June 28, 2019

Mr. Shayne Kuhaneck
Acting Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: File Reference No. 2019-700

Dear Mr. Kuhaneck:

PricewaterhouseCoopers LLP appreciates the opportunity to comment on the FASB’s Proposed Accounting Standards Update, *Income Taxes (Topic 740), Simplifying the Accounting for Income Taxes*.

We commend the Board’s efforts to identify, evaluate, and improve areas of ASC 740, *Income Taxes*, in which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to financial statement users. The current income tax accounting standard, developed nearly thirty years ago, includes many mechanical rules and exceptions to its fundamental principles that make it difficult to apply and often yields information that is challenging to understand. We believe the targeted improvements the Board has proposed can both reduce complexity for preparers, auditors and regulators and enhance decision-usefulness for users. We therefore generally support the proposed amendments.

Appendix A contains our detailed responses to the Questions for Respondents in the ED, which includes additional observations and suggestions to clarify the proposed guidance.

We also want to take this opportunity to present additional suggestions for simplification specifically in the area of accounting for the tax effects of outside basis differences in light of the 2017 Tax Cuts and Jobs Act (TCJA). A majority of the simplification items in the Exposure Draft were initially recommended to the FASB in November 2017 as part of a joint letter from Deloitte & Touche LLP, Ernst & Young LLP, KPMG LLP, and PricewaterhouseCoopers LLP. At that time, we specifically avoided making broad-based recommendations related to accounting for outside basis differences due to impending US tax reform. However, TCJA was enacted in December 2017, and its impacts on outside basis differences, including how various outside basis differences are expected to reverse, are now more clear. As a result, we believe there are additional opportunities to simplify income tax accounting for outside basis differences, which ideally can be addressed within the context of the current simplification project. Our suggestions, which constitute more technical corrections than changes in practice, are included in Appendix B. We believe these amendments would help clarify some of the guidance in this especially challenging area by (1) eliminating outdated US tax law references, (2) clarifying the conditions under which a deferred tax asset for an excess of the tax over book basis of an investment in subsidiary can be recognized, and (3) eliminating a reference in the Codification that is often perceived as running counter to the presumption in ASC 740-30-25-3 that all undistributed earnings will be transferred to the parent entity.
If you have any questions, please contact David Schmid at (973) 997-0768, Jennifer Spang at (973) 236-4757, or Brett Cohen at (973) 236-7201.

Sincerely,

PricewaterhouseCoopers LLP
Appendix A

Questions for Respondents

**Question 1: Do you agree that the amendments in this proposed Update would simplify the accounting for income taxes? If not, please explain which proposed amendment(s) you disagree with and why.**

We generally agree that the proposed amendments would simplify the accounting for income taxes. We agree with the FASB's decision to remove references to the equity method within ASC 323-740, *Investments—Equity Method and Joint Ventures—Income Taxes*, along with the related example in ASC 323-740-55-8. Within the Basis for Conclusions (BC27), the Board noted that guidance related to the equity method was not needed because ASC 323-740 is focused on the application of the proportional amortization method and not the general equity method of accounting. For the same reason, we think that references to the cost method with amortization should also be removed throughout ASC 323-740, along with the example in ASC 323-740-55-7.

In our experience, investments in qualified affordable housing projects rarely, if ever, qualify for application of the cost method of accounting. This is, in part, because SEC guidance (codified in ASC 323-30-S99) requires application of the equity method to limited partnership investments unless the investor's interest “is so minor that the limited partner may have virtually no influence over partnership operating and financial policies.” Further, as part of this guidance, the SEC wrote, “The SEC staff understands that practice generally has viewed investments of more than 3 to 5 percent to be more than minor.”

If, however, the cost method references and example are not removed, we recommend the FASB provide guidance on when the cost method would be acceptable since the cost method is otherwise no longer in use.

**Question 2: Do the proposed amendments maintain or improve the usefulness of information provided to users? Alternatively, would the proposed amendments result in the elimination of decision-useful information? Please explain why or why not.**

We generally agree that the proposed amendments would maintain or improve the usefulness of information provided to users. Specifically, we agree with the FASB’s decision not to require allocation of the consolidated amount of current and deferred taxes to single-member limited liability companies. A single-member LLC is a separate legal entity that is not severally liable for the taxes of its owner. We also understand the practical considerations the Board weighed in providing a policy election to allocate the consolidated amount of current and deferred tax expense to legal entities that are not subject to tax and that are disregarded by the taxing authority. However, we believe the language as currently drafted and the discussion in BC13 might inadvertently be interpreted as allowing the policy election to partnerships in addition to single-member LLCs and other disregarded entities. We do not believe it is the FASB’s intent to permit partnerships to make this policy election.

We suggest the FASB make the following addition (underlined) to the end of ASC 740-10-30-27 in order to clarify:

> An entity is not required to allocate the consolidated amount of current and deferred tax expense to legal entities that are not subject to tax (for example, certain partnerships and disregarded entities such as single-member limited liability companies). However, an entity may elect to allocate the consolidated amount of current and deferred tax expense to legal entities that are not subject to tax and that are disregarded by the taxing authority. For purposes of applying this election, partnerships should not be considered disregarded by the taxing authority.
Question 3: Are the proposed amendments operable and auditable? If not, which aspects pose operability or auditability issues and why? Would any of the proposed amendments impose significant incremental costs? If so, please describe the nature and extent of the additional costs.

We believe the proposed amendments are generally operable and auditable. However, we recommend the FASB consider clarifying the following items.

**Step up in the tax basis of goodwill (ASC 740-10-25-54(d))**

The proposed amendment in ASC 740-10-25-54(d) provides that one indicator that a step up in the tax basis of goodwill relates to a separate transaction is if “the transaction resulting in the step up in tax basis requires more than a simple tax election.” The term ”simple tax election” may not be well understood. Conversely, the term “perfunctory” is used in several different areas of the Codification. As such, we recommend revising ASC 740-10-25-54(d) to say, “The transaction resulting in the step up in tax basis requires more than a perfunctory tax election.”

**Step up in the tax basis of goodwill (ASC 740-10-25-54(c))**

The proposed amendment to ASC 740-10-25-54(c) provides that one indicator that a step up in the tax basis of goodwill relates to a separate transaction is if “the step up in tax basis is based on a valuation of the goodwill or business after the date of the business combination.” In order to clarify what we believe was the intention of this indicator, we propose the following revision (added text is underlined and deleted text is struck out).

The step up in tax basis is based on a valuation of the goodwill or business *after the performed as of a date of subsequent to the business combination.*

**Ownership changes in investments — subsidiary to equity method investment (ASC 740-30-45-3)**

The proposed amendment in ASC 740-30-45-3 requires that a parent “accrue as a current period expense income taxes on the temporary difference related to its remaining investment in common stock in accordance with the guidance in Subtopic 740.” We believe the phrase “current period expense” could be confusing or misleading because “current” and “deferred” have specific meanings within ASC 740. We recommend clarifying this item by changing “accrue as a current period expense” to “accrue in the current period.”

**Effect of new tax legislation (ASC 740-270-55-44(b))**

We encourage the FASB to remove Case B: Effective Date of New Legislation That is Administratively Effective (ASC 740-270-55-50), as it does not provide specific accounting guidance. Further, we believe that leaving the example in Case B will create unnecessary confusion, as there is no ongoing accounting relevance with respect to the effective date due to the proposed amendments to ASC 740-270-25-5.

We also note that the proposed amendment to ASC 740-270-55-44(b) introduces a new phrase, “that is administratively effective.” It is not clear what is meant by this term and it would seem to have no accounting significance. We recommend the FASB delete the phrase “administratively effective” from ASC 740-270-55-44(b).
Question 4: Are the transition requirements and transition disclosures for the proposed amendments appropriate? If not, what transition approach or transition requirements would be more appropriate and why?

We generally agree with the conclusions reached with respect to the transition requirements and transition disclosures for the proposed amendments.

For the proposed amendment related to franchise (or similar) taxes, we believe that an entity should be allowed to use either the modified retrospective or full retrospective basis.

Within the Basis for Conclusions (BC30), the FASB indicates that the full retrospective method would improve comparability without requiring an entity to incur significant costs. The FASB further explains that the only anticipated changes would be (1) reclassification of the capital tax presented outside of income tax expense to income tax expense (which would have already been calculated in order to determine which was greater), and (2) in some cases, adjustment to the deferred tax rate if temporary differences are expected to reverse in future years when annual taxable income was expected to exceed the capital tax base. The FASB concluded that, despite the potential for additional costs, prospective transition would not be appropriate because any changes to the deferred tax assets and liabilities as a result of the deferred tax rate change would be recognized in expense during the period of adoption.

We believe the FASB should allow the modified retrospective transition approach. As a result of applying the modified retrospective approach, the opening deferred tax balances would reflect the impact of the proposed amendment without the impact being recognized in expense during the period of adoption; it would instead be recorded as a cumulative adjustment to retained earnings. We anticipate that many entities will need to adjust their deferred tax rates, which could be a complex endeavor retrospectively for amounts that may be insignificant. We do not believe a full retrospective approach provides sufficient incremental benefits to users (as compared to a modified retrospective approach) to justify its costs. Even if modified retrospective transition is permitted, we believe an entity should have the option of applying a full retrospective approach.

Question 5: How much time would be needed to adopt the proposed amendments? Should early adoption be permitted? Should entities other than public business entities be provided with an additional year to implement the proposed amendments? Why or why not?

We believe that questions regarding the time period required for implementation are better addressed by preparers. We believe that early adoption should be permitted.
Appendix B

As noted within the cover letter, we believe there are additional opportunities to simplify income tax accounting for outside basis differences that might reduce confusion in the market. We offer the following recommendations (added text is underlined and deleted text is struck out):

> Undistributed Earnings of Subsidiaries and Corporate Joint Ventures

25-2: Including undistributed earnings of a subsidiary (which would include the undistributed earnings of a domestic international sales corporation eligible for tax deferral) in the pretax accounting income of a parent entity either through consolidation or accounting for the investment by the equity method results in a temporary difference.

25-3 It shall be presumed that all undistributed earnings of a subsidiary will be transferred to the parent entity. Accordingly, the undistributed earnings of a subsidiary included in consolidated income shall be accounted for as a temporary difference unless the tax law provides a means by which the investment in a domestic subsidiary can be recovered tax free.

>> Recognition of Deferred Tax Assets

25-9: A deferred tax asset shall not be recognized for an excess of the tax basis over the amount for financial reporting of an investment in either (1) a subsidiary or (2) a corporate joint venture that is essentially permanent in duration, if the related temporary difference (or portion thereof) will only reverse upon a specific action (for example, sale, liquidation or distribution) and no such action only if it is apparent that the temporary difference will reverse in the foreseeable future.

>> Exceptions to Comprehensive Recognition of Deferred Income Taxes

25-18: As indicated in paragraph 740-10-25-3, a deferred tax liability shall not be recognized for either of the following types of temporary differences: undistributed earnings of a domestic subsidiary, or a domestic corporate joint venture that is essentially permanent in duration, that arose in fiscal years beginning on or before December 15, 1992, unless it becomes apparent that those temporary differences will reverse in the foreseeable future.

a. An excess of the amount for financial reporting over the tax basis of an investment in a foreign subsidiary or a foreign corporate joint venture that is essentially permanent in duration.

b. Undistributed earnings of a domestic subsidiary or a domestic corporate joint venture that is essentially permanent in duration that arose in fiscal years beginning on or before December 15, 1992. A last-in, first-out (LIFO) pattern determines whether reversals pertain to differences that arose in fiscal years beginning on or before December 15, 1992.

Assuming the suggested amendments are made to ASC 740-30-25-18, conforming edits will be needed to either revise or delete ASC 740-30-25-6 and ASC 740-30-45-2.