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Accounting for Income Taxes
Quarterly Hot Topics

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Accounting developments

Revenue recognition

On May 28, 2014, the Financial Accounting Standards Board (FASB) and International Accounting Standards Board (IASB) issued their final standard on revenue from contracts with customers. The standard, issued as **Accounting Standards Update (ASU) 2014-09**[1] by the FASB, outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. The standard supersedes most current revenue recognition guidance, including industry-specific guidance.

Tax implications of the new ASU

Federal income tax law provides both general and specific rules for recognizing revenue on certain types of transactions (e.g., long-term contracts and arrangements that include advance payments for goods and services). These rules are often similar to the method a taxpayer uses for financial reporting purposes and, if so, the taxpayer employs the revenue recognition method it applies in maintaining its books and records — e.g., cash basis, U.S. Generally Accepted Accounting Principles (U.S. GAAP), International Financial Reporting Standards (IFRSs). Although the Internal Revenue Code (IRC) does not require entities to use any particular underlying financial accounting method to determine their taxable income (such as U.S. GAAP), entities must make appropriate adjustments (on Schedule M) to their financial accounting pretax income to determine taxable income under the IRC.

The ASU may change the timing of revenue recognition and, in some cases, the amount of revenue recognized for entities that maintain their books and records under U.S. GAAP or IFRSs. These changes may also affect taxable income. For example, under federal tax principles, income is generally recognized no later than when it is received. However, there are a few limited exceptions that allow a taxpayer to defer revenue recognition (one year or longer) for advance payments. Under one of these exceptions, a taxpayer

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[1] FASB ASU No. 2014-09, *Revenue From Contracts With Customers*. For an overview of the ASU, see Deloitte's May 28, 2014, **Heads Up**.

can defer revenue recognition for advance payments for one year to the extent that the revenue is deferred under the method used for the taxpayer's applicable books and records.

The standard may affect the timing and measurement of revenue for certain contracts with advance payments and thus may accelerate revenue recognition for contracts with multiple performance obligations, which could have an impact on current taxable income.

In addition, a few of the concepts in the standard may give rise to or affect the measurement of certain temporary differences. These concepts include:

- Revenue recognition upon a transfer of control that results in changes in book revenue recognition, as well as related contract assets and contract liabilities.
- Potential changes in the timing of revenue recognition for contracts that include variable consideration or a significant financing component.
- Capitalization of certain costs incurred to obtain or fulfill a contract, some of which currently may be deductible for tax purposes.

The tax implications associated with implementing the standard will be based on an entity's specific facts and circumstances. Thus, it will be important for tax professionals to understand the detailed financial reporting implications of the standard so that they can analyze the tax ramifications and facilitate the selection of any alternative tax accounting methods that may be available.

Before a taxpayer can select a new tax accounting method, the taxpayer must obtain consent from the Internal Revenue Service (IRS) commissioner. In addition to selecting alternative tax accounting methods, if a taxpayer is applying its book method and the book method changes, the taxpayer may have to secure the commissioner's consent to change to the new book method for tax purposes. Further, certain tax accounting method changes require the IRS to review an application before granting consent. Other tax accounting method changes provide automatic consent if the taxpayer complies with certain terms and conditions.

A taxpayer that chooses not to secure consent to change its tax accounting method (i.e., to conform to the new financial reporting method) may have to maintain its current tax accounting method and may need to keep additional records as a result. This additional record keeping will be unavoidable when entities are not permitted to use the standard's revenue recognition method for tax purposes.

The following are a few questions for entities to consider in planning for the transition:

- Will potential changes to the timing or measurement of U.S. GAAP or IFRS revenue or expense recognition affect the timing of revenue or expense recognition for income tax purposes?
- If the financial statement modifications in revenue recognition methods under the standard are favorable and permissible for tax purposes, is an entity required to request a formal change in tax accounting method from the tax authorities?
- If the financial statement modifications are unfavorable or impermissible for tax purposes, will the entity need to maintain certain legacy U.S. GAAP or IFRS accounting method records (i.e., records in accordance with the historical revenue recognition method that will be superseded by the standard)?
- When the amount of revenue in a contract with multiple performance obligations is allocated to the separate performance obligations under the standard, are there specific contractual terms that may result in a difference between the allocations for tax and book accounting purposes?
- To the extent that tax accounting methods differ from financial reporting accounting methods, are there any new data or system requirements that need to be considered?
- Are there any cash tax implications related to foreign controlled entities that, for example, maintain statutory accounting records under IFRSs?
- If there is a cumulative adjustment to the opening balance upon adoption of the standard at a foreign operation, should the U.S.-based parent entity reassess its indefinite reinvestment assertion and reevaluate the amount of deferred tax liabilities established for the related outside basis difference, if any?

- What is the effect on a multinational entity's transfer pricing strategy, especially when the transfer pricing is based on the amount of revenue recognized for financial reporting?
- Should there be a change in the financial statement presentation for sales taxes collected that are remitted to a tax authority on the basis of the principal-versus-agent guidance in the standard?
- Although the impact on state taxable income generally is the same as that on federal taxable income, what other state tax implications should an entity consider?

In certain industries, the ASU may also have a significant impact on other taxes such as sales, excise, industry-specific gross receipts, telecommunications, utility, business and occupation, and other specialty taxes. For example, for an arrangement that includes discounted tangible personal property (TPP), the standard may require entities to change the manner in which they allocate revenue between the sale of the TPP and the sale of related services — as opposed to following the invoicing and contract treatment. In such cases, part of the amount historically recognized as service revenue over the life of the related service agreement most likely will be reallocated to product revenue. This reallocation of revenue could affect the amount of some taxes or fees collected or reported by the vendor.

Taxes or fees that are at risk for overcollection or underreporting are those that are based solely on either sales of services or sales of products, when the other category is generally excluded from the tax or fee base. For example, customer tax billing systems are often designed to automatically collect these taxes and fees on the basis of the billed amounts. If the legal base of the tax or fee is the amount recognized for services — and sales of TPP are excluded from the base — there is a risk that the tax/fee will be overcollected from customers if it is computed on the basis of the invoiced amounts. In contrast, if the legal base of the tax or fee is the amount billed, there is a risk that the tax/fee will be underreported, if, after the adoption of the new standard, the vendor uses only the service revenue amount recognized for books as a source for tax base data.

Income tax credits

In January 2014, the FASB issued **ASU 2014-01**,[2] which provides criteria an entity must meet in order to account for Low-Income Housing Tax Credit investments using the proportional-amortization method. At its April 28, 2014 meeting, the FASB tentatively decided not to expand the scope of ASU 2014-01 to other tax credit investments, including Historic Tax Credits, New Market Tax Credits, and Renewable Energy Tax Credits. As these additional tax credit investments have a profit motive, it was noted that they would not meet the criteria in ASU 2014-01 to use the proportional-amortization method and thus should not be included in the scope of ASU 2014-01.

Financial instruments – Classification and measurement

In current practice, differing approaches exist when evaluating whether a valuation allowance (VA) should be recorded on a deferred tax asset (DTA) related to debt securities classified as available-for-sale. In circumstances where a DTA is recognized as a result of an unrealized loss on a debt security recorded in other comprehensive income (OCI) and an entity has the intent and ability to hold the debt security until recovery, the Securities Exchange Commission (SEC) staff has accepted two alternative views on the evaluation of the need for a VA related to the DTA: [3]

- View 1 — DTAs are excluded from other DTAs being evaluated for realization because the DTA recognized for unrealized losses of a debt security included in OCI does not require a source of future taxable income for realization — since the accounting assertions imply that the unrealized loss will never be realized and that no tax loss will therefore ever be reported on any tax return).

[2] FASB Accounting Standards Update No. 2014-01, Accounting for Investments in Qualified Affordable Housing Projects. For an overview of the ASU, see Deloitte's January 21, 2014, **Accounting Journal Entry**.

3 For additional background on this issue, refer to the Accounting for Impaired Debt Securities section of Deloitte's **Accounting Roundup — Special Edition: Annual Update on Accounting for Income Taxes.**

- View 2 —DTAs are combined with the other DTAs in the assessment of the realizability of the total DTAs of a given tax-paying component of the entity. If the future income —including the expected recovery of value related to the debt securities — is not sufficient to realize the DTAs, a VA is required.

In a recent meeting, the FASB discussed this matter and decided that "View 2" would be required under the guidance on the classification and measurement of financial instruments to be issued later this year. This decision remains tentative until the release of a final ASU by the FASB and entities currently applying "View 1" would not be required to revise their accounting policies until the effective date of the ASU, which is likely several years away. If an entity is considering changing its accounting policy in this regard before then, preferability analysis may be required under ASC 250.

Tax law developments

Under U.S. GAAP, the effects of new legislation are recognized upon enactment (ASC 740-10-25-47). More specifically, the effect of a change in tax laws or rates on a DTL or DTA is recognized as a discrete item in the interim period that includes the enactment date. The tax effects of a change in tax laws or rates on taxes currently payable or refundable for the current year are reflected in the computation of the annual effective tax rate (AETR) after the effective dates prescribed in the statutes, beginning no earlier than the first interim period that includes the enactment date of the new legislation. However, any effects of a tax law or rate change on taxes payable or refundable for a prior year, such as when the change has retroactive effects, is recognized upon enactment as a discrete item of tax expense or benefit for the current year.

Uncertain tax positions: The evaluation of new information may lead to subsequent changes in judgment as it relates to a particular position. Pursuant to ASC 740-10-25-15, a change in judgment that results in subsequent recognition, derecognition or a change in measurement of a position taken in a prior annual period must be recognized as a discrete item in the period in which the new information becomes available. ASC 740 states that the measurement of a tax position should "be based on management's best judgment given the facts, circumstances, and information available at the reporting date." Additional analysis of *existing* information would not typically constitute new information for purposes of adjusting prior estimates.

Classified balance sheet: An entity that presents a classified balance sheet must classify the deferred balances as either current or noncurrent on the basis of the financial accounting classification of the related liability or asset for which a temporary difference exists. A deferred tax balance that is not related to an asset or liability for financial reporting purposes, such as the deferred tax consequences related to an operating loss or a tax credit carryforward, is classified in accordance with the expected reversal date of the related temporary difference or tax attribute. The effect of a change in tax law on the current or noncurrent classification of a deferred tax amount that is not related to an asset or liability for financial reporting purposes should be recognized in the financial statements of the interim or annual period that includes the enactment date.

Tax expense: For both calendar and non-calendar-year-end reporting entities, the effect of the tax law change on prior-year taxes and on deferreds existing as of the enactment date would be presented as a component of income tax expense or benefit from continuing operations. The effects of changes in tax law on items not included in income from continuing operations (e.g., discontinued operations and other comprehensive income) arising in the current year and before the enactment date should be included in the current interim period as part of income from continuing operations. The effect of the change on total tax expense or benefit (current and deferred) related to post-enactment income would be allocated between continuing operations and other financial statement components in accordance with the intraperiod tax allocation guidance in ASC 740-20.

The topics below highlight what we believe are significant tax law developments that should be considered during the preparation of the financial statements. However, note that this is not a complete list of all recent tax law changes.

International

India: In a decision issued on April 25, 2014, on an appeal of a ruling from India's Authority for Advance Rulings (AAR), the Delhi High Court held that reimbursements of salaries by an Indian company to its overseas parent in relation to the secondment of employees would qualify as fees for technical services (FTS) under India's tax treaties with the UK and Canada. At the same time, the court ruled the services performed by the employees on secondment created a permanent establishment (PE) for the overseas parent. The decision is controversial because, under India's treaties with the UK and Canada, where payments qualify as FTS, the activities that generate such payments are specifically excluded from activities that can create a service PE; the court's decision, however, seems to suggest that the relevant payments qualify as FTS and that a service PE exists. For additional details on the India court ruling, see Deloitte's May 23, 2014 World Tax Advisor.

Italy: On April 24, 2014, the Italian Government passed the Law Decree n. 66 (published in the Official Gazette on the same date), to be converted into Law by June 23, 2014. The standard Italian regional production tax (IRAP) rate, previously at 3.9% has been reduced to 3.5% — while the standard rates were also reduced for financial institutions from 4.65% to 4.2% and for insurance companies from 5.9% to 5.3%. The new IRAP rates will be effective for fiscal years beginning after December 31, 2013.

Norway: Norway's Ministry of Finance issued regulations on April 24, 2014 that set out certain exceptions to the application of the interest deduction limitation rules. The initial interest deduction limitation rules were adopted in 2013 and are applicable for fiscal year 2014. The rules primarily limit the deduction of interest expense on related party debt to prevent earnings stripping, but also will capture interest on third-party debt if a related party provided security for the debt. The newly issued regulations exempt the following securities provided by related parties:

- Security provided by a company or entity that is at least 50% owned or controlled directly or indirectly by the borrower; and
- Security in the form of a pledge of shares or loan notes issued by the borrower.

If the security falls within one of these exceptions, interest expense on the external loan will be fully deductible for the borrower, regardless of the security granted by the related party. For additional details on the new Norway regulations, see Deloitte's **Norway Tax Alert**.

Singapore: The Singapore Inland Revenue Authority issued new guidelines on May 19, 2014 regarding the tax treatment of hybrid financial instruments. The guidelines address the factors generally used to determine whether they are debt or equity instruments for income tax purposes. The Singapore regulations, in English, can be found **here**.

Venezuela: The Commission for the Administration of Foreign Exchange (CADIVI) until recently controlled the sale and purchase of foreign currency in Venezuela and set an official exchange rate of 6.3 Venezuelan bolivar fuertes (BsF) to 1 U.S. dollar (USD) (the "official rate"). In 2013, the Venezuelan government authorized certain companies that operate in designated industry sectors to exchange a limited volume of bolivars for dollars at a bid rate established via weekly auctions under the Complementary System of Foreign Currency Acquirement ("SICAD 1").

Effective January 24, 2014, changes to the country's foreign exchange system were enacted by the Venezuelan government. The law (Convenio Cambiario 25) expanded the types of transactions that may be subject to a weekly auction process. In February 2014, the Venezuelan government announced plans for another currency exchange mechanism ("SICAD 2"), which:

- Is expected to provide a greater supply of USD from sources other than the Venezuelan government.
- Is expected to allow all sectors and companies to participate.
- Is regulated by the Venezuelan government.
- Permits USD to be offered in cash or bonds.

The SICAD 2 rate is intended to more closely resemble a market-driven exchange rate than the rates provided by Venezuela's other regulated exchange mechanisms (i.e., the official rate and the SICAD 1 rate). SICAD 2 became effective on March 24, 2014, and yielded an exchange rate significantly higher than the rates established through the other regulated exchange mechanisms.

As of March 31, 2014, an entity may be able to convert BsF to USD at one of three legal exchange rates obtained via the following four exchange rate mechanisms:

- CENCOEX (official rate).
- CENCOEX (latest published SICAD 1 rate).
- SICAD 1 auction (SICAD 1 rate).
- SICAD 2 auction (SICAD 2 rate).

For accounting considerations including remeasurement in an environment with multiple exchange rates, classified balance sheet considerations, deconsolidation and impairment considerations, and the need for robust disclosure, please read **Financial Reporting Alert 14-1**. We encourage entities with Venezuelan operations to consult with their accounting advisers and legal counsel.

U.S. Federal

IRS publishes guidance on how tax principles apply to transactions using convertible virtual currency

On March 25, 2014, the IRS issued Notice 2014-21, which clarifies the IRS position on convertible virtual currency. The Notice provides that convertible virtual currency is treated as property for federal tax purposes and would be subject to general tax principles applicable to property transactions. The Notice defines virtual currency as a "[D]igital representation of value that functions as a medium of exchange, a unit of account, and/or a store of value" and virtual currency that has an equivalent value for real currency is "convertible" virtual currency. An example of convertible virtual currency is Bitcoin, which can be digitally traded and purchased or exchanged into U.S. dollars, Euros, or other currencies.

The Notice discusses potential tax consequences of transactions in, or with, virtual currency, and sets forth guidance on various tax situations including: payment for goods or services, determination of fair market value, gain or loss upon exchange, mining of virtual currency, virtual currency as wages or income, information reporting, backup withholding, and penalties. The Notice states that taxpayers who receive virtual currency as payment for services must, in computing gross income, include the fair market value of the virtual currency, measured in U.S. dollars, as of the date that the virtual currency was received. The basis of the virtual currency that a taxpayer receives as payment for goods or services is the fair market value of the virtual currency in U.S. dollars, as of the date of the receipt of the virtual currency.

A taxpayer that exchanges virtual currency for other property or services may have gain or loss on the transaction, to the extent that the value of the property received is more or less than the taxpayer's basis in the virtual currency. The character of the gain or loss will generally depend on whether the virtual currency is a capital asset in the hands of the taxpayer. For example, stocks, bonds and other investment assets are generally capital assets, whereas, inventory and other property held mainly for sale to customers in a trade or business would not be capital assets. It is important to note that the Notice does not provide a safe harbor for virtual currency treatment prior to the issuance date of March 25, 2014. Accordingly, taxpayers should be aware of this guidance and consider potential tax ramifications when utilizing virtual currency. For additional details on the new virtual currency guidance, see Deloitte's May 2014 **IRS Insights**.

Federal update on safe harbor election for success-based fees paid to professionals other than investment bankers

Rev. Proc. 2011-29 allows taxpayers to make a safe harbor election for years ending after April 8, 2011 to treat 70% of success-based fees paid in connection with a covered transaction, as defined in Treas. Reg. § 1.263(a)-5(e), as an amount that does not facilitate the transaction for purposes of capitalization under

section 263(a). In 2013, the The Large Business and International (LB&I) issued a directive4 stating that LB&I auditors would not challenge a taxpayer's safe harbor treatment of its milestone payments for investment banking services made in the course of certain acquisitions that are creditable against a success-based fee. On January 27, 2014, the LB&I Division of the IRS issued an updated directive (**LB&I-04-0114-001**) (the "Revised Directive")[5], revising the definition of a "milestone" for purposes of applying the safe harbor provided in Rev. Proc. 2011-29 to non-refundable payments contingent upon the achievement of a milestone ("milestone payments"). Under the Revised Directive, the term milestone has been significantly broadened and now includes an event, including the passage of time, occurring in the course of a covered transaction — whether the transaction is ultimately completed or not. As previously noted in **Chief Counsel Advice (CCA) 201234027**, the National Office of the IRS does not agree with the Directives that non-refundable milestone payments qualify as success based fees.

On May 29, 2014, the Special Counsel to the Office of Associate Chief Counsel (Income Tax and Accounting) at the IRS clarified at a Federal Bar Association insurance tax seminar that taxpayers may include success-based fees paid to professionals other than investment bankers when making a safe harbor election under Rev. Proc. 2011-29 for allocating such fees paid in business acquisitions or reorganizations. The clarification was in response to confusion, created as a result of the Directives referenced above, as to whether the safe harbor applied to service providers other than investment bankers.

U.S. Multistate

Indiana: Currently, Indiana's corporate tax rate is 7.5% and, under previous law, had been scheduled to decrease to 7% after June 30, 2014, and to 6.5% after June 30, 2015. Effective July 1, 2014, a new law (S.B. 1) phases in revised state corporate tax rate reductions, eventually lowering the corporate tax rate to 4.9% after June 30, 2021. The corporate rates for subsequent periods will be reduced pursuant to the following schedule:

- After June 30, 2016, 6.25%
- After June 30, 2017, 6.0%
- After June 30, 2018, 5.75%
- After June 30, 2019, 5.5%
- After June 30, 2020, 5.25%
- After June 30, 2021, 4.9%

Additionally, the new law phases in revised financial institution tax (FIT) rate reductions, eventually lowering the FIT rate to 4.9% for tax years beginning after December 31, 2022. Currently, Indiana's FIT rate is 8% and, under previous law, had been scheduled to decrease to 7.5% for tax years beginning after December 31, 2014, to 7% for tax years beginning after December 31, 2015, and to 6.5% for tax years beginning after December 31, 2016. The FIT rates for subsequent periods will be reduced pursuant to the following schedule:

- After December 31, 2016, 6.5%
- After December 31, 2018, 6.25%
- After December 31, 2019, 6.0%
- After December 31, 2020, 5.5%
- After December 31, 2021, 5.0%
- After December 31, 2022, 4.9%

Michigan: On February 6, 2014, the State of Michigan has adopted into law Senate Bill 337, amending Michigan law with respect to various procedural tax provisions of the Michigan Revenue Act. These amendments include: the addition of deadlines by which certain events must occur within an audit, changes regarding how an audit or other events affect the statute of limitations, the addition of a deemed-denied

[4] LB&I-04-0413-002

[5] The Directives are not an official pronouncement of law, and cannot be used, cited, or relied on as such.

appeal option for certain refund claims, and changes to various responsible person and successor liability provisions. For additional details on the new Michigan tax law, see Deloitte's **Michigan Multistate Tax Alert**.

New Mexico: On March 10, 2014, New Mexico Governor Susana Martínez signed Senate Bill 106. This new law allows Corporate Taxpayers that generate net operating loss (NOL) for tax years beginning on or after January 1, 2013 to carry the loss forward twenty years. Losses generated before January 1, 2013 will continue to have a five year carryforward period.

New York: On March 31, 2014, New York Governor Andrew Cuomo signed the 2014-2015 Budget Act into law (enacted on the same day). The Budget Act *substantially* modifies and reforms various aspects of the New York Tax Law, including: reducing the corporate franchise tax rate on entire net income from 7.1% to 6.5%, effective for taxable years beginning on or after January 1, 2016; eliminating the tax liability on entire net income for "qualified New York manufacturers" for taxable years beginning on or after January 1, 2014; merging the Banking Corporation Tax (Article 32) into the Corporate Franchise Tax (Article 9-A); and a multitude of other changes. Furthermore, the previous physical nexus standards were replaced with a new bright-line statutory nexus threshold, resulting in certain corporations having a new New York filing obligation. The proposed (and fully enacted) New York law changes were previously highlighted in the **March 31, 2014, Accounting for Income Taxes Hot Topics Newsletter**. Furthermore, the New York law change is analyzed in Deloitte's **Sweeping New York State Reforms Enacted Multistate Alert** and an article published in the Bloomberg BNA Weekly State Tax Report (May 16, 2014), titled "**New York State Corporation Tax Reforms of 2014.**" Refer to these publications for an in-depth analysis on this law change.

Rhode Island: On June 19, 2014, Rhode Island Governor Lincoln Chafee signed into law the fiscal 2015 Budget, Bill No. H 7133 SUB A as amended (H.B. 7133) law. The new law substantially modifies and reforms various aspects of the Rhode Island Tax Law, including the following:

- Requires water's edge combined reporting for members of a unitary group of affiliated business entities that are more than 50% commonly owned and controlled. Such combination may, by way of a five-year binding election, be done on an affiliated group basis.
- Reduces the corporate income tax rate from 9% to 7%.[6]
- Adopts single-sales factor apportionment, with market-based sourcing for sales of other than tangible personal property. Each unitary business group member's receipts will be included without regard to whether the member has nexus in the state (i.e., the "*Finnigan"* approach).[7]
- Repeals the related-party expense addback requirement.
- Repeals the franchise tax.

The tax law changes contained in H.B. 7133 are effective for tax years beginning on or after January 1, 2015. For additional details on the new Rhode Island tax law, see Deloitte's **Rhode Island Multistate Tax Alert.**

Wisconsin: Effective March 26, 2014 and applicable to taxable years beginning on or after January 1, 2014, net business losses may be carried forward 20 years (previously, 15 years) for state corporate income tax purposes (S.B.1).

Looking forward

The section below highlights some of the legislative proposals that may affect a company's income tax provision in the future. An entity should not consider changes in tax laws or rates when assessing the realizability of a DTA before the period in which the change is enacted. This is an exception to the general

[6] H.B. 7133 Article 12 §15; R.I. Stat. §44-11-2(a). Tax rate reductions under the Jobs Development Act are preserved in H.B. 7133 however subject to updated limitations set forth in R.I. Stat. §42-64.5-4(a)(ii) and R.I. Stat. §42-64.14-11(a), (b).

[7] H.B. 7133 Article 12 §17; R.I. Stat. §44-11-14(b). The "*Finnigan*" approach is in reference to the California State Board of Equalization ("SBE") decisions in Appeal of Finnigan Corp. (88-SBE-022), decided on August 25, 1988 ("Finnigan I") and Appeal of Finnigan Corp. (88-SBE-022-A), Opinion on Petition for Rehearing, decided on January 24, 1990 ("Finnigan II"). In these decisions, for purposes of calculating the California sales factor, the SBE interpreted the term "taxpayer" to mean all members of a unitary group.

rule in ASC 740-10-30-17, under which entities should consider all currently available information about future events when determining whether a valuation allowance is needed for a DTA. Financial statement preparers should consider whether potential changes represent an uncertainty that management reasonably expects will have a material effect on the results of operations, liquidity, or capital resources. If so, financial statement preparers should consider disclosing information about the scope and nature of any potential material effects of the changes.

House Subcommittee hears testimony on Mobile Workforce Act (Pending H.R. 1129)

On April 29, 2014, the U.S. House of Representatives Judiciary Subcommittee on Regulatory Reform, Commercial and Antitrust Law held a hearing on the Mobile Workforce State Income Tax Simplification Act of 2013 (H.R. 1129). As Full Committee Chairman Goodlatte stated in his opening remarks, if adopted into law, the Bill "creates a bright-line thirty-day threshold to determine nonresident income tax liability . . . [and] ensures that employees will have a clear understanding of when they are liable for nonresident state income taxes, and employers will be able to accurately withhold these taxes." This hearing does not relate to a Corporation's income tax nexus, just the payroll withholding obligations for their employees. In light of ongoing state audit activity, taxpayers should consider whether their current employment tax reporting, withholding and compliance processes are up-to-date as well as whether they are prepared for the possibility of federal legislation in this area. For additional details on this hearing, see Deloitte's **Mobile Workforce Act Multistate Tax Alert**.

Retroactive anti-inversion legislation introduced in Congress

Michigan Democrats and brothers Sen. Carl Levin and Rep. Sander M. Levin introduced similar legislation on May 20th to tighten inversion rules which attempt to prevent U.S. companies from moving their tax residence overseas to avoid U.S. taxation. Both the Senate bill and House bill would treat a foreign corporation as a domestic corporation if it meets one of two tests. The first test is based on continuing ownership of legacy shareholders, but the bills would drop the current threshold of 80% to 50%. The second test would be based on management and control, without regard to continuing ownership by legacy shareholders of a domestic corporation. The similar bills would retroactively hinder the ability of U.S. companies for transactions on or after May 8, 2014. While the introduction of the two Levin bills may garner some press attention, their prospects for enactment are uncertain – especially as House and Senate Republicans have so far shown little appetite for addressing inversions outside of a tax code overhaul that lowers corporate tax rates and embraces a territorial system for taxing income of U.S. multinationals. However, this is an issue that needs to be followed closely as an increase in the number of companies attempting inversions could put additional political pressure on lawmakers to act. For additional details on this proposed legislation, see Deloitte's **Tax News and Reviews**.

Organization for Economic Cooperation and Development (OECD) update

The OECD has made considerable progress on the OECD/G20 BEPS project toward the goal of the G20 approving the BEPS transfer pricing deliverables in September 2014. Although the work of the OECD on BEPS is not complete, increasingly countries are not waiting for the final reports to take unilateral action. Especially with respect to the transfer pricing items, some local tax authorities are moving ahead with inquiries focusing on both information and theories they believe are consistent with the direction of the Action Plan items. An OECD working party (committee) has reached consensus on a new approach on transfer pricing documentation, which will include three levels of documentation:

- A country-by-country (CbC) template that will provide high-level financial and activity information for group members that will be used for risk assessment;
- A master file that will provide a big-picture view of the business's global operations; and
- A local file that will provide a detailed transfer pricing analysis.

Companies should continue to closely monitor these developments and be prepared to make appropriate adjustments to their global transfer pricing policies and their approach to resolving transfer pricing disputes. For additional details on the recent OECD developments, refer to the below resources:

- Deloitte archived Dbriefs webcasts[8]:
  - **BEPS and Financial Services: Addressing Unintended Consequences of OECD Guidance**
  - **Base Erosion and Profit Shifting (BEPS): What's Happened So Far? And What's Next?**
  - **Transfer Pricing Documentation and OECD's Country-by-Country Reporting: A First Look at the New Template**
- **Deloitte BEPS Central** —your one-stop shop for information on the BEPS Project. Here you can find all the official documents on the BEPS Project, as well as related Deloitte comments.
- **Deloitte Transfer Pricing Alert - OECD BEPS Transfer Pricing Deliverables on Track for September G20.**
- Deloitte Arm's Length Standard **February OECD Special Edition**, **February/March Issue** and **April/May Issue**.

Chile: Sweeping tax reform bill presented to congress

Chile's new president, Michelle Bachelet, presented a comprehensive tax reform bill to the National Congress on 1 April 2014. The proposed reform—which is broader than anticipated—primarily aims to increase tax revenue to fund an extensive reform of the education system, but also is designed to provide for a more equitable distribution of the tax burden, promote investment and savings and reduce tax avoidance. Many of the proposed changes would have an effect on companies (both domestic and foreign) doing business in the country. The most important proposals include the following:

- A gradual increase in the corporate income tax rate from the current 20% to 25%;
- A shift from shareholder/partner taxation on a cash basis to taxation on an accrual basis;
- New restrictions on interest deductions;
- New restrictions on payments to related entities abroad;
- The introduction of controlled foreign company (CFC) rules;
- The introduction of a general anti-avoidance rule; and
- Repeal of the foreign investment statute.

The governing coalition holds a sufficient majority in Congress to push the reform through, and it hopes to be able to enact the reform within the next four months. If enacted in its current form, the bill would adversely affect certain Chilean investment structures, in particular, the use of leveraged acquisitions. For additional details on the proposed Chile tax reform, see Deloitte's April 17, 2014 **Chile Tax Alert**.

Germany: Draft decree issued on interpretation of change-in-ownership rules

The German tax authorities have issued a draft decree outlining their interpretation of the change-in-ownership rules. The decree is intended to update a 2008 decree and includes, for the first time, guidance on the intra-group restructuring exemption rule and the built-in gains exemption rule. For additional details on the new German guidance, see Deloitte's May 23, 2014 **World Tax Advisor**

[8] Webcasts are archived for only 180 days after the live broadcast.

Learn more

Financial Reporting for Taxes Training: Professionals continue to face significant challenges in financial accounting and reporting for income taxes. Deloitte's winter 2014 training program can help you stay informed. A five-day program with multiple course offerings that allow the participant to choose the appropriate courses for his or her needs is set for December 8 – 12 in Las Vegas, Nevada. Course descriptions, pricing, registration, and additional information can be found **here**.

Accounting for Income Taxes – Global Tax Developments: This publication is issued on a quarterly basis and also periodically, as warranted by specific changes, and provides a user-friendly source of global tax information that may be considered in conjunction with accounting for income taxes under U.S. GAAP. It generally includes a brief summary of major international income tax developments and provides a summary of combined tax rates applicable in several key jurisdictions and the dates of enactment of rate changes, if applicable, under U.S. GAAP. The publication also contains select sample financial statement disclosures that may be considered relevant to accounting for income taxes. The June 2014 publication and archives of prior issues can be found **here**.

Example Disclosure: Accounting for Income Taxes: This example disclosure summarizes accounting and disclosure requirements outlined in SEC Regulation S-K, SEC Regulation S-X, and FASB ASC Topic 740, *Income Taxes*. The information in this example disclosure reflects pronouncements that are effective as of December 31, 2013. A copy of this publication can be found **here**.

Example SEC Comments: Income Taxes: We have compiled a sample of comments issued to public registrants by the SEC on income tax matters under ASC 740. A copy of this publication can be found **here**.

Additional resources that you may find helpful:

- **Deloitte Financial Accounting & Reporting - Income Taxes Home Page**
- **Deloitte Dbriefs Webcasts Archive**
- **Deloitte Heads Up Newsletter Archive**
- **Other Deloitte Tax Publications**

Talk to Us

If you have any questions or comments about the ASC 740 implications described above or other content of *Accounting for Income Taxes Quarterly Hot Topics,* contact the Deloitte Washington National Tax Accounting for Income Taxes Group at: **USNationalWNTActIncomeTaxesGrp@deloitte.com**

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