The Association of Accountants and Financial Professionals in Business

via email
To: director@fasb.org

May 30, 2023

Ms. Hillary Salo
Technical Director
Financial Accounting Standards Board
801 Main Ave
PO Box 5116
Norwalk, CT 06856-5116

RE: File Reference No. 2023-ED100, Exposure Draft, Income Taxes (Topic 740) – Improvements to Income Tax Disclosures

Dear Ms. Salo,

The Financial Reporting Committee (FRC or Committee) of the Institute of Management Accountants (IMA) is writing to share its views on the Financial Accounting Standards Board's (FASB or Board) Proposed Accounting Standards Update, *Income Taxes (Topic 740) – Improvements to Income Tax Disclosures* (the Proposed Update).

The IMA is a global association representing over 140,000 accountants and finance team professionals. Our members work inside organizations of various sizes, industries, and types, including manufacturing and services, public and private enterprises, not-for-profit organizations, academic institutions, government entities, and multinational corporations. The FRC is the financial reporting technical committee of the IMA. The Committee includes preparers of financial statements for some of the largest companies in the world, representatives from the world's largest accounting firms, valuation experts, accounting consultants, academics, and analysts. The FRC reviews and responds to research studies, statements, pronouncements, pending legislation, proposals, and other documents issued by domestic and international agencies and organizations. Additional information on the FRC can be found at www.imanet.org (About IMA, Advocacy, Financial Reporting Committee).

The Committee is supportive of the Board's intention to increase transparency and improve disclosures related to income taxes. The Committee understands investors are looking for more information and appreciates the Board's efforts to be responsive to investor needs. In general, the Committee believes that the Proposed Update is mostly clear and operable. However, certain aspects of the Proposed Update should be clarified and refined to ensure decision-useful information is provided to investors while also ensuring operability of the proposed requirements. Members of the Committee felt most strongly about two issues: 1) allowing unrecognized tax benefits to continue to be disclosed in total in the rate reconciliation, as opposed to being

disaggregated by jurisdiction; and 2) requiring annual cash taxes paid instead of adding an interim reporting requirement.

With that said, we would like to share our comments on each of the following Questions for Respondents included in the Proposed Update which were addressed to preparers.

Question 1: The amendments in this proposed Update would require that public business entities disclose specific categories in the rate reconciliation, with further disaggregation of certain reconciling items (by nature and/or jurisdiction) that are equal to or greater than 5 percent of the amount computed by multiplying the income (or loss) from continuing operations before tax by the applicable statutory federal (national) income tax rate.

a. Should any of the proposed specific categories be eliminated or any categories added? Please explain why or why not.

No. The proposed categories are reflective of the primary reconciling items affecting most companies and the addition or elimination of categories would not be impactful. However, judgment will be required to determine how to apply certain items to the defined categories and qualitative disclosures may be required for users to understand how judgments are applied. Further, disclosure of any of these individual categories should be subject to the same 5% threshold as other reconciling items – see response to Question 1.b and 1.c below.

b. Should incremental guidance be provided on how to categorize certain income tax effects in the proposed specific categories? If so, please describe the specific income tax effect and explain how it should be categorized and why.

Yes. Specifically, any final standard should codify the considerations in the Basis for Conclusions to the Proposed Update regarding the application of judgment. In BC17 and BC18, the Board acknowledged that judgment needs to be applied when categorizing income tax effects that do not fall into a clear single category or have characteristics of multiple categories as well as when identifying reconciling items within the cross-border tax law category specifically. We propose the Board codify this recognition of the judgment required in categorization of reconciling items, which supports the Board's principles-based approach to accounting standards as opposed to rigid rules that may not be applied consistently across preparers. Significant judgments would continue to be disclosed in accordance with proposed paragraph 740-10-50-12C.

Additionally, in certain instances, reconciling items between categories are currently presented on a net basis, not only for external reporting but also internally for management. Grossing up these items in external reporting would result in increased balances in the rate reconciliation that do not result in meaningful information. Preparers should be permitted to use judgment in the determination of how to disclose these items in the rate reconciliation. For example, a portion of items that would be included in the foreign or state non-taxable or non-deductible category are often netted with the foreign or state tax effects under current practice. Accordingly, any final standard should allow preparers the ability to exercise judgment with additional qualitative disclosure requirements to explain how judgments were applied in the reconciliation.

We also note that the categories "foreign tax effects" and "effect of cross-border tax laws" are overlapping concepts that require further clarification. Lastly, the enactment of new tax laws category is unnecessary and adds additional potential for diversity in practice. For example, if a new federal tax credit is enacted, it is unclear if it should be categorized as a new tax law or a tax credit. Another example would be a change in the federal tax rate which would be reflected in the starting effective rate, not as part of the enactment of new tax laws. One clarification that would enhance consistency would be to define the category for enactment of new tax laws as specifically limited to the deferred tax impact of new tax laws.

c. Do you agree with the proposed 5 percent threshold? Please explain why or why not.

We applaud the Board's efforts to align the Proposed Update with existing SEC requirements under Regulation S-X. However, the Board should go further and apply the 5% threshold to all reconciling items, including the eight listed categories. As drafted, companies would be required to disclose the eight defined reconciling categories regardless of whether they meet the 5% threshold. This would result in disclosure of items that are insignificant to the rate reconciliation and would be inconsistent with other efforts by the Board and the SEC to provide investors with clear and meaningful information. Additionally, as noted in the response to 1.b above, a requirement to report items that exceed the 5% threshold on a gross basis even when the net result is below the reporting threshold will create a burden on preparers without providing users with additional value.

Lastly, companies should not be required to disclose the impact of any uncertain tax positions by jurisdiction within the rate reconciliation. This disclosure would reveal information about the company's recorded exposure that would be detrimental to any ongoing audits or settlement negotiations with local taxing authorities. The example included in the Proposed Update, 740-10-55-231, shows changes in unrecognized tax benefits disaggregated by foreign jurisdiction. This type of information would become a floor to any tax audit settlement as the taxing authority would be able to ensure their audit adjustments were at least at this disclosed level. To resolve this issue, we strongly recommend the Board consider continuing to allow unrecognized tax benefits to be disclosed on a total basis. Coupled with the existing requirement to qualitatively disclose jurisdictions with material unrecognized tax benefits, investors would be provided with sufficient information while not providing information that would be detrimental to resolution of uncertain tax items.

Question 2: The proposed amendments would require that public business entities provide a qualitative description of the state and local jurisdictions that contribute to the majority of the effect of the state and local income tax category. A qualitative description of state and local jurisdictions was selected over a quantitative disclosure because state and local tax provisions are often calculated for multiple jurisdictions using a single apportioned tax rate. Do you agree with the proposed qualitative disclosure as opposed to providing a quantitative disaggregation? Please explain why or why not.

Yes, we agree that qualitative disclosures are meaningful to users in understanding whether a particular state or local jurisdiction would have a significant impact on the related expense or effective tax rate. This qualitative disclosure would not require significant cost to implement.

Question 3: The proposed amendments would require that public business entities provide an explanation, if not otherwise evident, of individual reconciling items in the rate reconciliation, such as the nature, effect, and significant year over-year changes of the reconciling items. Do you agree with the proposed disclosure? Please explain why or why not.

Yes. We agree and believe most entities are already providing these explanations. As such, we recommend the addition of an example of this qualitative disclosure to the amendments to ensure consistent understanding of the requirement and comparability between entities.

Question 5: For preparers and practitioners, would the proposed amendments to the rate reconciliation disclosure impose significant incremental costs? If so, please describe the nature and magnitude of costs, differentiating between one-time costs and recurring costs.

An initial investment would be required to systematically categorize and document reconciling items as well as put appropriate processes and controls in place. These costs are expected to be significant for some companies. Ongoing costs may be significant, particularly if disclosure of categories under the 5% threshold is required. While some of the new reporting can be automated, the additional requirements will create new complexity that would require additional resources to categorize and review information at a highly detailed level.

Question 6: Are the proposed amendments to the rate reconciliation disclosure clear and operable? Please explain why or why not.

As noted, the current categories need further refinement for the Proposed Update to be clear and operable. Two important revisions should be considered for any final standard: 1) the 5% threshold should apply to all reconciling items including the defined categories; and 2) language permitting judgment in the application of items to categories should be codified, along with qualitative disclosure requirements to explain how significant items are categorized.

Question 7: The Board decided not to provide incremental guidance for the rate reconciliation disclosure for situations in which an entity operates at or around break even or an entity is domiciled in a jurisdiction with no or minimal statutory tax rate but has significant business activities in other jurisdictions with higher statutory tax rates. Do you agree with that decision? Please explain why or why not, and if not, what incremental guidance (including the relevant disclosures) would you recommend?

We agree with the Board's decision. These situations are unique, and we are not aware of significant investor demand for additional disclosure or the need for incremental guidance. Current practice is generally understood.

Question 8: The proposed amendments would require that public business entities provide quantitative disclosure of the rate reconciliation on an annual basis and a qualitative

description of any reconciling items that result in significant changes in the estimated annual effective tax rate from the effective tax rate of the prior annual reporting period on an interim basis. Do you agree with that proposed frequency? Please explain why or why not.

We agree that reporting the rate reconciliation on an annual basis is appropriate. However, we strongly recommend the Board reconsider the requirement for qualitative disclosures on an interim basis. Currently, companies include qualitative discussion and comparison between interim and prior year tax rates within Management's Discussion and Analysis (MD&A) in filings with the SEC. Under current disclosure requirements, companies consider and ultimately disclose qualitative factors when an item is significant and not otherwise evident. MD&A continues to be the appropriate format to disclose these types of qualitative items and it would not be beneficial to introduce an incremental requirement which would include disclosure of the estimated annual tax rate within interim financial statements.

Question 9: The proposed amendments would require that all entities disclose the amount of income taxes paid (net of refunds received) disaggregated by federal (national), state, and foreign taxes, on an annual and interim basis, with further disaggregation on an annual basis by individual jurisdictions in which income taxes paid (net of refunds received) is equal to or greater than 5 percent of total income taxes paid (net of refunds received). Do you agree with the proposed 5 percent threshold? Please explain why or why not. Do you agree that income taxes paid should be disclosed as the amount net of refunds received, rather than as the gross amount? Please explain why or why not.

For certain entities which operate in many jurisdictions, the 5% threshold of income taxes paid (net of refunds received) would result in a high volume of jurisdictions to be disclosed. Additionally, the threshold may significantly vary period to period. As a result, the amount of detail disclosed would not be beneficial to users and may obscure more meaningful information. We believe a moderately higher threshold would ensure the jurisdictions disclosed are truly those that would be of most interest to investors. Specifically, we encourage the Board to consider 10% of income taxes paid (net of refunds received). The 10% threshold aligns with quantitative thresholds applied in other areas of GAAP for identifying significant items for disclosure. The 10% threshold is used in segment disclosure guidance under ASC 280 which requires a segment to be separately disclosed when it represents 10% of revenue, profitability, or assets. We believe this concept applies to determining significant jurisdictions for separate disclosure with respect to cash taxes paid.

Regarding the disclosure of income taxes paid on a gross or net basis, we agree the amount should be disclosed net of refunds received. We do not agree with the proposal to disclose interim cash taxes paid, as discussed further in the responses to Questions 11 through 13.

Question 11: For preparers and practitioners, would the proposed amendments to the income taxes paid disclosure impose significant incremental costs? If so, please describe the nature and magnitude of costs, differentiating between one-time costs and recurring costs.

Multi-national entities would incur significant costs to implement the reporting of interim cash taxes paid. The process for aggregating foreign tax reporting is complex, requiring parsing data

from payments systems to isolate income taxes paid from other cash payments, including non-income-based taxes. Although the investment in systems and staff to report this information on an interim basis in a well-controlled environment will vary by entity, it is apparent that the cost would be significant for many companies.

We acknowledge that cash taxes paid on an annual basis is a current disclosure requirement; however, current requirements are not at a disaggregated level. Additionally, annual reporting deadlines are generally longer with an extended filing period for Form 10-K with the SEC. To meet accelerated interim requirements for filing Form 10-Q, significant resources would be required to accelerate the data collection, analysis, and review, under the proposed disclosures.

Question 12: Are the proposed amendments to the income taxes paid disclosure clear and operable? Please explain why or why not.

Although the requirements are clear, for reasons noted in our response to Question 11, we do not believe the disclosure of interim cash taxes paid is operable without significant investment for many entities.

Question 13: The proposed amendments would require that all entities disclose (a) income taxes paid disaggregated by federal (national), state, and foreign taxes on an interim and annual basis and (b) income taxes paid disaggregated by jurisdiction on an annual basis. Do you agree with that proposed frequency? Please explain why or why not.

In addition to the inoperability of reporting interim cash taxes paid, we believe the interim frequency of this proposed disclosures would not provide decision-useful information to investors. Payment requirements vary across jurisdictions including annual, semi-annual, and quarterly frequencies. These varying payment frequencies result in cash taxes paid that vary significantly between interim periods. These varying interim payment amounts are not indicative of a trend that would be meaningful to investors. Further, certain entities may make large, estimated payments in an interim period and receive a refund later in the year, which would result in a lack of comparability between entities cash taxes paid on an interim basis, even when those entities operate in the same jurisdictions.

The Board noted in BC30 that interim cash taxes paid by individual jurisdiction would not provide decision useful information because taxes are not paid ratably. This conclusion in BC30 also applies to interim cash taxes paid for federal, state, and foreign categories. Accordingly, we support an annual frequency of this disclosure requirement and elimination of the interim disclosure of cash taxes paid in any final standard as it may result in users of financial statements coming to incorrect conclusions.

Question 16: The proposed amendments would be required to be applied on a retrospective basis. Would the information disclosed by that transition method be decision useful? Please explain why or why not. Is that transition method operable? If not, why not and what transition method would be more appropriate and why?

Retrospective adoption would provide comparable information at the time of adoption which would be of value to users of financial statements. The retrospective adoption method would be

operable if sufficient time is provided between issuance of a final standard and the required adoption date to complete any required system changes or software development.

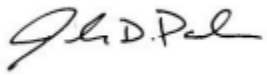
Question 17: In evaluating the effective date, how much time would be needed to implement the proposed amendments? Should the amount of time needed to implement the proposed amendments by entities other than public business entities be different from the amount of time needed by public business entities? Should early adoption be permitted? Please explain your response.

If the noted changes are made to apply the 5% threshold to all reconciling items in the rate reconciliation, as well as elimination of the interim cash taxes paid requirement, we anticipate retrospective reporting would be operable if the first effective date for all periods to be reported begins at least six months after the final Accounting Standards Update is issued. For example, if a final standard is issued in the first quarter of 2024, and requires retrospective reporting, then the earliest required adoption for all periods to be reported should not be until periods beginning after December 15, 2026. As a result, the first set of annual financial statements subject to the new reporting requirements would include 2025, 2026, and 2027. Further, in determining any effective date, the Board should consider the expected timing for implementation of Pillar Two from the Organization for Economic Co-operation and Development which would have overlapping processes for companies as they expand ETR reporting.

Entities other than public business entities may require an additional calendar year to ensure systems and procedures are in-place to capture the required information in a controlled environment for retrospective adoption.

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

Sincerely,



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