

FASB issues Exposure Draft for proposed changes to income tax disclosures

March 21, 2023

In brief

On March 15, 2023, the Financial Accounting Standards Board (FASB) issued an Exposure Draft (ED) of a proposed Accounting Standards Update (ASU), *Income Taxes (Topic 740): Improvements to Income Tax Disclosures*. The proposed ASU represents the FASB's ongoing efforts to enhance the transparency and decision usefulness of annual and interim income tax disclosures. These proposed changes would apply to all entities that are subject to income taxes, with certain of the proposed amendments being applicable only to public business entities. Comments from respondents are due to the FASB by May 30, 2023.

This *Insight* highlights the proposed amendments to income tax disclosures, which generally impact a company's rate reconciliation and income taxes paid disclosures, as well as other considerations.

In detail

Overview

Users of financial statements have indicated to the FASB that the current existing income tax disclosures should be enhanced to provide more transparency surrounding an entity's global operations and the related tax effects and risk, including future cash flows.

The proposed amendments generally impact a company's disclosures around the rate reconciliation and cash taxes paid, as well as certain other areas.

Rate Reconciliation

On an annual basis, public business entities (PBE) would be required to (1) disclose eight specific categories in the effective tax rate reconciliation (as shown in the example below), and (2) provide additional information for reconciling items that meet or exceed a quantitative threshold. The threshold is equal to 5 percent of the amount computed by multiplying pre-tax income (or loss) by the applicable statutory tax rate of the country of domicile (i.e., for US domiciled corporations, 21 percent multiplied by 5 percent, or 1.05 percent). The amounts disclosed within the rate reconciliation would include both percentages and reporting currency amounts. An example within the proposed ASU demonstrates the presentation and separate categories:

	Year Ended December 31, 20X2			Year Ended December 31, 20X1			Year Ended December 31, 20X0		
	Amount	Percent	%	Amount	Percent	%	Amount	Percent	%
U.S. Federal Statutory Tax Rate	\$ AA	aa	%	\$ BB	bb	%	\$ CC	cc	%
State and Local Income Taxes, Net of Federal Income Tax Effect ⁽¹⁾	AA	aa		BB	bb		CC	cc	
Foreign Tax Effects									
United Kingdom									
Tax rate differential	(AA)	(aa)		(BB)	(bb)		(CC)	(cc)	
Share-based payment awards	AA	aa		BB	bb		CC	cc	
Changes in unrecognized tax benefits	(AA)	(aa)		(BB)	(bb)		(CC)	(cc)	
Other	(AA)	(aa)		BB	bb		(CC)	(cc)	
Ireland									
Tax rate differential	(AA)	(aa)		(BB)	(bb)		(CC)	(cc)	
Valuation allowances adjustments	(AA)	(aa)		(BB)	(bb)		CC	cc	
Enactment of new tax laws	-	-		BB	bb		-	-	
Other	AA	aa		(BB)	(bb)		(CC)	(cc)	
Switzerland	(AA)	(aa)		(BB)	(bb)		(CC)	(cc)	
Mexico	AA	aa		BB	bb		CC	cc	
Other foreign jurisdictions	(AA)	(aa)		(BB)	(bb)		CC	cc	
Enactment of New Tax Laws									
Change in tax rate	-	-		-	-		(CC)	(cc)	
Effect of Cross-Border Tax Laws									
Global intangible low-taxed income	AA	aa		BB	bb		CC	cc	
Foreign-derived intangible income	(AA)	(aa)		(BB)	(bb)		(CC)	(cc)	
Base erosion and anti-abuse tax	AA	aa		BB	bb		CC	cc	
Other	AA	aa		-	-		-	-	
Tax Credits									
Research and development tax credits	-	-		(BB)	(bb)		(CC)	(cc)	
Energy-related tax credits	(AA)	(aa)		-	-		-	-	
Foreign tax credits	(AA)	(aa)		(BB)	(bb)		(CC)	(cc)	
Other	-	-		(BB)	(bb)		-	-	
Valuation Allowances	AA	aa		(BB)	(bb)		(CC)	(cc)	
Nontaxable or Nondeductible Items									
Share-based payment awards	AA	aa		BB	bb		CC	cc	
Goodwill impairment	AA	aa		BB	bb		-	-	
Other	AA	aa		(BB)	(bb)		CC	cc	
Changes in Unrecognized Tax Benefits	(AA)	(aa)		BB	bb		(CC)	(cc)	
Other Adjustments	AA	aa		(BB)	(bb)		(CC)	(cc)	
Effective Tax Rate	\$ AA	aa	%	\$ BB	bb	%	\$ CC	cc	%

(1) State taxes in California and New York contributed to the majority of the tax effect in this category.

Observation: It is important to note that the eight separate categories are required regardless of whether the category meets the 5 percent quantitative threshold.

PBEs will be required to separately disclose any reconciling item listed below that meets or exceeds the 5 percent threshold:

- If the reconciling item is within the category of “Effect of Cross-Border Tax Laws”, “Tax Credits” or “Nontaxable or Nondeductible Items”, these items must be disaggregated by nature
- If the reconciling item is with the category of “Foreign Tax Effects”, it must be disaggregated by jurisdiction and by nature
- If the reconciling item does not fall within any of the eight required categories, it must be disaggregated by nature

Observation: While certain of these categories (and reconciling items with these categories) may be consistent with a company’s current annual rate reconciliation disclosures, other requirements will likely be new. In particular, disaggregation of the “Foreign Tax Effects” by jurisdiction and nature may represent a significant increase to required disclosures for multinational enterprises.

In the “Basis for Conclusions” section of the ED, the FASB indicates that with respect to the “Foreign Tax Effects” category, if a foreign jurisdiction meets the 5 percent threshold on a total jurisdictional basis, then it would be separately disclosed. Moreover, for that foreign jurisdiction, a reconciling item that meets the 5 percent threshold by nature (e.g., a tax credit) would additionally be disclosed. Importantly, a foreign jurisdiction may not meet the 5

percent threshold on a total jurisdictional basis, but may have separate reconciling items by nature (e.g., tax credits) that meets the 5 percent threshold, thus requiring separate disclosure.

The “Foreign Tax Effects” category would reflect those impacts imposed by each foreign jurisdiction. The other seven categories would be evaluated from the lens of the country of domicile for the reporting group. For example, a tax credit generated in the country of domicile (e.g., US federal research and development tax credits) would be disclosed under “Tax Credits”, while tax credits in foreign jurisdictions would be disclosed in the “Foreign Tax Effects” category. Likewise, with respect to “Cross-Border Tax Laws”, the “Basis for Conclusions” section within the ED indicates that these reconciling items should reflect the incremental taxes imposed by the country of domicile with respect to income earned abroad. For a US multinational, this may include the impacts of BEAT, GILTI and FDII.

Observation: *It appears, based upon the proposed ASU, that impacts of “cross-border” matters such as GILTI or Subpart F inclusions are presented separately from any related foreign tax credit amounts that may ultimately reduce a company’s net tax impact from such regime(s).*

With respect to “State and Local Income Taxes”, this category would reflect income taxes imposed at the state and local level within the jurisdiction of domicile. In addition, PBEs would also be required to provide a qualitative description of the state and local jurisdictions that contribute to the majority of this category.

PBEs would be further required to provide an explanation (if not otherwise evident) of individual reconciling items disclosed, such as the nature, effect and significant year over year changes in the reconciling items. On an interim basis, PBEs would be required to provide a description of any reconciling items that would represent significant changes in the estimated annual effective tax rate, as compared to the effective tax rate from the prior annual period.

Non-PBEs would be required to provide qualitative disclosures about the specific categories of items and individual jurisdictions that contribute to any significant differences between the statutory rate (country of domicile) and the effective tax rate.

Income Taxes Paid

The proposed amendments in the ED include incremental disclosures of cash taxes paid for all entities (i.e., PBEs and non-PBEs), including:

- Disclosure of the year-to-date amounts of income taxes paid (net of any income tax refunds received) disaggregated by federal (i.e., national), state and foreign taxes. This is required on both an interim and annual basis.
- Disclosure of income taxes paid (net of any income tax refunds received) disaggregated 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). This requirement is on an annual basis.

In the “Basis for Conclusions”, the FASB indicated that the 5 percent threshold is determined by comparing the absolute value of the net payment or refund in each jurisdiction with the absolute value of the total net payment or refund.

Observation: *Given the 5% percent threshold for disclosure, companies may find that a significant number of jurisdictions may require separate disclosure under the proposed standard.*

Disclosures Previously Exposed for Comment

The ED contains certain proposed amendments that were included in the previous 2019 proposed ASU on income tax disclosures. The amendments include:

- For all entities, disclosure of (1) income (or loss) from continuing operations before income tax expense (or benefit), disaggregated by domestic and foreign, and (2) income tax expense (or benefit) from continuing operations disaggregated by federal (national), state and foreign
- Elimination of the requirement for all entities to disclose (1) the nature and estimate of the range of reasonably possible changes in the unrecognized tax benefits balance in the next 12 months, or (2) a statement that such an estimate of the range cannot be made
- Elimination of the requirement to disclose the cumulative amount of each type of temporary difference when a deferred tax liability is not recognized because of the application of the indefinite reinvestment assertion (f/k/a “APB 23”)

Observation: *Elimination of the requirement to disclose temporary differences related to outside basis differences in foreign subsidiaries where an indefinite reinvestment assertion is made is of importance for US multinational corporations, particularly where such amounts may have a diminished relevance after the enactment of US tax reform in December of 2017. It is important to note, however, that other required disclosures with respect to the indefinite reinvestment assertion are still applicable.*

Other Considerations

Among other considerations, FASB considered (but ultimately decided not to) provide guidance for situations where a company operates at or around a “break even” pre-tax income (or loss) basis, or where an entity is domiciled in a jurisdiction with no or minimal statutory tax rates, but has significant operations in other foreign jurisdiction(s) with higher tax rates. In both of these cases, application of the 5 percent threshold could result in a significant or unlimited amount of reconciling items. The FASB did acknowledge in its “Basis for Conclusions” that “such entities may consider materiality or use a normalized pretax income (or loss) amount or a higher federal or national tax rate for purposes of preparing the rate reconciliation to provide more relevant and meaningful information.”

Transition and Effective Dates

Both the effective date and whether early adoption of the amendments would be permitted are to be determined after consideration of feedback received during the comment period. As proposed the amendments in this ED would be applied retrospectively.

Observation: *Regardless of the final effective date determined with respect to these amendments, companies would need to provide three years of data with respect to these changes (i.e., the current year information from the year of adoption, plus two prior year comparables) under the current ED requirements. Given the data points needed with respect to these amendments, companies should consider evaluating existing reporting information (e.g., amounts from recently filed 2022 financial statements) and processes for sufficiency.*

See also

Policy on Demand: [FASB exposure draft: Key for companies to engage and prepare](#)

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Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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