets and liabilities based on the aforementioned threshold. The issue is that the current definition of assets and liabilities in SFAC 6 include “probable future economic benefits” and “probable future sacrifices of economic benefits” respectively. In other words, deferred tax assets and liabilities arising from the more-likely-than-not threshold does not satisfy the actual definition of assets and liabilities in the statement of concepts.

Entities can recognize DTAs and DTLs when there is a 51% chance or more that the financial statement effects of the tax position can be sustained. This can also affect the reliability of the balance sheet as deferred tax assets and liabilities only meet the more-likely-than-not threshold. To solve the inconsistency issue, I suggest that FASB review and adjust the ASC 740-10-25-6 guidance to follow the definition of assets and liabilities.

Furthermore, the issue that I have presented can be traced back to the vagueness of the term “probable” in the definition of assets and liabilities in SFAC 6. FASB has not suggested the probability percentages in relation to satisfying the term when recognizing an asset or liability. The term creates ambiguities in practice and I suggest that FASB eliminate or adjust the term to clarify the definitions.
In regards to the initial measurement, ASC 740-10-30-8 states that “deferred taxes shall not be accounted for on a discounted basis”, which goes against the notion of time value of money. This suggests the economic advantages of deferring payments is not recognized. For example, consistent with the time value of money concept, an entity is better off if it defers $1 million in taxes for 15 years than paying them now or only postponing them for two years. By following the aforementioned guidance, the entity must add $1 million of tax expense in all three scenarios.

Avoiding discounting on the basis of complexity is advantageous to only one constituent, which is the preparer of financial statements. Furthermore, discounting DTAs and DTLs is important as it reflects the uncertainties inherent in a forecast. The undiscounted deferred tax amounts are not as useful as they should be, since they do not report the real tax impact for the year. Users of financial statements are incurring significant costs to determine the actual discounted measures of deferred taxes, since they provide relevant decision useful information, which is considered to be the cornerstone of SFAC 2.

I suggest that the FASB add these issues to the EITF’s agenda to reduce the inconsistency in the guidance and provide more useful information to financial statement users with discounted measures of deferred taxes.

If you have any questions, please contact me through the following email:

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Sincerely,
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