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**Proposed Accounting Standards Update (Revised), Income Taxes (Topic 740):  
Disclosure Framework – Changes to the Disclosure Requirements for Income  
Taxes (File Reference No. 2019-500)**

Dear Mr. Kuhaneck:

We appreciate the opportunity to comment on the Proposed Accounting Standards Update (Revised), *Income Taxes (Topic 740): Disclosure Framework – Changes to the Disclosure Requirements for Income Taxes* (the Proposed Standard), from the Financial Accounting Standards Board (FASB or Board).

We support the FASB's disclosure framework project and its objective of improving the effectiveness of income tax disclosures in the notes to the financial statements. We also support the FASB's proposal to incorporate income tax disclosures required by the Securities and Exchange Commission (SEC) into US GAAP. We encourage the FASB staff to work with the SEC staff to eliminate the income tax disclosure requirements from Regulation S-X 4.08(h) once the guidance is finalized.

We support the proposal to remove the disclosures required by paragraphs 740-10-50-15(d) and 740-30-50-2(b). We encourage the FASB to continue to monitor the effects of the Tax Cuts and Jobs Act to determine whether additional changes should be made to the disclosure requirements in Accounting Standards Codification (ASC) 740. We also support the proposal to replace the term *public entity* in ASC 740 with the term public business entity (PBE) as defined in the Master Glossary of the Codification but recommend that the FASB consider giving certain companies affected by the proposed change additional time to provide the disclosures.

As detailed in the attached responses, we have concerns about the proposed requirement that entities separately disclose foreign and domestic pretax income (or loss) from continuing operations before intra-entity eliminations. We believe that companies may face implementation and reporting challenges without further guidance. We suggest that the FASB consider requiring disclosures about the components of income (loss) before income tax expense (benefit) as either domestic or foreign, as is currently required by Regulation S-X 4.08 (h)(1).



We also have concerns regarding the operability and cost of requiring PBEs to disclose the amount of the valuation allowance recognized for carryforwards. ASC 740 does not require an entity to allocate its valuation allowance to specific deferred tax assets, and the proposed guidance may result in an entity performing detailed scheduling of its temporary differences or making judgments to allocate its valuation allowance to carryforwards. We recommend that the FASB complete its research project on backwards tracing to determine whether changes should be made to ASC 740's prohibition on backwards tracing before moving forward with this proposal. However, if the FASB moves forward with the proposal, the Board should consider providing additional guidance and examples on how a valuation allowance should be allocated to carryforwards.

We also have concerns with requiring entities other than PBEs to disclose certain carryforwards on a gross basis (i.e., not tax effected). In addition, we recommend that the Board clarify certain aspects of the proposed requirements to promote consistency and make the disclosures as useful as possible.

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Our responses to the questions posed in the Proposed Standard are set out in the appendix of this letter.

We would be pleased to discuss our comments with the Board or its staff at your convenience.

Very truly yours,

*Ernst & Young LLP*

**Appendix – Responses to questions raised in the Proposed Accounting Standards Update (Revised), Income Taxes (Topic 740): Disclosure Framework – Changes to the Disclosure Requirements for Income Taxes**

**Question 1:** Would the amendments in this proposed Update that add or modify disclosure requirements result in more effective, decision-useful information about income taxes? Please explain why or why not. Would the proposed amendments result in the elimination of decision-useful information about income taxes? If yes, please explain why.

We believe that the proposed amendments generally would result in disclosures that are more effective and provide decision-useful information in most cases. However, we have concerns that the usefulness of the proposed disclosures on the following topics may be limited.

***Explanation of changes of certain income tax amounts***

We have concerns with the proposed disclosure requirements in paragraphs 740-10-50-6B and 740-10-50-12 that would require explanations of the total amount of the valuation allowance recognized and released during the reporting period and the year-to-year changes in reconciling items in the rate reconciliation. We believe that these disclosures would be consistent with the existing requirements for management's discussion and analysis (MD&A).

The purpose of MD&A is to discuss a company's business as seen through the eyes of management and provide information about the quality of and potential variability of a company's earnings and cash flows so investors can determine the likelihood of past performance indicating future performance. Management is generally required to discuss the following information that is not part of the notes to the financial statements:

- ▶ Specific information about the registrant's liquidity, capital resources, off balance-sheet arrangements, aggregate contractual obligations and results of operations
- ▶ Known material trends, events and uncertainties that may make historical financial information not indicative of future operations or financial condition
- ▶ The cause of material changes in line items of the consolidated financial statements from prior period amounts
- ▶ Any other information the registrant believes necessary for an investor to understand its financial condition, changes in financial condition and results of operations

We believe that the proposal to require entities to provide explanations of these changes may be best disclosed as part of MD&A. However, if the FASB moves forward with the proposal, we recommend that the Board consider making the following changes:

Valuation allowance – Under the proposed requirement in ASC 740-10-50-6B, PBEs would disclose the total amount of the valuation allowance recognized during the period and the total amount of the valuation allowance released during the reporting period, with an explanation of each. We believe explanations for changes in the valuation allowances that are only a result of the entity's normal operations during the year may not provide decision-useful information about income taxes.

For example, a PBE that increases its valuation allowance during the year because of additional net operating loss carryforwards arising from pretax losses or from the expected reversal of existing deferred tax liabilities (increasing the overall net deferred tax asset position) would have to discuss the reasons for current-period operating losses or the timing of the reversal patterns of its deferred tax amounts. If the FASB moves ahead with this guidance, we recommend that it require a PBE to make this disclosure only when there are circumstances that result in a change in judgment regarding the beginning of the year valuation allowance or because of transactions or other events that occur during the period (e.g., a business combination, a disposal of a division).

Rate reconciliation – It is not clear why requiring additional discussion about year-to-year changes of individual reconciling items would be meaningful to the financial statement users, given that the proposed threshold for the rate reconciliation would require PBEs to separately disclose the nature of the reconciling items that caused the annual effective tax rate to be different from the applicable statutory federal income tax rate. In some cases, minor changes in ordinary income can have a significant effect on the annual effective tax rate. A common example is when a company has operating results that are at or about breakeven or when a company has experienced significant fluctuations in earnings (e.g., it is profitable in one year and has losses in another year). In these cases, while there may be year-over-year changes in the reconciling items, the explanation for these changes would be the change in earnings, which we don't believe would provide relevant and decision-useful information to financial statement users. Absent any further guidance or clarification, we also believe that entities may interpret this requirement differently (e.g., provide different levels of detail in their explanations), and the Board should consider whether such diversity in practice would be acceptable and, therefore, whether the disclosures would provide useful information to financial statements users.

If the FASB moves forward with this proposal, we recommend that the language in 740-10-50-12 be revised to clarify when an explanation should be provided. We recommend that the Board consider aligning the threshold for providing an explanation of the year-to-year change in an individual reconciling item to the threshold for reporting individual line items. For example, an entity could be required to provide an explanation for the change in an individual reconciling line item only if the line amount change was at least 5% of the amount computed by multiplying the current year income before tax by the statutory tax rate.

### ***Carryforwards***

We believe that the proposed requirement in ASC 740-10-50-8A for entities other than PBEs to disclose carryforwards that are not tax effected may increase their operational costs. It is not clear how the disclosure of the gross amount of tax carryforwards provides decision-useful information about the potential cash tax savings from those carryforwards. As such, we believe that requiring these entities to disclose the amount before income tax effects may increase complexity for these entities without improving the decision usefulness of the disclosure.

Entities that are not PBEs are currently required to compute the tax-effected amount of these carryforwards in their statement of financial position and, therefore, that information should be readily available. We recommend that the FASB consider amending this paragraph to require the disclosure to be on a tax-effected basis, which would be consistent with the measurement proposed for PBEs. This would improve the comparability of the information with disclosures on tax credit carryforwards and allow users to better understand the potential future cash tax savings from these tax attributes.

We also have concerns about the implementation example in ASC 740-10-55-220A of the disclosure required by ASC 740-10-50-8A for entities other than PBEs. The second paragraph of the example states:

“Realization of the deferred tax asset is dependent on generating sufficient taxable income to utilize the carryforwards. Although realization is not assured, management believes that it is more likely than not that all of the deferred tax asset will be realized. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward periods are reduced.”

The discussion in this paragraph appears to go beyond the guidance proposed in ASC 740-10-50-8A. If the FASB intended to require entities other than PBEs to provide this disclosure, the guidance in ASC 740-10-50-8A should be expanded to provide guidance when this disclosure should be made, and the Board should clarify why this disclosure is necessary. If the FASB's intent is to provide an example of the disclosure that may be required by ASC 275-10-50-6, we recommend that the illustration include additional background information to note this and the reasons why the disclosures required by ASC 275 have been met (i.e., it is reasonably possible that the estimate will change in the near term and the effect of the change will be material).

### ***Income taxes paid***

The proposed amendments to paragraph 230-10-50-2 would require entities to disclose total income taxes paid during quarter and year-to-date interim periods. We believe the proposed disclosure may not result in more decision-useful information, may not correlate with the limited income tax measures disclosed on an interim basis and the period-over-period change may not be comparable. As a result, we question whether the proposed interim disclosure requirements would provide users with additional decision-useful information regarding income taxes.

The usefulness of the disclosures of carryforwards and pretax income (or loss) from continuing operations before intra-entity eliminations are separately addressed in Question 2 and Question 4.

**Question 2:** Are the proposed disclosure requirements operable and auditable? If not, which aspects pose operability or auditability issues and why?

We believe that many entities are likely to have the systems, processes and controls in place to capture the data required to comply with many of the proposed requirements, particularly those that would be consistent with existing SEC disclosure requirements. However, we are concerned about the operability and auditability of the following proposed requirements:

Valuation allowance – We believe further clarification on the definition of *federal or national, state and foreign* is needed. For example, further clarification is required to determine when a state amount should be included in another category (e.g., foreign) or whether all states (domestic and foreign) should be combined in this disclosure. See “Disaggregation of income tax expense” below for further discussion.

We do not believe the proposed guidance in 740-10-50-6A(c) is operational. ASC 740 does not require an entity to allocate a valuation allowance to specific deferred tax assets or other tax attributes and, without further guidance, it is unclear how an entity would allocate a valuation allowance to its carryforwards. We understand the FASB has a research project underway to evaluate whether changes to ASC 740’s prohibition on backwards tracing should be made, and we recommend that the FASB complete its research project before moving forward with this aspect of the proposal.

If the FASB moves forward with the proposed guidance in ASC 740-10-50-6A(c), we believe it should provide additional guidance on how an entity should allocate a portion of its valuation allowance to carryforwards. Without more guidance, entities may take different approaches to do this, such as scheduling the reversal patterns of their deferred tax assets and liabilities or making judgments about which deferred tax assets and tax attributes may not be realizable.

Disaggregation of income tax expense – We recommend that the FASB rename the “state” category for the disaggregation of income tax expense (or benefit) from continuing operations proposed under ASC 740-10-50-10B to “other” or “state and local.” Under the current proposal, we believe it’s not clear how local tax expense or benefit should be classified. In addition, the FASB should clarify when a state, local or other income tax should be separately presented (e.g., state and local taxes are only presented when these taxes represent an additional income tax in the country of domicile). For example, if the reporting entity is domiciled in a country other than the US, the FASB should clarify whether a US state income tax should be included in the foreign or the state component when making this disclosure.

The operability of the disaggregation of domestic and foreign income from continuing operations before intra-entity eliminations proposed in ASC 740-10-50-10A is separately addressed in Question 4.

**Question 3:** Would any of the proposed disclosures impose significant incremental costs? If so, please describe the nature and extent of the additional costs.

We defer to preparers on whether any of the proposed disclosures would impose significant incremental costs. However, we believe the information necessary to provide the additional disclosures would generally be available and, therefore, entities would generally not incur significant costs. However, certain entities may need to expend additional effort to implement some of the proposed requirements, as discussed in Questions 1, 2, 4 and 9.

**Question 4:** One of the proposed amendments would require entities to disclose pretax income (or loss) from continuing operations before intra-entity eliminations disaggregated between domestic and foreign, which initial feedback indicated would reduce diversity in practice. Would this proposed amendment be operable? Should the Board specify whether the disclosed amounts should be before or after intra-entity eliminations? Why or why not?

We do not believe the proposed requirements in ASC 740-10-50-10A to provide pretax income (or loss) from continuing operations before intra-entity eliminations would result in more decision-useful information about income taxes and have concerns about the operability of this proposal. The Background Information and Basis for Conclusions states that the FASB proposed this change to eliminate diversity in practice in whether entities disclose income from continuing operations before or after intercompany eliminations under existing SEC requirements. The Board indicated in BC21 that the amount before intra-entity eliminations would have a more direct relationship with income tax expense (or benefit) and would provide more decision-useful information to financial statement users. However, in some cases the amounts recorded related to intra-entity transactions may bear no relationship to the tax amounts.

We also believe the proposed requirement to disaggregate domestic and foreign income (or loss) from continuing operations before intra-entity eliminations may not be operational for some companies. For example, if a company performs eliminations in a manner inconsistent with the proposed disaggregation (e.g., within the enterprise resource planning system, at a segment level rather than the legal entity or jurisdictional level), the company may need to do extensive work to identify and unwind elimination entries. In addition, when an entity reports pretax income outside of continuing operations (e.g., in other comprehensive income, in discontinued operations), it will need to separately track intra-entity eliminations entries based on how the source of income or loss is presented in the financial statements to determine whether the intra-entity amounts affect income before tax from continuing operations or another financial statement component.

Further, we believe that SEC registrants that make a similar disclosure today under SEC Regulation S-X 4.08 (h)(1) apply judgment in defining their foreign operations when disclosing income before taxes and income tax expense from foreign operations, resulting in diversity in practice that would continue unless additional guidance is provided on how entities should determine when pretax income should be reported as a component of domestic or foreign pretax income from continuing operations. For example, a foreign legal entity that is consolidated in a US reporting entity may be subject to tax in both the US and in a foreign jurisdiction. That would be the case for a branch that is incorporated in a

foreign jurisdiction but included in the US federal tax return or a foreign entity that is disregarded for US federal tax purposes. Also, a branch may operate in a foreign jurisdiction but be part of a US legal entity whose activity is included as part of the US entity's operating results. In addition, there may be diversity in how entities characterize intra-entity elimination entries between foreign and domestic for purposes of the disclosure.

We recommend that the FASB revise the proposed guidance to align with SEC Regulation S-X 4.08 (h)(1). Further, if the Board's intention is to eliminate diversity that exists today in these disclosures, we recommend that the Board develop additional guidance to clarify the definition of domestic and foreign income from continuing operations so that all entities would apply the guidance in a consistent manner. However, the FASB should perform a robust cost benefit analysis for any proposed clarification.

If the Board moves forward with its proposal, in addition to the matters discussed above, we believe additional guidance may be needed to address the complexities of presenting income before tax expense from continuing operations before intra-entity eliminations. For example, we believe the usefulness of the information required by ASC 740-10-50-10A and 10B may be reduced because income tax consequences from intra-entity transfers of inventory are deferred until the inventory is sold to a third party (as required by ASC 740-10-25-3e and ASC 810-10-45-8). Depending on the nature of a company's supply chain and the timing and movement of inventory between domestic and foreign entities, this information could distort the relationship between pretax income before elimination entries and income tax expense. We recommend that the FASB address whether the disclosures of income tax expense should also be adjusted for income tax expense deferred in the period related to intra-entity transfers of inventory since the intra-entity profit on these transactions will be included in income from continuing operations before tax expense and intra-entity eliminations.

Also, companies may declare and pay dividends from members of the consolidated financial statement group to their parent entities. These dividends may be included in income from continuing operations by the investor/parent entities prior to elimination entries being recorded. As these dividends may not be related to the current period earnings, their inclusion may further reduce the usefulness of proposed disclosure.

**Question 5:** Would a proposed amendment to require disaggregation of income tax expense (or benefit) from continuing operations by major tax jurisdiction be operable? Would such a proposed amendment result in decision-useful information about income taxes? Why or why not?

While a proposed amendment to require disaggregation of income tax expense (or benefit) from continuing operations by major tax jurisdiction may be operable for many entities, it would likely require them to develop processes and controls to aggregate such information in that manner. Additionally, if the FASB were to propose this change, we would recommend that the Board clarify how entities would determine their major tax jurisdictions (e.g., based on a measure of pretax earnings, based on income tax expense) and whether the definition of major jurisdiction would apply to only foreign tax jurisdictions or all jurisdictions (e.g., state and local) and provide clarification on the how branches and other disregarded entities should be treated as discussed in Question 4.



We defer to users about whether such a proposed amendment would result in decision-useful information about income taxes.

**Question 6:** The proposed amendments would modify the existing rate reconciliation requirement for public business entities to be consistent with SEC Regulation S-X 210.4-08(h). That regulation requires separate disclosure for any reconciling item that amounts to more than 5 percent of the amount computed by multiplying the income before tax by the applicable statutory federal income tax rate. Should the Board consider a threshold that is different than 5 percent? If so, please recommend a different threshold and give the basis for your recommendation.

We are not aware of PBEs that are registrants experiencing any challenges in providing the disclosure required under Regulation S-X 210.4-08(h). We would, therefore, support aligning the US GAAP rate reconciliation requirement with Regulation S-X. However, we do acknowledge that the reduction in the US corporate federal income tax rate from the Tax Cuts and Jobs Act could result in a US-domiciled entity including items that may be immaterial. We encourage the SEC and FASB staff to work together to determine whether increasing this threshold would be appropriate.

**Question 7:** Are there any other disclosures that should be required by Topic 740 on the basis of the concepts in Chapter 8 of Concepts Statement 8, as a result of the Tax Cuts and Jobs Act, or for other reasons? Please explain why.

We do not believe that any other disclosures should be required on the basis of the concepts in Chapter 8 of Concepts Statement 8, as a result of the Tax Cuts and Jobs Act, or for other reasons.

**Question 8:** Are there any disclosure requirements that should be removed on the basis of the concepts in Chapter 8, as a result of the Tax Cuts and Jobs Act, or for other reasons? Please explain why.

We do not believe any disclosure requirements should be removed on the basis of the concepts in Chapter 8, as a result of the Tax Cuts and Jobs Act, or for other reasons. However, we recommend that the Board continue to monitor the effects the Tax Cuts and Jobs Act is having on disclosures entities are currently required to provide.

**Question 9:** The proposed amendments would replace the term *public entity* in Topic 740 with the term *public business entity* as defined in the Master Glossary of the Codification. Do you agree with the change in scope? If not, please describe why.

We support using the term PBE in ASC 740. However, we believe the FASB should consider giving entities that are PBEs but aren't considered public entities under ASC 740 today more time to implement any final guidance.

That is, we are concerned that the FASB's proposal to use the term PBE would make implementation more complex and challenging for these entities. In addition to community banks (as indicated in paragraphs BC14 and BC15), these entities include:

- ▶ Entities whose financial statements are included in a registrant's SEC filing because they are significant acquirees under Rule 3-05 of Regulation S-X
- ▶ Equity method investees under Rule 3-09 of Regulation S-X
- ▶ Equity method investees whose summarized financial information is included in a registrant's SEC filing under Rule 4-08(g) of Regulation S-X
- ▶ Certain financial institutions that are required by the Exchange Act to file financial statements with the Federal Deposit Insurance Corporation, the Federal Reserve or the Office of the Comptroller of the Currency, but not the SEC
- ▶ Certain insurance companies that file financial statements with state insurance regulators, but not the SEC

This proposal would result in an increase in income tax disclosure requirements for PBEs that are currently considered nonpublic entities under ASC 740. These entities would likely need more time to implement the proposal than public entities and would likely incur significant costs.

**Question 10:** Should the proposed disclosures be required only for the reporting year in which the requirements are effective and thereafter or should prior periods be restated in the year in which the requirements are effective? Please explain why.

We believe that entities should have the option to apply the provisions either prospectively or retrospectively (i.e., by restating prior year disclosures), if they believe comparative disclosures would provide more decision-useful information.

**Question 11:** How much time would be needed to implement the proposed amendments? Should the amount of time needed to implement the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities? Should early adoption be permitted? Please explain why.

We believe that preparers are in a better position to respond to this question. We believe SEC registrants would not incur significant costs to implement the proposed requirements that are consistent with existing SEC disclosure requirements. However, we believe that entities that are not PBEs and PBEs that are currently not considered public entities under ASC 740 (as discussed in Question 9) should have additional time to adopt the proposed standard.

We believe that early adoption of the proposal should be permitted for all entities.