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May 28, 2015

Technical Director  
Financial Accounting Standards Board  
401 Merritt 7  
PO Box 5116  
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**RE: Exposure Drafts, “Income Taxes (Topic 740) – Intra-Entity Asset Transfers”  
(File Reference No. 2015-200) and “Income Taxes (Topic 740) – Balance Sheet  
Classification of Deferred Taxes” (File Reference No. 2015-210)**

Dear Technical Director:

We appreciate the opportunity to comment on the Board’s Exposure Drafts, *Income Taxes (Topic 740) – Intra-Entity Asset Transfers* and *Income Taxes (Topic 740) – Balance Sheet Classification of Deferred Taxes*. We support the Board’s simplification initiative and agree that areas of U.S. generally accepted accounting principles (GAAP) for which cost and complexity can be reduced without sacrificing the usefulness of the information provided to users should be evaluated and improved.

**Intra-Entity Asset Transfers**

We believe both the current and proposed models of accounting for the income tax consequences of intra-entity asset transfers have merit; however, it is not apparent to us that the proposed model necessarily simplifies or improves the accounting for income taxes. The complexity in the current model primarily resides in recognizing the existence of the exception and evaluating its scope. The proposal does not eliminate this complexity because it creates a new exception to the ASC Topic 810 consolidation model for preparers to identify. It also introduces new complexity in measuring the temporary difference in the buyer’s jurisdiction and estimating the effect of intra-entity asset transfers on the already-challenging estimate of the annual effective tax rate.

Previous Boards agreed with these arguments in developing Statement of Financial Accounting Standards No. 109, *Accounting for Income Taxes* (SFAS No. 109) and in deliberating short-term convergence opportunities. Given the inherent complexity of any accounting change, particularly one that may result in significant system and process changes for some entities, we do not believe the proposed change would simplify or improve the existing model. The primary benefit of the proposal is that it would converge U.S. GAAP with international financial



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reporting standards (IFRS). Although we continue to support efforts for further convergence of U.S. GAAP and IFRS to work towards more comparable global accounting standards, it is unclear whether ongoing convergence efforts are a priority of the FASB. If further convergence is no longer a priority for the FASB, we believe that the costs of implementing the change would exceed the benefits.

### **Presentation of Deferred Tax Assets and Liabilities**

The Board's proposal to require that the net deferred tax asset or liability for each tax-paying component be presented as noncurrent in a classified balance sheet may have minimal effect on complexity because companies generally have the information available to identify the assets and liabilities related to the deferred tax assets and liabilities. However, the proposal would simplify the determination of the appropriate presentation of deferred tax assets and liabilities in circumstances where the deferred tax assets and liabilities do not relate to assets and liabilities for financial reporting purposes and the allocation of the valuation allowance. Although we believe the proposed change is acceptable, we encourage the Board to emphasize in its redeliberations the feedback from financial statement users to evaluate whether the elimination of the requirement to classify deferred tax assets and liabilities as current and noncurrent is concerning to them and whether additional disclosures may be necessary.

### **Overall Plan to Address Complexity in Accounting Standards**

Consistent with our past comments on the Board's simplification projects, while we support the Board's efforts to address unnecessary complexity in accounting standards through its narrow-scope projects within the simplification initiative, we believe that there are significant instances of complexity in accounting standards and financial reporting that transcend the scope of narrow projects intended to simplify specific provisions within existing standards. In addition to the narrow simplification initiatives, we believe the Board should develop a broader overall plan to address systemic causes of complexity within accounting standards and financial reporting. That plan should result in developing a framework that illustrates how the Board will identify, evaluate, and prevent or mitigate potential complexity on an ongoing basis as an integral aspect of its standard-setting activities. The Board also should develop plans to address more significant areas of complexity in existing standards beyond the scope of the narrow projects within the simplification initiative. The narrow projects within the simplification initiative appropriately address concerns about complexity from the perspective of applying a specific provision of a standard. However, we believe an overall framework on complexity, subject to due process, should consider and address cost and complexity based on the potential effects on the overall standard-setting process and financial reporting system, including complexity for financial statement users.



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We look forward to working with the Board as it continues to explore additional opportunities for change as part of the simplification initiative. Our responses to the Board's specific questions and our other observations on the proposed Accounting Standard Updates on Intra-Entity Asset Transfers and the Balance Sheet Classification of Deferred Taxes are included in Appendix I and II, respectively. If you have any questions about our comments or wish to discuss any of the matters addressed herein, please contact Mark Bielstein at (212) 909-5419, Darryl Briley at (212) 909-5680, or Angela Storm at (212) 909-5488.

Sincerely

*KPMG LLP*

KPMG, LLP

## Appendix I – Intra-Entity Asset Transfers

Question 1: *Should the current and deferred income tax consequences of an intra-entity asset transfer be recognized when the transfers occurs? If not, why?*

As discussed in our letter, we believe both the current and proposed models for accounting for the income tax consequences of intra-entity asset transfers have merit, but it is not clear to us that the proposed model is simpler or results in better financial information than the existing model.

- While the proposed model would eliminate an existing exception in U.S. GAAP, it would create a new exception in the principles of consolidation.
- The proposed model would eliminate the requirement to separately track the tax consequences in the seller's jurisdiction; however, it requires additional tracking of the deferred taxes in the buyer's jurisdiction. This simply modifies the existing bookkeeping efforts, and may increase the amount of effort due to potentially complex measurements of the cross-border deferred tax effects in the buyer's jurisdiction (including indirect effects and unrecognized tax benefits) and ongoing valuation allowance assessments. This measurement complexity was acknowledged by the Board in its deliberations of SFAS No. 109.
- The proposed model may result in additional complexity in determining the estimated annual effective tax rate. Although the associated pre-tax income or loss is eliminated in consolidation, the tax consequences will affect the effective tax rate due to different tax rates in different jurisdictions and the lack of pre-tax income recognized on those transactions. Additional effort may be necessary to forecast the cross-border tax effects of intra-entity transfers in estimating the annual effective tax rate.

Given the potential added complexity described above and the inherent complexity of any accounting change, particularly one that may result in significant system and process changes for some entities, we do not believe the proposed change would be a *simplification* or an improvement to the existing model. The primary benefit of the proposal is that it would converge U.S. GAAP with international accounting standards. Although we continue to support efforts for further convergence of U.S. GAAP and IFRS to work towards more comparable global accounting standards, it is unclear whether ongoing convergence efforts are a priority of the FASB. If the Board intends to undertake efforts to make U.S. GAAP more comparable to IFRS, we believe the proposed change would be a worthwhile step in that process. However, if further convergence is no longer a priority for the FASB, we believe that the costs of implementing the change would exceed the benefits. If the Board's intent is to *simplify* the accounting for intra-entity transfers, perhaps it should reconsider whether clarifying the scope of the existing exception better addresses where the complexity lies without introducing new complexities.

Question 3: *Should the proposed guidance be applied on a modified retrospective basis? Are the transition disclosures appropriate?*

Although retrospective application generally is more appropriate for changes in accounting principles, we acknowledge the potential difficulties in applying the full retrospective approach for this proposal (e.g., evaluating deferred tax asset realizability in hindsight). We also acknowledge that because many asset transfers are executed only occasionally, entities may not achieve comparability under any transition method.

Related to disclosures, we believe the Board should consider adding a disclosure to specifically describe the tax consequences of intra-entity transfers (regardless of whether those transfers are asset transfers or license arrangements). BC 10 states that adequate disclosure requirements exist for significant intra-entity transfers; however, we are not clear what requirements in U.S. GAAP the Board is referring to.

Question 4: *Should the amendments in this proposed Update be effective for:*

- a. *Public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2016.*
- b. *All other entities for annual periods beginning after December 15, 2017, and interim periods in annual periods beginning after December 15, 2018, with an early adoption permitted, but not before the effective date for public business entities?*

We support the proposed effective dates, but do not believe that concurrent early adoption of both proposals by private entities is necessary. We view each proposal as a separate matter for which transition linkage should not be required. In addition, it is not clear why private entities would need until the beginning of 2019 to apply the new standard in interim periods.

#### *Miscellaneous*

In subparagraph 740-10-25-20(i), the description of the temporary difference arising from an intra-entity asset transfer refers to the cost of the asset. The Board should revise the paragraph to replace *cost* with *carrying amount* to reflect circumstances where the carrying amount at the time of the transfer differs from its cost.

We recommend the Board make conforming amendments to ASC Topic 323, *Investments—Equity Method and Joint Ventures*. For example, ASC paragraph 323-10-35-7 describes the elimination of profits, including the tax effect, from transactions between an entity and an equity method investee.

## Appendix II – Balance Sheet Classification of Deferred Taxes

Question 1: *Should all deferred income tax liabilities and assets be presented as noncurrent in a classified statement of financial position? If not, why, and what alternatives should the Board consider, and what is the conceptual basis for the alternatives?*

The Board's proposal to require that the net deferred tax asset or liability for each tax-paying component be presented as noncurrent in a classified balance sheet may have minimal effect on complexity because companies generally have the information available to identify the assets and liabilities related to the deferred tax assets and liabilities. However, we agree this proposal may simplify the determination of the appropriate presentation of deferred taxes in certain circumstances by eliminating the requirements to (1) analyze the current/noncurrent classification for each underlying asset or liability to calculate a net current deferred tax asset or liability and a net noncurrent deferred tax asset or liability for each tax paying component, and (2) allocate valuation allowances. In particular, the proposal would simplify the determination of the appropriate presentation of deferred tax assets and liabilities in circumstances where the deferred tax assets and liabilities do not relate to assets and liabilities for financial reporting purposes and the allocation of the valuation allowance. Although we believe the proposed change is acceptable, we encourage the Board to emphasize in its redeliberations the feedback from financial statement users to evaluate whether the elimination of the requirement to classify deferred tax assets and liabilities as current and noncurrent is concerning to them. The Board also should consider whether additional disclosure may be necessary to provide greater transparency into deferred tax reversal patterns.

Question 2: *Should the proposed guidance be applied on a prospective basis?*

We believe the proposed guidance should be applied retrospectively. Retrospective application will provide comparability for financial statement users and should not be difficult for preparers.

Question 3: *Should the amendments in this proposed Update be effective for:*

- a. *Public business entities for annual periods, including interim periods within those annual periods, beginning after December 16, 2016*
- b. *All other entities for annual periods beginning after December 15, 2017, and interim periods in annual periods beginning after December 15, 2018, with early adoption permitted, but not before the effective date for public business entities?*

We believe all companies should be allowed to early adopt this proposed guidance, particularly if the Board agrees to retrospective transition. We also believe, as previously stated, that entities should be able to early adopt this standard without also early adopting the standard on intra-entity asset transfers. In addition, it is not clear why private entities would need until the beginning of 2019 to apply the new standard in interim periods.

*Miscellaneous*

We believe the Board should reconsider the amendment to the last sentence of ASC paragraph 740-10-55-63. Because entities will need to continue to evaluate in their valuation allowance assessments the reversal patterns of temporary differences (regardless of their balance sheet classification), we suggest deleting only the phrase "...and the deferred tax liability should be classified as noncurrent," so that the guidance about the indefinite reversal pattern is retained.