



KPMG LLP
345 Park Avenue
New York, N.Y. 10154-0102

Telephone +1 212 758 9700
Fax +1 212 758 9819
Internet www.us.kpmg.com

June 19, 2019

Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

**RE: Proposed Accounting Standards Update, *Simplifying the Accounting for Income Taxes*
(File Reference No. 2019-700)**

Dear Technical Director:

We appreciate the opportunity to comment on the proposed ASU, *Simplifying the Accounting for Income Taxes*. We support the Board's objective to reduce complexity in accounting standards while maintaining or improving the usefulness of the information provided to the users of the financial statements.

We generally believe that the proposals would reduce cost and complexity, consistent with the Board's objectives in its Simplification Initiative. However, with respect to the proposal that companies account for a franchise tax that is partially based on income as an income tax under Topic 740, with incremental tax accounted for as a non-income-based tax, we recommend that the Board:

- permit modified retrospective transition rather than require only retrospective transition, and
- provide additional guidance on assessing the need for a valuation allowance.

We believe these changes would further reduce the costs of implementing the proposals and increase the benefits to financial statement users.

With respect to transition, we do not believe the benefits of income statement comparability outweigh the costs of recasting up to three years of financial results. Retrospective transition would require companies to recognize (or remeasure) deferred tax assets and liabilities and assess (or re-assess) the need for a valuation allowance in each prior period. Those requirements may be especially challenging for a company that generally pays its franchise tax based on a non-income-based measure. Many companies in that position operate at, or close to, breakeven from a taxable income perspective, so the 'higher of' computation results in paying non-income-based tax. To comply with the proposals, that company would identify deferred tax assets and liabilities for that jurisdiction for the first time under Topic 740 in each prior period, and may recognize a net deferred tax asset. It may be challenging in that circumstance to evaluate whether the historical net deferred tax asset is realizable because the company has not had sufficient taxable income to pay income-based taxes in those prior periods and may not expect to have sufficient taxable income to pay income-based taxes in future periods.

Technical Director
Financial Accounting Standards Board
June 19, 2019
Page 2

We acknowledge that this challenge also would exist at the adoption date and in future periods, but believe the costs of implementing the new guidance would be greatly reduced with modified retrospective transition. To further reduce the costs to implement the new guidance, we recommend that the Board provide guidance on the valuation allowance assessment, similar to guidance that the FASB staff provided in other situations in which alternative tax mechanisms exist. We believe establishing a clear framework for the assessment not only reduces costs, but also increases the transparency of the accounting to financial statement users. For example, for valuation allowance purposes, the Board could allow a company to choose between two methods, similar to current practice for the expected valuation allowance effects of global intangible low-taxed income (GILTI) when a company accounts for GILTI as a period cost. A company could:

1. Assume that it would always pay income-based tax and not evaluate the effect of paying non-income-based tax in the future. This approach is similar to the guidance in FASB Staff Q&A, Topic 740, No. 4, Accounting for the Base Erosion Anti-Abuse Tax.
2. Consider the interaction between the non-income-based and income-based tax regimes using a 'with-and-without' approach. Under the with-and-without approach, a company measures the benefit of a deferred tax asset as the difference between (a) what it expects its cash taxes to be with the deferred tax asset and (b) what its cash taxes would have been without the deferred tax asset. This approach is similar to the approach companies use related to GILTI, which was discussed with the FASB staff and is described by several firms in their published guidance.

We believe the FASB should permit modified retrospective transition and provide additional guidance on the valuation allowance assessment. These adjustments would reduce the costs of implementing the new guidance for preparers and increase transparency when applying it for financial statement users.

Our responses to the Questions for Respondents are in Appendix I to this letter. Our additional recommendations are in Appendix II.

* * * * *

If you have questions about our comments or wish to discuss the matters addressed in this comment letter, please contact Kimber Bascom at (212) 909-5664 or kbascom@kpmg.com or Angie Storm at (212) 909-5488 or astorm@kpmg.com.

Sincerely,

KPMG LLP

KPMG LLP

Appendix I – Responses to Questions for Respondents

Question 1: Do you agree that the amendments in this proposed Update would simplify the accounting for income taxes? If not, please explain which proposed amendment(s) you disagree with and why.

Yes, we believe that the proposals generally would simplify the accounting for income taxes and increase comparability. However, we believe that the proposal for companies to account for a franchise tax that is partially based on income as an income tax under Topic 740, with incremental tax accounted for as a non-income-based tax, may increase the costs for some companies. As discussed in our cover letter, we recommend that the Board provide guidance on the valuation allowance assessment, similar to guidance that the FASB staff provided in other situations in which alternative tax mechanisms exist. We believe establishing a clear framework for the assessment increases the transparency of the accounting to financial statement users. For example, for valuation allowance purposes, the Board could allow a company to choose between two methods, similar to current practice for the expected valuation allowance effects of global intangible low-taxed income (GILTI) when it accounts for GILTI as a period cost. A company could:

1. Assume that it would always pay income-based tax and not evaluate the effect of paying non-income-based tax in the future. This approach is similar to the guidance in FASB Staff Q&A, Topic 740, No. 4, Accounting for the Base Erosion Anti-Abuse Tax.
2. Consider the interaction between the non-income-based and income-based tax regimes using a ‘with-and-without’ approach. Under the with-and-without approach, a company measures the benefit of a deferred tax asset as the difference between (a) what it expects its cash taxes to be with the deferred tax asset and (b) what its cash taxes would have been without the deferred tax asset. This approach is similar to the approach companies use related to GILTI, which was discussed with the FASB staff and is described by several firms in their published guidance.

We believe providing additional guidance on the valuation allowance assessment would reduce the costs of implementing the new guidance for preparers and increase the transparency of its application for financial statement users.

Question 2: Do the proposed amendments maintain or improve the usefulness of information provided to users? Alternatively, would the proposed amendments result in the elimination of decision-useful information? Please explain why or why not.

Yes, we believe the proposals generally maintain or improve the usefulness of information provided to users and would not eliminate decision-useful information. We believe the proposals generally simplify the accounting (subject to our recommendations in our response to Question 1) and eliminate exceptions that are easily missed or misinterpreted.

Appendix I
Page 2

Question 3: Are the proposed amendments operable and auditable? If not, which aspects pose operability or auditability issues and why? Would any of the proposed amendments impose significant incremental costs? If so, please describe the nature and extent of the additional costs.

Yes, we generally believe that the proposed amendments are operable and auditable. However, as discussed in our responses to Questions 1 and 4, we believe that companies that generally pay in-scope franchise taxes based on a non-income-based measure would incur incremental costs to implement the proposal to account for those franchise taxes as an income tax.

Question 4: Are the transition requirements and transition disclosures for the proposed amendments appropriate? If not, what transition approach or transition requirements would be more appropriate and why?

Yes, we generally agree that the transition requirements and transition disclosures for the proposals are appropriate. However, as discussed in our cover letter, we recommend that the Board permit modified retrospective transition for the proposal to require companies to account for a franchise tax that is partially based on income as an income tax under Topic 740, with incremental tax accounted for as a non-income-based tax (paragraph 740-10-15-4).

We do not believe the benefits of income statement comparability outweigh the costs of recasting up to three years of financial results. Retrospective transition would require companies to recognize (or remeasure) deferred tax assets and liabilities and assess (or re-assess) the need for a valuation allowance in each of those prior periods. Those requirements may be especially challenging for a company that generally pays its franchise tax based on a non-income-based measure. Many companies in that position operate at, or close to, breakeven from a taxable income perspective, so the 'higher of' computation results in paying non-income-based tax. To comply with the proposals, that company would identify deferred tax assets and liabilities for that jurisdiction for the first time under Topic 740 in each prior period and may recognize a net deferred tax asset. It may be challenging in that circumstance to evaluate whether the historical net deferred tax asset is realizable because the company has not had sufficient taxable income to pay income-based taxes in those prior periods and may not expect to have sufficient taxable income to pay income-based taxes in future periods.

We acknowledge that this challenge also would exist at the adoption date and in future periods, but believe the costs of implementing the new guidance would be greatly reduced with modified retrospective transition. As discussed in our response to Question 1, to further reduce the costs to implement the new guidance and increase the transparency of its application, we recommend that the Board provide guidance on the valuation allowance assessment, similar to guidance that the FASB staff provided in other situations in which alternative tax mechanisms exist.

Appendix I
Page 3

Question 5: How much time would be needed to adopt the proposed amendments? Should early adoption be permitted? Should entities other than public business entities be provided with an additional year to implement the proposed amendments? Why or why not?

Yes, we believe that an entity should be permitted to early adopt the proposals. We believe entities other than public business entities should be provided an additional year to implement the proposals. This would allow them sufficient time to analyze the effects of the franchise tax changes and the policy decision on whether to allocate income taxes to disregarded entities.

Appendix II – Additional Recommendations

We have the following recommendations to enhance or clarify the proposals (additions are underlined; deletions are strikethrough):

Reference	Recommendation	Rationale
740-10-15-4	If a franchise tax is partially based on income (for example, an entity pays <u>requires an entity to pay</u> the greater of an income-based tax and a non-income-based tax,tax);	To prevent entities from including within the scope of the new guidance ‘lesser of’ taxes (which are entirely within the scope of Topic 740 under current guidance)
740-10-30-27	Clarify whether the intercorporate tax allocation policy can be made on an entity-by-entity basis (versus applying to all eligible entities once it is elected).	To prevent entities from inappropriately applying the policy choice
740-10-30-27	However, an entity may elect to allocate the consolidated amount of current and deferred tax expense to legal entities that are <u>both</u> not subject to tax and that are disregarded by the taxing authority.	To clarify that both conditions must be met so that it is clear that income taxes <u>cannot</u> be allocated to entities that are not subject to tax but are not ‘disregarded’ – e.g. partnerships
740-10-50-17A	An entity that is <u>both</u> not subject to tax and that is disregarded by the taxing authority...	
740-10-55-26	Local (including franchise) taxes based on income are within the scope of this Topic. A tax, to the extent it is based on capital, is a <u>non-income-based tax</u> franchise tax.	To remove the suggestion that all taxes based on capital are franchise taxes
740-10-55-143	The portion of the current tax liability based on total computed franchise tax that exceeds the amount equal to the tax on the corporation’s net taxable earned surplus is required to be accrued with a charge to <u>pretax</u> income during the period....	To clarify the geography of the non-income-based tax
740-270-30-11	The effects of changes in judgment about beginning-of-year valuation allowances and effects of changes in tax laws or rates on deferred tax assets or liabilities and taxes payable or refundable <u>for a prior year</u> (in the case of	To more closely align the new guidance with the language in 740-270-25-6 and clarify that the new guidance applies to only taxes that are retroactive to a prior annual period

Appendix II
Page 2

	a retroactive change) shall be excluded from the estimated annual effective tax rate calculation.	
718-740-45-7	<u>Because certain dividends on unallocated shares are not charged to retained earnings under the requirements of paragraph 718-40-25-16, the tax benefit of tax-deductible dividends on allocated and unallocated employee stock ownership plan shares reported as compensation costs shall be recognized in the income statement. All other tax benefits of tax-deductible dividends on employee stock ownership plan shares shall be taxes-allocated to continuing operations.</u>	To permit an entity to present the tax benefits of dividends on unallocated shares in discontinued operations when the related compensation expense on those shares is presented in discontinued operations
740-10-65-9(c)	We recommend the Board not require this disclosure for those items with prospective transition	To reduce unnecessary complexity in transition disclosures by not requiring an entity to assess whether it would have been subject to the four items adopted through prospective transition
323-740	Replace ‘cost method’ with a new term – e.g. modified cost – that is specific to Subtopic 323-740	To eliminate confusion because: <ul style="list-style-type: none"> the ‘cost method’ as illustrated operates differently from the historical ‘cost method’; and the historical cost method is no longer applied to most passive equity investments
323-740-25-2 – 25-2A	25-2 For an investment in a qualified affordable housing project through a limited liability entity not accounted for using the proportional amortization method, the investment shall be accounted for in accordance with Subtopic 970-323, <u>except as provided in paragraph 323-740-25-2A</u> . In accounting for such an investment under that Subtopic, the requirements in paragraphs 323-740-25-3 through 25-5 and paragraphs 323-740-50-1 through 50-2	To eliminate the conflict in Subtopic 323-740 about whether an investor that has virtually no influence must (or is permitted) to apply: <ul style="list-style-type: none"> Topic 321 as required by Subtopic 970-323, because paragraph 323-740-25-2 requires an investor to apply the guidance in Subtopic 970-323 when it does not use the proportional amortization method; or

Appendix II
Page 3

	<p>of this Subsection that are not related to the proportional amortization method, shall be applied.</p> <p>25-2A <u>If a reporting entity has virtually no influence over the operating and financial policies of the limited liability entity, Accounting it may account for an investment in a qualified affordable housing project using the modified cost method as illustrated in Example 1 (see paragraph 323-740-55-2) may be appropriate.</u> In accounting for such an investment using the <u>modified cost method as illustrated in this Subtopic</u>, the requirements in paragraphs 323-740-25-3 through 25-5 and paragraphs 323-740-50-1 through 50-2 of this Subsection that are not related to the proportional amortization method shall be applied.</p>	<ul style="list-style-type: none"> the cost method as illustrated in Subtopic 323-740, because it is stated in existing paragraph 323-740-25-2A
--	---	--