

**30 Cannon Street, London EC4M 6XH, United Kingdom**  
**Phone: +44 (0)20 7246 6410, Fax: +44 (0)20 7246 6411**  
**Email: [iasb@iasb.org](mailto:iasb@iasb.org) Website: <http://www.iasb.org>**



*This document is provided as a convenience to observers at IASB meetings, to assist them in following the Board's discussion. It does not represent an official position of the IASB. Board positions are set out in Standards.*

*Note: These notes are based on the staff paper prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB paper. However, because these notes are less detailed, some paragraph numbers are not used.*

## **INFORMATION FOR OBSERVERS**

**IASB Meeting:**        **February 2006, London**

**Project:**            **Short-term convergence: income taxes – FASB  
redeliberations on uncertain tax positions  
(Agenda Paper 2D)**

---

### **Introduction**

1. The FASB issued the Exposure Draft, *Accounting for Uncertain Tax Positions—an interpretation of FASB Statement No. 109*, in July 2005 and ended its comment period in September 2005. In addition to public comment on the Exposure Draft, the FASB held a public roundtable in October 2005 at which Messrs. Leisenring and Smith participated.
2. After analysing the comment letters and considering the comments, the FASB began redeliberations in November 2005.<sup>1</sup> To date, the FASB has had two meetings to redeliberate the provisions of the UTP project. This memorandum will:
  - a. Summarize the FASB's conclusions to date in redeliberations

---

<sup>1</sup>Board or staff members who wish to receive a copy of the comment letter analysis or the FASB Board memoranda issued during redeliberations can contact Anne McGeachin or Donald Thomas.

- b. Discuss the FASB's immediate plans and future activities
- c. Solicit IASB feedback on matters learned during the comment letter analysis of the Exposure Draft on the amendments to IAS 37.

### **FASB Conclusions to Date in Redeliberations**

- 3. To date, the FASB has deliberated a number of issues. The following sections will present the issues as expressed in the Exposure Draft and the FASB's tentative decisions in redeliberations.

### **Scope**

- 4. The Exposure Draft indicates that the Interpretation should broadly apply to all tax positions, including those taken in connection with business combinations. In redeliberations, the FASB affirmed the provisions of the Exposure Draft.
- 5. The Exposure Draft indicates that the appropriate unit of account for a tax position is a matter of facts and circumstances. Several comment letters implore the FASB to promulgate additional guidance on unit of account. The FASB decided in redeliberations that the appropriate unit of account is a matter of facts and circumstances, and refused to provide specific guidance on unit of account.

### **Recognition**

- 6. The Exposure Draft has four significant provisions related to recognition, which are:
  - a. Benefit recognition approach
  - b. Probable recognition threshold
  - c. Detection risk
  - d. Dual recognition and derecognition threshold.
- 7. In the approach to accounting for income taxes, one could look at income taxes as an obligation and accounting for the amount that will ultimately be required to be paid to the taxing authority. However, a tax benefit can express itself in a myriad of forms on the balance sheet. A tax benefit can result in an asset (including the creation of a net operating loss that creates a deferred tax asset, or a current tax receivable), a liability (either a current or deferred tax liability), or shift between liabilities and assets, or current and deferred income taxes. Since an income tax can express itself in

numerous ways on the balance sheet, the FASB decided to use a benefit recognition approach.

8. The Exposure Draft indicates that it must be probable, as the term is used in Statement 5, that a tax position will be sustained on audit, including resolution of any related appeals or litigation processes, prior to recognition of a benefit from that position in the financial statements. The confidence level expressed by the term *probable* as used in Statement 5 is similar to the confidence level expressed by the term *highly probable* as used in IFRS. In redeliberations the FASB reduced the recognition threshold to more likely than not. The term *more likely than not* in U.S. GAAP is similar to the term probable as used in IFRS.
9. The Exposure Draft indicates that in determining if the probable recognition threshold has been met, it shall be presumed that a tax position will be examined by the taxing authorities. The FASB reaffirmed that decision in redeliberations.
10. The Exposure Draft has one threshold for recognition and another threshold for derecognition, which is referred to as the dual recognition threshold. A tax benefit would be recognized when it is probable and it would be sustained and derecognized when it is more likely than not that the position would no longer be sustained. During redeliberations, the FASB concluded to have one threshold for both recognition and derecognition.

## **Measurement**

11. The Exposure Draft expresses two significant decisions on measurement, which are:
  - a. Use of a two-step model with recognition as the first step and measurement as the second step
  - b. Use of a single point estimate, the best estimate, as the term is used in Concepts Statement 7 to mean the single most likely amount from the range of possible estimated amounts.
12. The FASB reaffirmed the two-step model and the use of a single point estimate, best estimate, as the term is used in Concepts Statement 7.
13. Since the FASB made the decision on best estimate, two comment letters have been received on that decision. As a result of those comments letters, as well as some concern from FASB staff members about the potential results that can occur with the

use of a best estimate measurement attribute, the FASB staff has completed a supplemental memorandum on measurement. That memorandum will be discussed at a FASB education session on February 15, 2005, and at the FASB Board meeting on March 1, 2005. IASB Board or staff members who wish a copy of that memo can contact Anne McGeachin or Donald Thomas.

14. A particular interest of FASB Board members is the IASB's decision to use an expected outcome approach in its approach to uncertain tax positions. The FASB considered the use of expected value or expected outcome, and has tentatively concluded that it may not be practicable. Thus, the FASB is particularly interested in the IASB's current thinking on the subject since the IASB solicited public comment on the use of expected value in the accounting for contingencies in the Exposure Draft on the amendments to IAS 37.

### **Subsequent Recognition and Measurement**

15. The Exposure Draft indicates that an external event is not required to subsequently recognize or measure a tax benefit. The comment letters on the Exposure Draft focus on triggering events and evidence. In researching the issue to present to the Board for redeliberations, the FASB staff began to believe that the most important issue is not the discussion of triggering event or not, or verifiable evidence or not, but the degree to which there is some certainty or finality of the dispute's outcome to qualify for subsequent recognition or measurement. [Not reproduced in Observer Notes.]
16. In redeliberations, the FASB concluded that the best estimate at the reporting date would be based on all information available to management at the reporting date. Absolute certainty of the resolution of the tax position or finality of the outcome is not necessary. However, changes in estimates about recognition and measurement would be based on new information available to the enterprise, not on a new interpretation of old or previously available information.

### **Change in Judgment**

17. The Exposure Draft relies on paragraph 194 of Statement 109 to analogize to accounting in interim periods. Additionally, the Exposure Draft indicates that all changes in judgment, *in-period* or *out-of-period*, would be reflected as discrete items

in the period of the change in judgment. During redeliberations, the FASB concluded that interim period accounting should follow the guidance in Opinion 28 and Interpretation 18, which currently prescribes changes in judgments in interim periods.

## **Interest and Penalties**

18. The Exposure Draft indicates that interest and penalties should be accrued in the period they are deemed to be incurred, based on the provisions of the tax law. Additionally, interest should be computed based on the total amount of the difference between the amounts recognized in the tax return and the financial statements. In redeliberations, the FASB considered three issues on the matter of interest and penalties, which include:
  - a. Recognition of interest and penalties
  - b. Amount of interest expense to recognize
  - c. Classification of interest and penalties.
19. In redeliberations, the FASB considered whether interest and penalties should be recognized when they are assessed by the taxing authorities, or in the period they are deemed to be incurred, based on the provisions of the tax law. The FASB concluded that interest and penalties should be recognized in the period they are deemed to be incurred, based on the provisions of the tax law.
20. In redeliberations, the FASB considered whether to require computation of interest and penalties based on the best estimate of the amount that will be paid, or on the full difference between the amounts recognized in the financial statements and taken on the tax return. The FASB concluded that interest should be accrued on the full difference between the tax return and the financial statements.
21. During initial deliberations the FASB elected not to consider the classification of interest and penalties, since the basis for conclusions in Statement 109 indicates that the FASB specifically chose not to consider the matter when Statement 109 was issued. During redeliberations, the FASB concluded that classification of interest and penalties should be treated as an accounting policy election, and that the election

should be disclosed as well as the amount of interest and penalties recognized in the financial statements.<sup>2</sup>

## **Classification**

22. The Exposure Draft indicates that the difference between the amounts recognized in the financial statements, and the amounts reported in the tax returns should be classified as a current liability to the extent that amounts are anticipated to be paid within the next 12 months or the operating cycle, if longer. Additionally, amounts would not be classified as a deferred tax liability unless they resulted from a taxable temporary difference, as defined in Statement 109. In redeliberations, the FASB affirmed the conclusions expressed by the Exposure Draft.

## **Transition**

23. The Exposure Draft indicates that in transition, enterprises should recognize the change in net assets as a result of applying the provisions of the Interpretation as the cumulative effect of a change in accounting principle. Additionally, the FASB concluded that restatement is not permitted.
24. Subsequent to the Exposure Draft, the FASB issued Statement 154. Paragraph 11 of Statement 154 includes provisions for when it is impracticable to retroactively apply accounting principles. Some of those reasons, the significant and inappropriate use of hindsight, were similar to the reasons the Board concluded that restatement is not permitted in the Exposure Draft.
25. Thus, in redeliberations, the FASB concluded that transition should be made using the cumulative effect of a change in accounting principle. The change in net assets as a result of applying the provision would be treated as an adjustment to the beginning balance of retained earnings. The FASB also concluded that retroactive application is not permitted.

---

<sup>2</sup> The IASB staff notes that the IFRIC has been asked and has declined to give guidance on this issue under IAS 12. The IASB staff recommends that the IASB adopt the FASB approach in the amendments to IAS 12.

## **Effective Date**

26. During redeliberations, the FASB concluded that the final Interpretation would be effective for the first annual period beginning after December 15, 2006. Early application is encouraged provided that financial statements have not been publicly released in the period of adoption.

## **FASB'S IMMEDIATE PLANS**

27. As earlier noted, the FASB is currently deliberating certain measurement issues. If the FASB affirms previous decisions on measurement at the March 1 meeting, the FASB will then deliberate disclosure and sweep issues and anticipates issuing a final Interpretation in March or April, 2005.

## **IASB FEEDBACK ON IAS 37 AMENDMENTS EXPOSURE DRAFT**

28. As noted earlier, of particular interest to FASB members is the IASB's decision to use an expected outcome approach in accounting for uncertain tax positions. The FASB has acknowledged that expected outcome is a superior measurement attribute to recognition threshold coupled with a single point estimate. However, some of the FASB Board and staff have some concerns about the practicability of the application of an expected outcome approach for income taxes.
29. Based on what the IASB has learned during the FASB's deliberations of uncertain tax positions, the FASB's due process on the project (including IASB member involvement in the FASB roundtable), and the public input it has received on the IAS 37 amendments Exposure Draft, does the IASB still anticipate using an expected outcome approach in its approach to account for uncertain tax positions?