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Navigating the Changes in FASB's Income Tax Disclosure Plan

Companies should start reviewing their tax systems to prepare for an overhaul of income tax disclosure requirements by the Financial Accounting Standards Board, say Marcum's Robert McGuinness, Mark Ladolce, and James Petty.

The Financial Accounting Standards Board is weighing a proposal to overhaul its accounting standards to "enhance the transparency and decision usefulness of income tax disclosures." Investors had asked FASB to modify its disclosure requirements to provide more insight into an entity's risks and opportunities related to their worldwide tax profile, and to better assess the impact of income taxes on future cash flows and capital allocation decisions.

Under the proposal, businesses would be required to:

1. Disclose all items that are equal to or greater than 5% of the entity's statutory tax rate (1.05% in the US, using 21% as current applicable statutory tax rate).
2. Disclose items both in percentages and dollar amounts.
3. Disclose, regardless of threshold, state and local taxes net of federal benefit; foreign tax effects broken out by country for any that are above the 5% threshold; tax law changes; changes in cross-border tax laws; tax credits; changes in valuation allowances; permanent differences; and changes in uncertain tax positions.
4. Provide qualitative disclosure explaining the individual states that make up the majority of the state effective tax rate line item.
5. Provide, on an interim basis, a qualitative description explaining the overall effective tax rate, compared to the statutory tax rate.

The proposal also removes the requirement to disclose the estimated amount of uncertain tax positions to change in the next 12 months. It adds a requirement to state that an "estimate of the range of changes in uncertain tax positions cannot be made," and required a table showing, by jurisdiction, the taxes paid—net of refunds received—for all jurisdictions that make up greater than 5% of the total taxes paid.

While investors generally have supported the additional requirements, many businesses have been apprehensive about the effort it would take to comply with them and have asked FASB to roll back some of the changes or eliminate them entirely.

We agree that the proposed amendments would allow for more transparency for investors, resulting in more useful decision making. Companies need to analyze whether they can meet the new requirements through existing processes or if they need to invest in building new processes and procedures.

Client Concerns

There are many concerns related to the proposed standards. Companies may face unfair scrutiny resulting from some of the information required to be disclosed. Releasing such information also could create a reduced competitive advantage, political pressure, and the potential for misinterpretation of information in the tax disclosures.

The proposed standards also would pressure companies to hire additional resources and overhaul processes, and they may not have the time to provide the data necessary to comply with the new standards. It would take effect on a retrospective basis, causing businesses to restate prior periods.

Companies need to consider if their existing processes capture the information at the granular level needed to present it in the financial statements.

Multinational businesses may face additional complexities in gathering information in foreign jurisdictions. They would have to analyze internal controls to ensure disclosures are sufficient to meet the new standards. If not, they would need to enhance existing controls to ensure these disclosures would be accurate.

Due to the reliance on pre-tax book income, accounting for income taxes generally is prepared in a compressed time frame. As part of analyzing the proposed update, it's imperative for businesses to evaluate whether there is sufficient time within the tax reporting process to meet the changes. If not, companies must determine how to overhaul their processes to accommodate the new standards within the time available.

One of the most effective ways to improve the existing tax accounting processes and reduce the risk for the organization is by using technology to capture data at its source and directly integrate it into financial reporting systems. At Marcum, our technology group is working with our tax teams and clients to improve accounting and tax processes using various client software.

Combining targeted technical analysis and implementing automated mapping processes to capture the required data points will lead to greater efficiency and accuracy of the data needed to implement the proposed standards. Companies should begin reviewing their tax systems in the interim, anticipating the proposed standards becoming final.

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Author Information

Robert McGuinness is a partner in Marcum's tax and business services practice. He providing federal, state and local, and international tax compliance, accounting, planning, and controversy services.

Mark Ladolce is a senior tax manager at Marcum and a member of the firm's national transactions and ASC 740 practice.

James Petty is a tax director in Marcum's New York City tax and business services department. He provides federal, state, and international tax accounting and compliance services.