

FINANCIAL ACCOUNTING SERIES



EXPOSURE DRAFT

Proposed Accounting Standards Update

Issued: February 21, 2013
Comments Due: April 22, 2013

Income Taxes (Topic 740)

Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward or Tax Credit Carryforward Exists

a consensus of the FASB Emerging Issues Task Force

This Exposure Draft of a proposed Accounting Standards Update of Topic 740 is issued by the Board for public comment. Comments can be provided using the electronic feedback form available on the FASB website. Written comments should be addressed to:

Technical Director
File Reference No. EITF-13C

Financial Accounting Standards Board
of the Financial Accounting Foundation

The *FASB Accounting Standards Codification*[®] is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. An Accounting Standards Update is not authoritative; rather, it is a document that communicates how the Accounting Standards Codification is being amended. It also provides other information to help a user of GAAP understand how and why GAAP is changing and when the changes will be effective.

Notice to Recipients of This Exposure Draft of a Proposed Accounting Standards Update

The Board invites comments on all matters in this Exposure Draft and is requesting comments by April 22, 2013. Interested parties may submit comments in one of two ways:

- Emailing a written letter to director@fasb.org, File Reference No. EITF-13C
- Sending written comments to "Technical Director, File Reference No. EITF-13C, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116."

Do not send responses by fax.

All comments received are part of the FASB's public file. The FASB will make all comments publicly available by posting them to the online public reference room portion of its website.

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Summary and Questions for Respondents

Why Is the FASB Issuing This Proposed Accounting Standards Update (Update)?

Topic 740, Income Taxes, does not include explicit guidance on the presentation in the statement of financial position of an unrecognized tax benefit when a net operating loss carryforward or a tax credit carryforward exists. There is diversity in practice in the presentation of unrecognized tax benefits in those instances. Some entities present unrecognized tax benefits as a liability unless the unrecognized tax benefit is directly associated with a tax position taken in a tax year that results in, or that resulted in, the recognition of a net operating loss carryforward for that year and the net operating loss carryforward has not been utilized. Other entities present unrecognized tax benefits as a reduction of a deferred tax asset for a net operating loss carryforward or tax credit carryforward. The objective of the amendments in this proposed Update is to eliminate that diversity in practice.

Who Would Be Affected by the Amendments in This Proposed Update?

This proposed Update applies to all entities that have unrecognized tax benefits when a net operating loss carryforward or a tax credit carryforward exists.

What Are the Main Provisions?

Under the proposed amendments, an unrecognized tax benefit, or a portion of an unrecognized tax benefit, would be presented in the statement of financial position as a reduction to a deferred tax asset for a net operating loss carryforward or a tax credit carryforward, except as follows. To the extent that a net operating loss carryforward or tax credit carryforward at the reporting date is not available under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position, the unrecognized tax benefit would be presented in the statement of financial position as a liability.

No new recurring disclosures would be required.

How Would the Main Provisions Differ from Current U.S. Generally Accepted Accounting Principles (GAAP) and Why Would They Be an Improvement?

Current U.S. GAAP does not include explicit guidance on the presentation in the statement of financial position of an unrecognized tax benefit when a net operating loss carryforward or a tax credit carryforward exists. The amendments in this proposed Update would be an improvement to current U.S. GAAP because they are expected to reduce diversity in practice by providing guidance on the presentation of unrecognized tax benefits and they will better reflect an entity's ability to settle any additional income taxes that would result from the disallowance of a tax position when net operating loss carryforwards or tax credit carryforwards exist.

When Would the Amendments Be Effective?

The amendments in the proposed Update would be applied retrospectively. Early adoption would be permitted. The effective date will be determined after the Task Force considers stakeholder feedback on the proposed Update.

How Do the Proposed Provisions Compare with International Financial Reporting Standards (IFRS)?

IFRS does not include explicit guidance on the presentation of unrecognized tax benefits.

Questions for Respondents

The Board invites individuals and organizations to comment on all matters in this proposed Update, particularly on the issues and questions below. Comments are requested from those who agree with the proposed guidance as well as from those who do not agree. Comments are most helpful if they identify and clearly explain the issue or question to which they relate. Those who disagree with the proposed guidance are asked to describe their suggested alternatives, supported by specific reasoning.

Question 1: Do you agree with the proposed approach for the presentation in the statement of financial position of unrecognized tax benefits when net operating loss carryforwards or tax credit carryforwards exist? If not, what approach do you prefer and why?

Question 2: Do you agree that no new recurring disclosures about the presentation of unrecognized tax benefits should be required? If not, what disclosures would be appropriate?

Question 3: Do you agree that the proposed Update should be adopted retrospectively? If not, why not?

Question 4: For preparers, how much time is necessary to implement the proposed Update? Should the effective date for public and nonpublic entities be the same? If not, why not?

Amendments to the *FASB Accounting Standards Codification*[®]

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–4. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is underlined, and deleted text is ~~struck out~~.

Amendments to Subtopic 740-10

2. Add paragraph 740-10-45-10A and amend paragraphs 740-10-45-11 and 740-10-45-13, with a link to transition paragraph 740-10-65-3, as follows:

Income Taxes—Overall

Other Presentation Matters

> Statement of Financial Position Classification of Income Tax Accounts

>> Tax Accounts, Other Than Deferred

>>> Unrecognized Tax Benefits

740-10-45-10A An unrecognized tax benefit, or a portion of an unrecognized tax benefit, shall be presented in the statement of financial position as a reduction to a deferred tax asset for a net operating loss carryforward or a tax credit carryforward, except as follows. To the extent a net operating loss carryforward or tax credit carryforward at the reporting date is not available under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position, the unrecognized tax benefit shall be presented in the statement of financial position as a liability.

740-10-45-11 An entity that presents a classified statement of financial position shall classify a liability associated with an **unrecognized tax benefit** as a current liability ~~(or the amount of a net operating loss carryforward or amount refundable is reduced)~~ to the extent the entity anticipates payment (or receipt) of cash within one year or the operating cycle, if longer. ~~This~~The liability for unrecognized tax

benefits (or reduction in amounts refundable) shall not be combined with deferred tax liabilities or assets.

740-10-45-12 A liability recognized for an unrecognized tax benefit shall not be classified as a deferred tax liability unless it arises from a **taxable temporary difference**. Paragraph 740-10-25-17 explains how the recognition and measurement of a **tax position** may affect the calculation of a temporary difference.

>>> **Offsetting**

740-10-45-13 The offset of cash or other assets against the tax liability or other amounts owing to governmental bodies is not acceptable except as noted in ~~paragraph~~paragraphs 210-20-45-6 and 740-10-45-10A.

Amendments to Subtopic 210-20

3. Amend paragraph 210-20-15-3 and 210-20-60-3, with a link to transition paragraph 740-10-65-3, as follows:

Balance Sheet—Offsetting

Scope and Scope Exceptions

> Other Considerations

210-20-15-3 The general principle of a **right of setoff** involves only two parties, and exceptions to that general principle shall be limited to practices specifically permitted by the Subtopics listed in this paragraph. Various accounting Subtopics specify accounting treatments in circumstances that result in offsetting or in a presentation in a statement of financial position that is similar to the effect of offsetting. The guidance in this Subtopic does not modify the accounting treatment in the particular circumstances prescribed by any of the following Subtopics:

- a. Paragraphs 840-30-35-32 through 35-52 (leveraged leases)
- b. Subtopic 715-30 (accounting for pension plan assets and liabilities)
- c. Subtopic 715-60 (accounting for plan assets and liabilities)
- d. Subtopic ~~740-30~~740-10 (net tax asset or liability amounts reported)
- dd. Paragraphs 815-10-45-1 through 45-7 (derivative instruments with the right to reclaim cash collateral or the obligation to return cash collateral)
- e. Subtopics 940-320 (trade date accounting for trading portfolio positions) and 910-405 (advances received on construction contracts)
- f. Paragraph 942-305-45-1 (reciprocal balances with other banks).

Relationships

> Income Taxes

210-20-60-3 For guidance on amounts reported for net tax assets or liabilities, see Subtopic 740-10-740-30.

4. Add paragraph 740-10-65-3 and its related heading as follows:

> Transition Related to Accounting Standards Update No. 2013-XX, *Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward or Tax Credit Carryforward Exists*

740-10-65-3 The following represents the transition and effective date information related to Accounting Standards Update No. 2013-XX, *Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward or Tax Credit Carryforward Exists*:

- a. The pending content that links to this paragraph shall be effective for fiscal years and interim periods within those years, beginning after [date to be inserted after exposure]. Early adoption is permitted.
- b. The pending content that links to this paragraph shall be applied retrospectively to all prior periods presented.
- c. An entity shall provide the disclosures in paragraphs 250-10-50-1 through 50-3 in the period the entity adopts the pending content that links to this paragraph.

The amendments in this proposed Update were approved for publication by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Leslie F. Seidman, *Chairman*
Daryl E. Buck
Russell G. Golden
Thomas J. Linsmeier
R. Harold Schroeder
Marc A. Siegel
Lawrence W. Smith

Background Information and Basis for Conclusions

Introduction

BC1. The following summarizes the Task Force's considerations in reaching the conclusions in this proposed Update. It includes the Board's basis for ratifying the Task Force conclusions when needed to supplement the Task Force's considerations. It also includes reasons for accepting certain approaches and rejecting others. Individual Task Force and Board members gave greater weight to some factors than to others.

Background Information

BC2. Topic 740 does not include explicit guidance on the presentation in the statement of financial position of an unrecognized tax benefit when a net operating loss carryforward or a tax credit carryforward exists. Some entities present unrecognized tax benefits as a liability unless the unrecognized tax benefit is directly associated with a tax position taken in a tax year that results in, or that resulted in, the recognition of a net operating loss carryforward for that year and the net operating loss carryforward has not been utilized. Other entities present unrecognized tax benefits as a reduction of a deferred tax asset for a net operating loss carryforward or tax credit carryforward.

General Considerations

BC3. The Task Force considered three approaches for the presentation in the statement of financial position of an unrecognized tax benefit when a net operating loss carryforward or tax credit carryforward exists. Two of the approaches, which are described in paragraph BC2, are the accounting policies followed by most entities. The third approach was to allow an entity to make an accounting policy election to apply one of the other two approaches to all unrecognized tax benefits. The Task Force rejected that approach, however, because it would not resolve the diversity in practice in the presentation of unrecognized tax benefits.

BC4. The Task Force concluded that an unrecognized tax benefit, or a portion of an unrecognized tax benefit, should be presented in the statement of financial position as a reduction to a deferred tax asset for a net operating loss carryforward or a tax credit carryforward, except as follows. To the extent a net operating loss carryforward or tax credit carryforward at the reporting date is not

available under the tax law of the applicable jurisdiction to settle any additional income taxes that would result from the disallowance of a tax position, the unrecognized tax benefit would be presented in the statement of financial position as a liability.

BC5. Some Task Force members selected this approach because, in their view, an entity's tax provision should be prepared as if the uncertain tax position was not claimed on the entity's tax return. If an uncertain tax position was settled with the taxing authority on the basis recognized and measured in the financial statements, then the resolution of the position effectively amounts to additional taxable income or income tax. If under the tax law for the applicable jurisdiction, the net operating loss carryforward or tax credit carryforward would be applied to the additional liability that would arise in the event that the uncertain tax position is not sustained and the settlement related to the uncertain tax position will not result in a payment of taxes, but instead would reduce the net operating loss carryforward or tax credit carryforward, then the deferred tax asset presented in the statement of financial position would be reduced for the unrecognized tax benefit accordingly.

BC6. Some Task Force members believe that the proposed presentation is consistent with the offsetting guidance in Subtopic 210-20, Balance Sheet—Offsetting. Those Task Force members observed that in some jurisdictions, an unrecognized tax benefit, a net operating loss carryforward, and a tax credit carryforward may satisfy the conditions of paragraph 210-20-45-1 because the liability would be offset under the provisions of the tax law.

BC7. The Task Force decided that no new recurring disclosures would be required as a result of the amendments in this proposed Update because the amendments do not affect the recognition or measurement of uncertain tax positions under Topic 740 and because the currently required tabular reconciliation of the gross amount of unrecognized tax benefits will provide public entity users with relevant information about the unrecognized tax benefits offset against net operating loss carryforwards or tax credit carryforwards. The existing disclosure requirements in Topic 740 would be unchanged by the amendments in this Update.

Transition and Early Adoption

BC8. The Task Force reached a consensus-for-exposure that the amendments in this proposed Update would be applied retrospectively. The Task Force believes that a retrospective approach would increase the comparability of financial statements for users and would not be costly. The Task Force decided to solicit stakeholder input about the retrospective approach by including a question for respondents in this proposed Update.

BC9. The Task Force decided to permit early adoption of the proposed amendments to eliminate existing diversity in practice as soon as is practicable.

Benefits and Costs

BC10. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Task Force's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC11. The Task Force does not anticipate that entities will incur significant costs as a result of the amendments in this proposed Update. The accounting policy of some entities is similar to the approach in this proposed Update. The accounting policy of other entities is different from the approach in this proposed Update, but the Task Force anticipates that these entities would have the information necessary to apply the proposed amendments to recognize and measure uncertain tax positions, present unrecognized tax benefits in the statement of financial position, and prepare a tax return. The benefits of the proposed amendments would be increased comparability of financial statements among entities and reduced diversity in practice.

Amendments to the XBRL Taxonomy

The provisions of this Exposure Draft, if finalized as proposed, would require changes to the U.S. GAAP Financial Reporting Taxonomy (UGT). We welcome comments on these proposed changes to the UGT at [ASU Taxonomy Changes](#) provided at www.fasb.org. After the FASB has completed its deliberations and issued a final Accounting Standards Update, proposed amendments to the UGT will be made available for public comment at www.fasb.org and finalized as part of the annual release process.