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Frequently Asked Questions About Tax Reform

Introduction

On December 22, 2017, President Trump signed into law the tax legislation commonly known as the Tax Cuts and Jobs Act (the "Act").¹ Under ASC 740,² the effects of new legislation are recognized upon enactment, which (for federal legislation) is the date the president signs a bill into law. Accordingly, recognition of the tax effects of the Act is required in the interim and annual periods that include December 22, 2017.

This *Financial Reporting Alert* (FRA) contains responses to frequently asked questions (FAQs) about how an entity should account for the tax effects of the Act in accordance with ASC 740. While the answers to the FAQs reflect our current views, these views are subject to change on the basis of additional input received or further developments in practice. We plan to continue to update this document to reflect developments as they occur and as additional questions surface. The following is a high-level summary of the updates to this FRA thus far:

- Originally issued on January 3, 2018.
- Updated on January 19, 2018, to address a number of additional FAQs and to reflect the activities of the FASB and its staff.
- Updated on March 20, 2018, to cover a number of additional FAQs (e.g., a new section on interim considerations was added) and to incorporate guidance that previously appeared separately in FRAs 18-3 and 18-4.

¹ H.R. 1/Public Law 115-97, "An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018."

² For titles of *FASB Accounting Standards Codification* (ASC) references, see Deloitte's "[Titles of Topics and Subtopics in the FASB Accounting Standards Codification](#)."

- [Separate-Company Financial Statements](#)
- [Disclosure Considerations](#)
- [IFRS Considerations](#)
- [Interim Reporting Considerations](#)
- [ASU 2018-02](#)

- Updated on June 20, 2018, principally to provide a new section related to the adoption of ASU 2018-02.
- Updated on August 30, 2018, principally to amend, add, or delete certain FAQs related to measuring the U.S. deferred tax impact of future global intangible low-taxed income (GILTI) inclusions for companies that have elected or will elect to use the deferred method.

Amended, added, and deleted FAQs are marked as such in the question line.

SAB 118

Shortly after enactment, the SEC staff issued SAB 118,³ which provides guidance on accounting for the Act's impact. Under SAB 118, an entity would use something similar to the measurement period in a business combination. That is, an entity would recognize those matters for which the accounting can be completed ("Bucket 1"), as might be the case for the effect of rate changes on deferred tax assets (DTAs) and deferred tax liabilities (DTLs). For matters that have not been completed, the entity would either (1) recognize provisional amounts to the extent that they are reasonably estimable and adjust them over time as more information becomes available ("Bucket 2") or (2) for any specific income tax effects of the Act for which a reasonable estimate cannot be determined, continue to apply ASC 740 on the basis of the provisions of the tax laws that were in effect immediately before the Act was signed into law — that is, the entity would not adjust current or deferred taxes for those tax effects of the Act until a reasonable estimate can be determined ("Bucket 3").

i. How do SAB 118 and the need to record "reasonable estimates" interact with the guidance in ASC 740 regarding uncertain tax positions (i.e., FIN 48) with respect to the Act? [Added March 20, 2018]

SAB 118 addresses certain practical problems created by the enactment of a vast amount of new and complex legislation only nine days before December 31, 2017 — the end of a reporting period for most entities. The Act was developed over a very condensed timeframe, and preparers and practitioners had little time to analyze its preliminary or final versions. As a consequence, there may be tax technical matters with respect to the Act for which it is not feasible to prepare a complete "more-likely-than-not" assessment during the enactment period or potentially even in subsequent quarters within the measurement period.

Accordingly, we believe that uncertainties about how the Act should be interpreted may be accounted for provisionally under SAB 118. More specifically, during the one-year measurement period, an entity may account for an uncertain tax technical matter with respect to the Act on the basis of a reasonable estimate of how the Act will ultimately be interpreted. As new information becomes available, an entity would then adjust its provisional estimate until it can complete its more-likely-than-not assessment. It would need to complete that assessment, along with appropriate measurement of the resulting positions, by the end of the measurement period. In a manner consistent with SAB 118, an entity should make a good faith effort to develop reasonable estimates until it prepares a complete more-likely-than-not assessment.

Determining whether a tax technical matter is within the scope of SAB 118 during the one-year measurement period will, of course, depend on the specific facts and circumstances of each individual entity and will require considerable judgment.

³ SEC Staff Accounting Bulletin No. 118.

FASB ASU and Q&As (Updated June 20, 2018)

Since the Act was signed into law, the FASB has issued the following new guidance on accounting for certain aspects of it:

- [Staff Q&A](#) (January 2018) stating that entities that are not SEC registrants may apply SAB 118 to financial statements.
- [Four staff Q&As](#) (January 2018) outlining the FASB staff's interpretations of ASC 740 and U.S. GAAP with respect to (1) discounting of the deemed repatriation transition tax and refundable alternative minimum tax (AMT) credit carryforwards, (2) GILTI, and (3) the base erosion anti-abuse tax (BEAT). See additional discussion in [FAQs 3.2, 4.1, 6.1, and 7.3](#).
- [ASU 2018-02⁴](#) (February 2018), which addresses industry concerns about the requirement in ASC 740 that the effect of a change in tax laws or rates on DTAs and DTLs be included in income from continuing operations in the reporting period that contains the enactment date of the change. That guidance applies even when the tax effects were initially recognized directly in other comprehensive income (OCI) at the previous rate, resulting in "stranded" amounts in accumulated other comprehensive income (AOCI) related to the income tax rate differential. See additional discussion in [FAQs 13.1 through 13.8](#).

Change in Corporate Tax Rate

The Act reduces the corporate tax rate to 21 percent, effective January 1, 2018, for all corporations. Because ASC 740-10-25-47 requires the effect of a change in tax laws or rates to be recognized as of the date of enactment, all corporations, regardless of their year-end, must adjust their DTAs and DTLs as of December 22, 2017. The effect of changes in tax laws or rates on DTAs or DTLs is allocated to continuing operations as a discrete item rather than through the annual effective tax rate (AETR).

1.1 For calendar-year-end entities, what is the impact of the change in the corporate tax rate on DTAs and DTLs that exist as of the enactment date?

DTAs and DTLs that exist as of the enactment date and are expected to reverse after the Act's effective date (January 1, 2018, for calendar-year-end entities) should be adjusted to the new statutory tax rate of 21 percent. Any DTAs and DTLs expected to reverse before the Act's effective date should not be adjusted to the new statutory tax rate.

1.2 If some deferred tax balances are attributable to items of pretax comprehensive income or loss other than continuing operations (e.g., discontinued operations, OCI, or items charged or credited directly to equity), should the adjustment for the effect of the tax rate change still be allocated to continuing operations? [Amended January 19, 2018]

Yes. Under ASC 740-10-45-15, the tax effects of changes in tax laws or rates are allocated to income from continuing operations irrespective of the source of the income or loss to which the deferred tax item is related. In a manner consistent with ASC 740-10-30-26, the tax effects of items not included in continuing operations that arose before the enactment date are measured on the basis of the enacted rate at the time the transaction was recognized. (For more information, see Sections 3.65 and 3.66 of Deloitte's [A Roadmap to Accounting for Income Taxes](#).)

1.2A [Amended and renumbered to [FAQ 13.1](#) on June 20, 2018]

⁴ FASB Accounting Standards Update No. 2018-02, *Income Statement — Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects From Accumulated Other Comprehensive Income*.

1.3 How should a reporting entity compute its temporary differences as of the enactment date when measuring its DTAs and DTLs? [Amended January 19, 2018]

A reporting entity should calculate temporary differences by comparing the relevant book and tax basis amounts as of the enactment date. To determine book basis amounts as of the enactment date, the reporting entity should apply U.S. GAAP on a year-to-date basis up to the enactment date. For example:

- Any book basis accounts that must be remeasured at fair value under U.S. GAAP would be adjusted to fair value as of the enactment date (e.g., certain investments in securities or derivative assets or liabilities).
- Book balances that are subject to depreciation or amortization would be adjusted to reflect current period-to-date depreciation or amortization up to the enactment date.
- Book basis account balances such as pension and other postretirement assets and obligations for which remeasurement is required as of a particular date (and for which no events have occurred that otherwise would require an interim remeasurement) would not be remeasured as of the enactment date (i.e., no separate valuation of the benefit obligation is required as of the enactment date) for purposes of adjusting the temporary difference that will be measured to the new statutory tax rate as of December 22, 2017. For example, a calendar-year reporting entity that has a pension plan with an annual measurement date of December 31 would adjust its balance sheet accounts for the effects of current-year net periodic pension cost and other contribution and benefit payment activity through the date of enactment.
- Any book basis balances associated with share-based payment awards that are classified as liabilities would be remeasured (on the basis of fair value, calculated value, or intrinsic value, as applicable) as of the enactment date. In addition, for those share-based payment awards that ordinarily would result in future tax deductions, compensation cost would be determined on the basis of the year-to-date requisite service rendered up to the enactment date.

1.4 Given that the enactment date may be close to, but does not coincide with, the end of a reporting period, may an entity measure the effect by using temporary differences and the resulting deferred tax balances as of the end of the reporting period?

No. Subject to materiality, an entity should adjust DTAs and DTLs for the effect of a change in tax laws or rates as of the enactment date even if such date does not coincide with the end of a financial reporting period.

1.5 How should the tax effects of adjustments to book and tax bases up to the enactment date be allocated among the components of comprehensive income?

The tax effects of year-to-date activity *before* enactment would be allocated in accordance with the intraperiod tax allocation guidance in ASC 740-20.

1.6 Are the calculations for fiscal-year-end entities the same as those discussed in [FAQ 1.1](#)?

Not exactly. Given the mechanics of Internal Revenue Code (IRC) Section 15,⁵ we believe that the change in tax rate resulting from the Act will be administratively effective for a fiscal-year-end entity at the beginning of the entity's fiscal year. Accordingly, in a manner consistent with the guidance in ASC 740-270-55-50 and 55-51, the applicable tax rates for deferred tax balances are as follows:

⁵ IRC Section 15, "Effect of Changes."

- For balances expected to reverse after the enactment date and within the current fiscal year, the applicable rate is the “blended tax rate” (see FAQ 1.7 below), which will be effective for the fiscal year.
- For balances not expected to reverse within the current fiscal year, the applicable rate is the new statutory tax rate of 21 percent, which will be effective for the first fiscal year beginning after January 1, 2018.

1.7 What is meant by the “blended tax rate,” and how is it calculated?

For the period that includes enactment, the blended tax rate should be determined in accordance with IRC Section 15 and therefore based on the applicable rates before and after the change and the number of days in the period within the taxable year before and after the effective date of the change in tax rate.

As illustrated in the table below, the domestic federal statutory tax rate (blended tax rate) for all non-calendar-year-end entities with the same fiscal year-end will be the same, regardless of income (or projected income used for interim reporting). It is assumed in the table that the entities’ fiscal year-end is March 31, 2018, and the effective date of the new tax rate is January 1, 2018.

	Tax Rate	Days Under Tax Rate	Tax Ratio	Tentative Tax Rate
Effective rate before enactment (April 1, 2017, to December 31, 2017)	35%	275	75.34%	26.37%
Effective rate after enactment (January 1, 2018, to March 31, 2018)	21%	90	24.66%	5.18%
Domestic federal statutory tax rate (blended tax rate)		365		31.55%

1.8 Since a fiscal-year-end entity will also have to calculate an AETR for its current fiscal year, how should the change in tax rate be factored into its AETR (exclusive of any adjustment for permanent items) for interim periods ending after the enactment date?

In a manner consistent with the guidance in IRC Section 15 discussed above, such an entity should use its blended tax rate to calculate the U.S. federal tax expense/benefit to include in its AETR computation. The new AETR would then be applied to pretax income or loss for the year to date at the end of the interim period that includes the enactment date, and for all subsequent interim periods in the year.

1.9 What rate should a fiscal-year-end company use as the statutory tax rate when preparing rate reconciliation disclosures as required by ASC 740-10-50-11?

The entity should use the blended tax rate as explained in [FAQ 1.7](#).

1.10 If the exception in ASC 740-20-45-7 is applicable in the annual period that includes the enactment date, should an entity consider the change in the corporate tax rate in applying the exception? [Added January 19, 2018]

Yes. An entity must consider taxable income expected in future years for measurement of a DTA related to the carryforward of a current-year loss from continuing operations. For example, assume that a calendar-year-end company with a full valuation allowance has a current-year \$1,000 loss in continuing operations and a \$100 gain reported in OCI related to an available-for-sale (AFS) security that is in an overall gain position, resulting in a DTA and

DTL of \$210 and \$21, respectively, as of December 31, 2017. A \$21 tax benefit and \$21 tax expense would be allocated to continuing operations and OCI, respectively. See Sections 7.07 and 7.21A of Deloitte's [A Roadmap to Accounting for Income Taxes](#) for more information.

Modification of Carryforwards and Certain Deductions

Modification of Net Operating Loss Carryforwards

The Act modifies aspects of current law regarding net operating loss (NOL) carryforwards. Under current law, NOLs generally have a carryback period of 2 years and a carryforward period of 20 years. For NOLs incurred in years subject to the new rules, the Act eliminates, with certain exceptions, the NOL carryback period and permits an indefinite carryforward period. The amount of the NOL deduction is limited to 80 percent of taxable income, which is computed without regard to the NOL deduction.

2.1 Should a taxable temporary difference associated with an indefinite-lived asset be considered a source of taxable income to support realization of an NOL with an unlimited carryforward period? What if a deductible temporary difference is expected to reverse into an NOL with an unlimited carryforward period?

A taxable temporary difference associated with an indefinite-lived asset is generally considered to be a source of taxable income to support realization of an NOL with an unlimited carryforward period. This would also generally be true for a deductible temporary difference that is scheduled to reverse into an NOL with an unlimited carryforward period. However, because the Act includes restrictions on the ability to use NOLs with unlimited carryforward periods (i.e., NOLs arising in years subject to the new rules are limited in use to 80 percent of taxable income), only 80 percent of the indefinite-lived taxable temporary difference would serve as a source of taxable income. See Section 4.27 of Deloitte's [A Roadmap to Accounting for Income Taxes](#) for more information.

Limitation on Business Interest

Under current law, IRC Section 163(j) limits the ability of certain corporations to deduct interest paid or accrued on indebtedness. In general, this limit applies to interest paid or accrued by certain corporations (when no U.S. federal income tax is imposed on the interest income) whose debt-to-equity ratio exceeds 1.5 to 1.0 and when net interest expense exceeds 50 percent of the adjusted taxable income.

The Act removes the debt-to-equity safe harbor, expands interest deductibility limitations, and generally limits the interest deduction on business interest to (1) business interest income plus (2) 30 percent of the taxpayer's adjusted taxable income.

2.2 When an entity develops an objective and verifiable estimate of future taxable income in its assessment of the realizability of its DTAs, can the entity adjust its historical operating results to factor in the effects of adjustments to IRC Section 163(j) resulting from the Act? [Added January 19, 2018]

Yes. An entity should consider the effects of the new IRC Section 163(j) limitation in a manner similar to nonrecurring items for which the entity makes an adjustment in its historical results. However, the ability to adjust historical operating results to obtain an objectively verifiable estimate of future taxable income does not change the fact that the entity would still need to consider such losses as part of its prior earnings history (i.e., the entity may not exclude such losses in determining whether it has cumulative losses in recent years).

For more information, see Sections 4.40 and 4.41 of Deloitte's [A Roadmap to Accounting for Income Taxes](#).

2.3 Should a taxable temporary difference associated with an indefinite-lived asset be considered a source of taxable income to support realization of disallowed interest carryforwards? What if an entity has both disallowed interest carryforwards and NOLs with an unlimited carryforward period? [Added June 20, 2018]

Yes, as discussed in [FAQ 2.1](#), a taxable temporary difference related to an indefinite-lived asset can be a source of taxable income to support realization of DTAs with an unlimited carryforward period, such as disallowed interest carryforwards. However, because the Act restricts the amount of net business interest entities can deduct to 30 percent of modified taxable income, no more than 30 percent of the indefinite-lived taxable temporary difference would serve as a source of taxable income with respect to disallowed interest carryforwards.

That said, an entity may sometimes have both NOLs with an unlimited carryforward period *and* disallowed interest carryforwards with an unlimited carryforward period such that portions of the indefinite-lived taxable temporary difference might serve as a source of taxable income for both because of the limitations provided in the Act. For example, because the annual interest limitation is calculated before NOLs are taken into account, the taxable temporary difference associated with an indefinite-lived asset would first be a source of taxable income for the disallowed interest carryforward (limited to 30 percent of the taxable temporary difference, as discussed above), but then any *remaining* taxable temporary difference on the indefinite-lived asset might also be a source of taxable income for NOLs with an unlimited carryforward period (limited to 80 percent of the *remaining* taxable temporary difference, as noted above in [FAQ 2.1](#)).

See Section 4.27 of Deloitte's [A Roadmap to Accounting for Income Taxes](#) for more information.

Deemed Repatriation Transition Tax (IRC Section 965⁶)

A U.S. shareholder of a specified foreign corporation (SFC)⁷ must include in gross income, at the end of the SFC's last tax year beginning before January 1, 2018, the U.S. shareholder's pro rata share of certain of the SFC's undistributed and previously untaxed post-1986 foreign earnings and profits (E&P). The inclusion generally may be reduced by foreign E&P deficits that are properly allocable to the U.S. shareholder. In addition, the mandatory inclusion may be reduced by the pro rata share of deficits of another U.S. shareholder that is a member of the same affiliated group. A foreign corporation's E&P are taken into account only to the extent that they were accumulated during periods in which the corporation was an SFC (referred to below as a "foreign subsidiary"). The amount of E&P taken into account is the greater of the amounts determined as of November 2, 2017, or December 31, 2017, unreduced by dividends (other than dividends to other SFCs) during the SFC's last taxable year beginning before January 1, 2018. [Amended January 19, 2018]

The U.S. shareholder's income inclusion is offset by a deduction designed to generally result in an effective U.S. federal income tax rate of either 15.5 percent or 8 percent. The 15.5 percent rate applies to the extent that the SFCs hold cash and certain other assets (the U.S. shareholder's "aggregate foreign cash position"), and the 8 percent rate applies to the extent that the income inclusion exceeds the aggregate foreign cash position.

The Act permits a U.S. shareholder to elect to pay the net tax liability⁸ interest free over a period of up to eight years.

⁶ IRC Section 965, "Temporary Dividends Received Deduction."

⁷ An SFC includes all controlled foreign corporations and all other foreign corporations (other than passive foreign investment companies) in which at least one domestic corporation is a U.S. shareholder.

⁸ Net tax liability under IRC Section 965 is the excess, if any, of the taxpayer's net income tax for the taxable year in which the IRC Section 965 inclusion amount is included over such taxpayer's net income tax for the taxable year, excluding (1) the IRC Section 965 amount and (2) any income or deduction properly attributable to a dividend received by such U.S. shareholder from any deferred foreign income corporation.

3.1 Should an entity that is required to include post-1986 foreign earnings in its current-year taxable income but elects to pay the one-time deemed repatriation transition tax (under IRC Section 965) over a period of up to eight years classify the tax as a DTL or a current/noncurrent income tax payable?

In the period of enactment, a U.S. shareholder should record a current/noncurrent income tax payable for the transition tax due. ASC 210 provides general guidance on the classification of accounts in statements of financial position. An entity should classify as a current liability only those cash payments that management expects to make within the next 12 months to settle the transition tax. The installments that the entity expects to settle beyond the next 12 months should be classified as a noncurrent income tax payable.

3.2 If an entity elects to pay the one-time deemed repatriation transition tax over the eight-year period, should the income tax payable be discounted? [Amended January 19, 2018]

Although ASC 740-10-30-8 clearly prohibits discounting of DTAs and DTLs, it does not address income tax liabilities payable over an extended period. In the absence of explicit guidance in ASC 740, we believe that an entity would need to consider ASC 835-30. Specifically, we note the following:

- ASC 835-30 is generally applied to “exchange transactions” rather than nonreciprocal transactions.
- ASC 835-30-15-3(e) notes that the guidance in ASC 835-30 does not apply to “[t]ransactions where interest rates are affected by the tax attributes or legal restrictions prescribed by a governmental agency (for example, industrial revenue bonds, tax exempt obligations, government guaranteed obligations, income tax settlements).”
- Because the amount of the deemed repatriation transition tax is inherently subject to uncertain tax positions, measurement of the ultimate amount to be paid is potentially subject to future adjustment.

Accordingly, we do not believe that the deemed repatriation transition tax should be discounted.

In January 2018, the FASB staff issued a [Q&A](#) stating that the deemed repatriation transition tax liability should not be discounted.

3.3 Depending on the year-ends of a U.S. entity and its foreign subsidiaries, the deemed repatriation transition tax may or may not be reported on the current-year tax return. If the deemed repatriation transition tax will not be reported on the current-year tax return, should the liability for the one-time deemed repatriation transition tax be limited to the amount that corresponds to the entity’s outside basis difference in the foreign subsidiary, or should the entire amount be recorded? [Amended January 19, 2018]

Although we generally believe that the recognition of a liability related to a foreign subsidiary would be limited to the amount that corresponds to the entity’s outside basis difference in the foreign subsidiary, we believe that it would be appropriate to record the entire amount of the deemed repatriation transition tax in the period of enactment given the unique circumstances presented in this FAQ (i.e., the amount due is calculated by reference to the greater of the E&P amounts determined as of November 2, 2017, or December 31, 2017 — that is, E&P related to past transactions — and will simply be payable in a subsequent year).

3.4 If the deemed repatriation transition tax will not be reported on the current-year tax return, should the entity classify the one-time deemed repatriation transition tax as a DTL or a noncurrent income tax payable?

On the basis of the unique nature of tax reform and the mandatory one-time deemed repatriation income inclusion, we believe that the deemed repatriation transition tax liability may be classified as a noncurrent income tax payable.

3.5 With the Act's establishment of a participation exemption system of taxation, does an entity still need to consider whether the outside basis differences in its foreign subsidiaries (and foreign corporate joint ventures that are essentially permanent in duration) are indefinitely reinvested?

Yes. Even under the new tax system, an entity may still be subject to income tax on its foreign investments (e.g., foreign exchange gains or losses on distributions, capital gains on sale of investment, foreign income taxes, and withholding taxes) and should consider whether it needs to record any deferred taxes on outside basis differences in foreign investments. In making this determination, an entity should consider its outside basis differences at each level in the organization chart, starting with the subsidiary at the lowest level in the chain.

3.5A How should the SAB 118 guidance be applied to an entity's indefinite reinvestment assertions under ASC 740-30-25-6, ASC 740-30-25-18(a), and ASC 740-30-25-17? [Added March 20, 2018]

Example 1 in SAB 118 discusses a Bucket 3 fact pattern and states the following:

Prior to the reporting period in which the Act was enacted, Company X did not recognize a deferred tax liability related to unremitted foreign earnings because it overcame the presumption of the repatriation of foreign earnings. [Footnote omitted] Upon enactment, the Act imposes a tax on certain foreign earnings and profits at various tax rates. Based on Company X's facts and circumstances, it was not able to determine a reasonable estimate of the tax liability for this item for the reporting period in which the Act was enacted by the time that it issues its financial statements for that reporting period; that is, Company X did not have the necessary information available, prepared, or analyzed to develop a reasonable estimate of the tax liability for this item (or evaluate how the Act will impact Company X's existing accounting position to indefinitely reinvest unremitted foreign earnings). As a result, Company X would not include a provisional amount for this item in its financial statements that include the reporting period in which the Act was enacted, but would do so in its financial statements issued for subsequent reporting periods that fall within the measurement period, beginning with the first reporting period falling within the measurement period by which the necessary information became available, prepared, or analyzed in order to develop the reasonable estimate, and ending with the first reporting period within the measurement period in which Company X was able to obtain, prepare, and analyze the necessary information to complete the accounting under ASC Topic 740. [Emphasis added]

In addition, SAB 118 indicates that the SEC staff's views were informed by FASB FSP FAS 109-2,⁹ which contains similar guidance and states, in part:

The FASB staff believes that the lack of clarification of certain provisions within the [2004] Act and the timing of the enactment necessitate a practical exception to the Statement 109 [ASC 740] requirement to reflect in the period of enactment the effect of a new tax law. Accordingly, an enterprise is allowed time beyond the financial reporting period of enactment to evaluate the effect of the [2004] Act on its plan for reinvestment or repatriation of foreign earnings for purposes of applying Statement 109 [ASC 740].

Accordingly, we believe that, in a manner similar to the guidance in FSP FAS 109-2, and as specified in Example 1 of SAB 118, an entity should apply ASC 740 as it completes its plans for reinvestment of its outside basis difference, including its plans for reinvestment or repatriation of unremitted foreign earnings. More specifically, to the extent that an entity has finalized its plans and can calculate the resulting tax effects, the entity should disclose those plans and record the associated tax effects (Bucket 1). If an entity has completed all or portions of its

⁹ FASB Staff Position (FSP) FAS 109-2, *Accounting and Disclosure Guidance for the Foreign Earnings Repatriation Provision Within the American Jobs Act of 2004* (superseded).

assessment (e.g., made the decision to repatriate from all or certain entities) and has the ability to reasonably estimate the effects of that assessment (or portions thereof), it should record provisional amounts for those effects and disclose the status of its efforts (Bucket 2). If an entity has made insufficient progress to reasonably estimate its plans, it should disclose the status of its evaluation and should not adjust its previous indefinite reinvestment assertions for the effects of the Act (Bucket 3).

An entity should be mindful that its plans for reinvestment or repatriation of unremitted foreign earnings could be affected by matters other than those associated with the Act. For example, if an entity's cash flow needs in the United States change significantly for reasons other than those caused by the Act (e.g., the need for cash in the United States to pay off debt, settle litigation, or fund an acquisition), the entity should evaluate those matters outside the SAB 118 framework to ensure that its prior intent related to reinvestment is still appropriate.

3.6 If an entity changes its indefinite reinvestment assertion with respect to its investment in a foreign subsidiary (or foreign corporate joint venture that is essentially permanent in duration) because it now intends to distribute earnings subject to the deemed repatriation transition tax, may the entity change its historic accounting policy and approach for determining the DTL for withholding taxes that are within the scope of ASC 740?

Historically, we have accepted the following two approaches for determining whether a parent should recognize a DTL for withholding taxes that would be imposed by the local tax authority on a distribution:

- *Parent jurisdiction approach* — A parent¹⁰ would apply ASC 740-10-55-24 by treating the withholding tax as a tax that the parent would incur upon the reversal of a taxable temporary difference in the parent's jurisdiction that is attributable to its investment in the foreign subsidiary. The parent would be unable to recognize a DTL when the financial reporting carrying value of the investment does not exceed the tax basis in the investment as determined by application of tax law in the parent's jurisdiction. However, if an outside basis difference does exist in the parent's investment in the foreign subsidiary, the parent would apply ASC 740-10-55-24 when measuring the DTL to be recognized.
- *Subsidiary jurisdiction approach* — An entity considers the perspective of the jurisdiction that is taxing the recipient (i.e., the local jurisdiction imposing the withholding tax) when determining whether the parent has a taxable temporary difference. From the perspective of the local jurisdiction, the parent has a financial reporting carrying amount in its investment in the distributing entity that is greater than its local tax basis (i.e., from the perspective of the local jurisdiction, the IRC Section 965(a) transition income inclusion that increased the tax basis is not relevant in the local jurisdiction). Therefore, there is an "outside" taxable temporary difference and, in accordance with ASC 740-10-55-24, the measurement of the DTL should reflect withholding taxes to be incurred when the taxable temporary difference reverses.

These approaches would continue to be appropriate for determining whether a parent should recognize a DTL for withholding taxes after the effective date of the tax law change. For more information about the two approaches, see Section 3.06 of Deloitte's [A Roadmap to Accounting for Income Taxes](#).

Note that the tax effect of any change in the indefinite reinvestment assertion (e.g., a withholding tax DTL) would be considered an indirect effect of tax reform for purposes of the disclosure required under ASC 740-10-50-9(g).

¹⁰ The "parent" in this context is the immediate owner of the investment.

3.7 Should an entity consider the one-time deemed repatriation income inclusion to be a source of income when analyzing the realization of DTAs in the year of the inclusion?

Yes. An entity should consider the one-time deemed repatriation income inclusion to be a source of taxable income when analyzing the realization of DTAs. The entity should verify that the one-time deemed repatriation income inclusion coincides with the timing of the deductions and other benefits associated with the DTAs.

For more information about sources of taxable income that may enable realization of a DTA, see Section 4.22 of Deloitte's *A Roadmap to Accounting for Income Taxes*.

3.8 If a company has the ability and intent to make an election under Revenue Procedure 2006-45 to change a controlled foreign corporation's (CFC's) tax year-end (i.e., to a one-month deferral year as described in Section 898(c)(2)), when should the impact of the change in the CFC's year-end be recognized for financial statement purposes? [Added January 19, 2018]

Generally speaking, an election made under Revenue Procedure 2006-45 would be considered an automatic change from one permissible method to another. Accordingly, the financial statement impact would be reflected in the period in which the entity has concluded that it qualifies for the change in accounting method and that it has the intent and ability to file the change.

For more information about when to recognize the impact of tax method changes, see Section 3.51 of Deloitte's *A Roadmap to Accounting for Income Taxes*.

3.9 What factors should an entity consider in measuring the one-time deemed repatriation transition tax? [Added January 19, 2018]

Typically, we would expect the one-time deemed repatriation transition tax to be based on the facts that exist as of the balance sheet date (e.g., E&P amounts, cash and other asset balances) or a prior date if required by law. However, in some instances, certain actions (or elections) that management expects to take (make) and for which no other impediments or regulatory hurdles to execution exist (i.e., the plans are within the entity's control) can be considered in the measurement of the tax liability. In such cases, an entity would need to use significant judgment and assess its individual facts and circumstances.

Global Intangible Low-Taxed Income

Although the Act generally eliminates U.S. federal income tax on dividends from foreign subsidiaries of domestic corporations, it creates a new requirement that certain income (i.e., GILTI) earned by CFCs must be included currently in the gross income of the CFCs' U.S. shareholder. GILTI is the excess of the shareholder's "net CFC tested income" over the net deemed tangible income return (the "routine return"), which is defined as the excess of (1) 10 percent of the aggregate of the U.S. shareholder's pro rata share of the qualified business asset investment (QBAI) of each CFC with respect to which it is a U.S. shareholder over (2) the amount of certain interest expense taken into account in the determination of net CFC-tested income.

A domestic corporation is permitted a deduction of up to 50 percent of the sum of the GILTI inclusion and the amount treated as a dividend, because the corporation has claimed a foreign tax credit (FTC) as a result of the inclusion of the GILTI amount in income ("IRC Section 78¹¹ gross-up"). If the sum of the GILTI inclusion (and related IRC Section 78 gross-up) and the corporation's foreign-derived intangible income (FDII) (see [FAQ 5.1](#)) exceeds the corporation's taxable income, the deductions for GILTI and for FDII are reduced by the excess. As a result, the GILTI deduction can be no more than 50 percent of the corporation's taxable income

¹¹ IRC Section 78, "Dividends Received From Certain Foreign Corporations by Domestic Corporations Choosing Foreign Tax Credit."

(and will be less if the corporation is also entitled to an FDII deduction). The maximum GILTI deduction is reduced to 37.5 percent for taxable years beginning after December 31, 2025.

4.1 Is a company required to record U.S. deferred taxes for investments in foreign subsidiaries and corporate joint ventures that are essentially permanent in duration (collectively, “foreign investments”) and that are subject to the GILTI provision but otherwise indefinitely reinvested? [Amended January 19, 2018]

If a GILTI inclusion is not expected in future years, no U.S. deferred taxes would be recorded. In addition, even if a GILTI inclusion is expected in future years, U.S. deferred taxes would not be *required*.

In January 2018, the FASB staff issued a [Q&A](#) stating that a company may elect, as an accounting policy, to either (1) treat taxes due on future U.S. inclusions in taxable income under the GILTI provision as a current-period expense when incurred or (2) factor such amounts into the company’s measurement of its deferred taxes (the deferred method). The FASB staff acknowledged that companies that elect to factor GILTI into the measurement of deferred taxes will face additional implementation issues but did not explain how those issues should be addressed.

Note: FAQs 4.2 through 4.9 and 4.11 have been amended, added, or deleted to reflect our current views on the accounting for DTAs and DTLs with basis differences that are expected to affect the amount of GILTI inclusion upon reversal. We have discussed a number of the more significant aspects of these FAQs with the FASB and SEC staff. Accordingly, while other acceptable accounting approaches may exist, entities that plan to apply methods that are inconsistent with those discussed in the FAQs below are strongly encouraged to consult with their income tax accounting advisers.

4.2 If a company expects to have a U.S. inclusion in taxable income under the GILTI provision in future years, and elects to factor such amounts into the measurement of DTAs and DTLs, how should it determine the amount of U.S. investor-level deferred taxes necessary for the related foreign investment? [Amended January 19, 2018; August 30, 2018]

A U.S. investor in a CFC has a financial reporting carrying value (i.e., book basis) and an outside tax basis for U.S. tax purposes in its foreign investment. If those amounts are not the same, the U.S. investor would have an outside basis difference in the foreign investment. In addition, the U.S. investor has U.S. tax basis in the CFC’s underlying assets and liabilities held that will be used for calculating GILTI inclusions. Accordingly, a U.S. investor may have book/U.S. tax inside basis differences that, upon reversal, will increase or decrease the GILTI inclusion and, because GILTI inclusions increase the U.S. tax basis in the foreign investment, will also affect the outside basis difference in the foreign investment.

Accordingly, in determining the amount of U.S.-investor-level deferred taxes necessary for foreign investments under this model, companies should “look through” the outside basis of the CFC to determine how the book/U.S. tax inside basis differences will reverse and how such reversals will affect future GILTI inclusions and the outside basis difference.

Any residual outside basis difference that is not related to the CFC’s underlying assets or liabilities (i.e., inside/outside tax basis disparities) should then be analyzed in the determination of whether that residual basis difference would result in a taxable or deductible amount when the investment is recovered and, if so, whether an ASC 740 outside basis exception (i.e., ASC 740-30-25-18(a) or ASC 740-30-25-9) applies. Unlike other situations involving outside basis differences in foreign subsidiaries, this “look through” approach would be employed even if no overall outside basis difference in the CFC exists, or if only an overall deductible outside basis difference in the CFC exists.

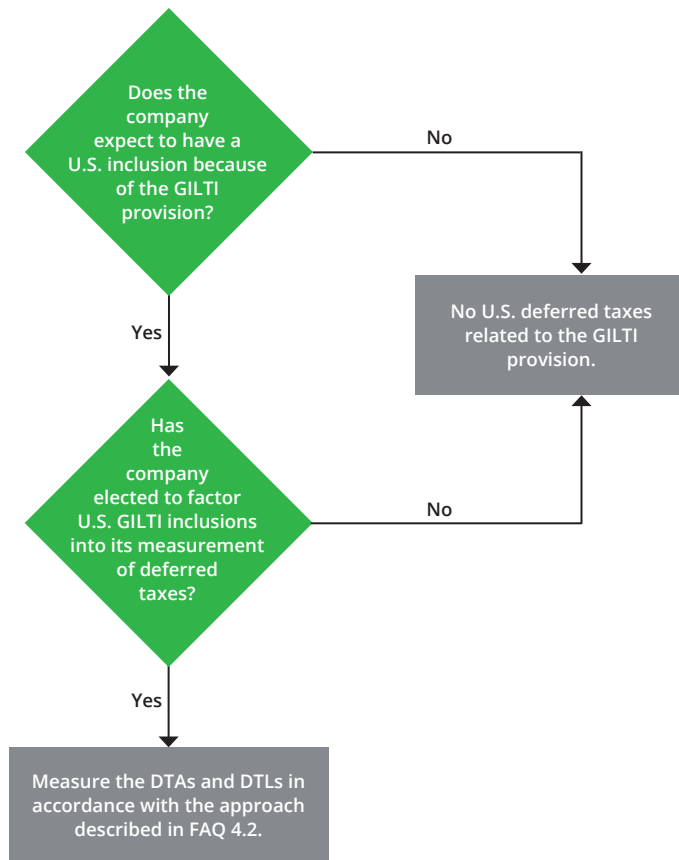
In addition, in assessing the GILTI impact of the CFC's underlying assets and liabilities, a company would, in a fashion similar to branch accounting, establish U.S. DTAs or DTLs to account for the U.S. income tax effects of the future reversal of any in-country DTAs and DTLs (also referred to as "anticipatory foreign tax credit/deduction" or "anticipatory" DTAs and DTLs). When determining the amount of a U.S. anticipatory DTA or DTL, an entity must carefully consider all applicable provisions in the tax law, since the amount of the incremental foreign taxes that will be creditable and realizable, or forgone, because of the future reversal of the local in-country DTAs and DTLs may be difficult to assess and subject to limitations (e.g., an 80 percent limitation, limitations as a result of expense allocations, and a limitation on utilization as a result of the absence of a carryforward or carryback period). For example, a local-country DTL that will reverse in the same year(s) in which a GILTI inclusion is expected may be creditable against the U.S. tax in that year, subject to the 80 percent limitation. In addition, U.S. DTAs that reverse in the same year as the local in-country deferred might further limit the FTC. Future FTCs directly related to future book income and future expense allocation limitations directly related to future book expense generally should not be included in the measurement of the anticipatory DTA or DTL until such income or expense, or both, are recognized (i.e., such FTCs and expense allocation limitations should be limited to those directly tied to existing temporary differences).

For more information about accounting for foreign branch operations, see Section 3.51A of Deloitte's [A Roadmap to Accounting for Income Taxes](#).

In summary, recorded GILTI DTAs and DTLs under this model will consist of the following three items:

- DTAs and DTLs related to inside book/U.S. tax basis differences that will affect future GILTI inclusions, identified by "looking through" the CFC's outside basis to the CFC's underlying assets and liabilities.
- DTAs and DTLs related to the U.S. tax consequences of settling the CFC's in-country DTAs or DTLs (i.e., anticipatory DTAs and DTLs).
- Any DTA or DTL related to a residual outside basis temporary difference for which an exception has not been applied.

The decision tree below illustrates the approach for determining the deferred tax accounting for outside basis differences in foreign investments as a result of the GILTI provision.



4.2A Should GILTI DTAs and DTLs, including U.S. anticipatory DTAs and DTLs, be established on a CFC-by-CFC basis (individual) or a U.S.-shareholder basis (aggregate)? [Added August 30, 2018]

We believe that in a manner consistent with the mechanics of the GILTI computation, GILTI DTAs and DTLs should generally be computed on a U.S.-shareholder-by-U.S.-shareholder basis. Therefore, multiple CFCs under one U.S. shareholder would be analyzed in the aggregate. If a U.S. shareholder has a mixture of profitable and unprofitable CFCs that, in the aggregate, are not profitable such that future GILTI inclusions are not expected at the U.S. shareholder level, no GILTI DTAs and DTLs would be recorded. Conversely, if a U.S. shareholder has a mixture of profitable and unprofitable CFCs that, in the aggregate, are profitable such that future GILTI inclusions are expected, that U.S. shareholder should measure GILTI DTAs and DTLs in accordance with [FAQ 4.2](#).

4.3 Given that the CFC’s routine return is excluded from the GILTI inclusion, how should an entity account for the routine return when recording GILTI DTAs and DTLs? [Amended January 19, 2018; August 30, 2018]

We believe that there is more than one acceptable approach to accounting for the routine return in the measurement of GILTI DTAs and DTLs, including the following:

- *Special deduction* — The routine return could be treated akin to a special deduction, with the benefit recognized when the GILTI inclusion is reduced by the routine return. Under this approach, the routine return is viewed as dependent on future events, including future investments in QBAI and interest expense deductions, and it therefore would not be factored into the tax rate expected to apply to the temporary differences.

- *Graduated tax rate* — Under this approach, the amount of taxable income equal to the routine return would be considered income taxed at a zero rate. Accordingly, if the routine return represents a significant factor, companies would measure GILTI DTAs and DTLs by using the average graduated tax rate applicable to the amount of estimated annual taxable income in the periods in which the aforementioned deferred taxes are estimated to be settled or realized. Companies will need to use judgment in determining the periods in which GILTI DTAs and DTLs will reverse and the estimated annual taxable income in each of those periods. See Sections 4.09 and 4.10 of Deloitte's [A Roadmap to Accounting for Income Taxes](#) for more details.

Other models may also be acceptable in certain situations (e.g., a portion of the book/U.S. tax basis difference that will reverse and represent a routine return might not be considered a taxable temporary difference for which a deferred tax would be recorded in accordance with ASC 740-10-25-30).

The approach an entity selects would be an accounting policy election that, like all other such elections, must be applied consistently.

4.4 Would an acceptable alternative approach to measuring deferred taxes for an outside basis difference in a CFC be to measure deferred taxes “as if” the CFC were a branch? [Amended January 19, 2018; August 30, 2018]

No. While many “branch-like” principles are employed in the model described in [FAQ 4.2](#), unlike a branch, a CFC that will have substantially all of its income taxable in the United States as a result of a GILTI inclusion still has an outside tax basis that is relevant in certain instances, such as a sale or distribution. Accordingly, measurement of deferred taxes should also factor in the residual outside basis difference as described in [FAQ 4.2](#).

For more information about accounting for foreign branch operations, see Section 3.51A of Deloitte's [A Roadmap to Accounting for Income Taxes](#).

4.5 [Deleted August 30, 2018]

4.6 [Deleted August 30, 2018]

4.7 Should the GILTI deduction be considered in the measurement of GILTI DTAs and DTLs? [Added January 19, 2018; Amended August 30, 2018]

The GILTI deduction is intended to lower the GILTI income inclusion (with the intent of lowering the effective tax rate on the included income) and, in many cases, will immediately apply when a company has a GILTI inclusion. Accordingly, we believe that if a company generally expects to be able to apply the full GILTI deduction in the period in which the GILTI DTAs and DTLs reverse, it should consider the deduction in the measurement of the GILTI DTAs and DTLs in accordance with ASC 740-10-55-24. As noted above, however, the GILTI deduction is “up to,” rather than “guaranteed” to be, 50 percent and could be reduced by the taxable income limitation, which is applied in combination with the FDII deduction (see [FAQ 5.1](#)). An entity should carefully consider this limitation when factoring the GILTI deduction into the measurement of U.S. GILTI DTAs and DTLs. For example, when the taxable income limitation and expense allocation limitations are expected to apply and be significant (e.g., in situations in which the U.S. operations generate significant losses or an entity expects to forgo the GILTI deduction because it expects to use existing NOL carryforwards), entities may conclude that factoring the GILTI deduction into the rate is not appropriate. See additional discussion in [FAQ 4.11](#).

4.8 If an entity elects to factor taxes due on future U.S. GILTI inclusions in taxable income into the entity's measurement of its deferred taxes, how should it recognize, upon adoption of ASU 2016-16¹² and the establishment of a DTA for previously unrecognized tax basis in the buyer's jurisdiction, any corresponding change in the measurement of deferred taxes attributable to GILTI? [Added January 19, 2018]

Entities are required to adopt ASU 2016-16 on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the year of adoption. ASC 250-10-45-8 requires entities to include the direct effects of a change in accounting principle, *including any related income tax effects*, when applying that principle retrospectively. Although ASU 2016-16 will be applied on a modified retrospective basis, we believe that a similar concept would apply in this situation. Therefore, the corresponding change in the measurement of deferred taxes attributable to GILTI would be considered a direct effect and, accordingly, would be recognized as an adjustment directly to retained earnings as well.

4.9 Does SAB 118 apply to the selection of an accounting policy for GILTI in such a manner that an entity can use the measurement period of one year to make its selection? [Added March 20, 2018]

While SAB 118 does not explicitly refer to accounting policy choices, we believe that the following application of its guidance to a company's GILTI policy election would be appropriate:

- A company is not required to adopt an accounting policy for GILTI in the financial statements for the period that includes the enactment date. To create and preserve the flexibility to make that election at some time during the measurement period, however, the company must disclose that it has not yet adopted an accounting policy. This guidance applies even if the company already knows, or has reasonable estimates of, the effect of the two different accounting policies on the financial statements and the difference is material.
- If a company's accounting policy is still "open" during any subsequent quarters within the one-year measurement period, a policy is not established by including the current-year estimated actual tax effects of GILTI as a current-period expense in the company's AETR used for calculating its interim tax provision.
- Once a company records deferred taxes with respect to GILTI, and the recognition of such deferred taxes is considered material, the company has elected an accounting policy regardless of whether the amount recorded is considered a provisional amount under SAB 118. Changes made to that policy during or after the measurement period would be subject to ASC 250.
- Subsequent adjustments of the deferred tax amount recorded for GILTI, including adjustments related to the company's policies used to calculate such amount (e.g., inside basis vs. outside basis), would not be subject to ASC 250 provided that (1) they occur during the one-year measurement period and (2) the amounts recorded in prior periods were marked as provisional.
- Once the deferred tax amount for GILTI is considered final, ASC 250 would apply to any future adjustments related to the company's policies used to calculate such amount.

This application of SAB 118 has been discussed with the SEC staff, and we understand that the staff will not object to it as long as a company provides the disclosures required by the SAB.

¹² FASB Accounting Standards Update No. 2016-16, *Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory*.

GILTI Valuation Allowance Considerations

Under the GILTI tax regime, foreign taxes paid or accrued in the year of the inclusion may be creditable against U.S. taxes otherwise payable, subject to certain limitations (e.g., foreign source income, expense allocations). If not utilized in the year of inclusion, however, the FTC would be permanently lost. Further, because Section 250 deductions are limited to 50 percent of taxable income after NOL deductions, utilization of NOLs could reduce or eliminate the eligibility for a Section 250 deduction. In fact, as a result of expected future GILTI inclusions, a U.S. entity that has historically experienced cumulative losses may expect that existing NOL carryforwards, for which a valuation allowance has historically been recorded, will now be utilized. Utilization of the NOL carryforwards may, however, result in an actual cash tax savings that is less than the DTA (before reduction for any valuation allowance) and, in some cases, may result in no cash tax savings at all because, without the NOL, the entity would have been eligible for a Section 250 deduction that would have reduced the net taxable income inclusion and would have been able to utilize FTCs.

4.10 When assessing the realizability of NOL DTAs, how should an entity consider future GILTI inclusions? [Added March 20, 2018]

There are two acceptable views. The first is that an entity would consider future GILTI inclusions on the basis of tax law ordering rules when estimating available sources of future taxable income to assess the realizability of DTAs. Under a tax law ordering approach, the future reduction or elimination of the Section 250 deduction and FTCs will not result in the need for a valuation allowance for an entity's existing NOL DTAs. Use of a tax law ordering approach is consistent with Example 18 in the implementation guidance (see ASC 740-10-55-145 through 55-148). The same conclusion would apply to DTAs for other tax attributes and deductible temporary differences.

Alternatively, an entity could assess the realizability of DTAs on the basis of the incremental economic benefit they would produce. In other words, because future GILTI inclusions are an integrated part of the regular tax system, an entity would determine how much, if any, benefit is expected to be realized from an entity's existing NOL carryforwards on a "with-and-without" basis. That is, a DTA would be recognized for only the amount of incremental tax savings the DTAs are expected to produce after the entity considers all facts and circumstances, elements of the tax law, and other factors that would otherwise limit the availability of the Section 250 deduction and utilization of the FTCs.

4.11 What should the relationship be between an entity's assessment of the realizability of NOL DTAs that may be affected by future GILTI inclusions and its measurement of other U.S. GILTI DTAs and DTLs? [Added August 30, 2018]

We believe that when measuring U.S. GILTI DTAs and DTLs (more specifically, evaluating whether future Section 250 deductions should affect the measurement of GILTI DTAs and DTLs as discussed in [FAQ 4.7](#)), an entity should apply an approach that is consistent with its assessment of how future Section 250 deductions affect the realizability of a NOL DTA, as described in [FAQ 4.10](#).

For example, if the entity evaluates the realizability of NOL DTAs on the basis of the incremental economic benefit the NOLs would produce (i.e., the "with-and-without" approach described in [FAQ 4.10](#)), it would be appropriate for the entity to factor in the Section 250 deduction that would be available without the NOL when measuring its GILTI DTAs and DTLs. Alternatively, if the entity evaluates the realizability of NOL DTAs on the basis of tax law ordering rules, the measurement of GILTI DTAs and DTLs should only take into account the impact of the Section 250 deduction that will actually be available after use of the NOL in the year the GILTI DTAs and DTLs reverse, because the ordering rules would suggest that the maximum amount of GILTI deduction will not be obtained in those circumstances.

Foreign-Derived Intangible Income

The Act allows a domestic corporation an immediate deduction in U.S. taxable income for a portion of its foreign-derived intangible income (FDII). The amount of the deduction depends, in part, on U.S. taxable income. The percentage of income that can be deducted is reduced in taxable years beginning after December 31, 2025.

5.1 How should companies account for the FDII deduction? [Amended January 19, 2018]

We believe that FDII deductions related to future book income are analogous to the special deductions cited in ASC 740-10-25-37 and should be accounted for as such.

For more information, see Section 4.17 of Deloitte's *A Roadmap to Accounting for Income Taxes*.

Base Erosion Anti-Abuse Tax

For tax years beginning after December 31, 2017, a corporation is potentially subject to tax under the BEAT provision if the controlled group of which it is a part has sufficient gross receipts and derives a sufficient level of "base erosion tax benefits." Under the BEAT, a corporation must pay a base erosion minimum tax amount (BEMTA) in addition to its regular tax liability after credits. The BEMTA is generally equal to the excess of (1) a fixed percentage of a corporation's modified taxable income (taxable income determined without regard to any base erosion tax benefit related to any base erosion payment, and without regard to a portion of its NOL deduction) over (2) its regular tax liability (reduced by certain credits). The fixed percentage is generally 5 percent for taxable years beginning in 2018, 10 percent for years beginning after 2018 and before 2026, and 12.5 percent for years after 2025. However, the fixed percentage is 1 percentage point higher for banks and securities dealers (i.e., 6, 11, and 13.5 percent, respectively).

6.1 What tax rate should companies that are subject to the BEAT provisions use when measuring temporary differences? [Amended January 19, 2018]

We believe that the BEAT system can be analogized to an AMT system. ASC 740 notes that when alternate tax systems like the AMT exist, deferred taxes should still be measured at the regular tax rate. Because the BEAT provisions are designed to be an "incremental tax," an entity can never pay less than its statutory tax rate of 21 percent. Like AMT preference items, related-party payments made in the year of the BEMTA are generally the BEMTA's driving factor. The AMT system and the BEAT system were both designed to limit the tax benefit of such "preference items." Further, as was the case under the AMT system, an entity may not know whether it will always be subject to the BEAT tax, and we believe that most (if not all) taxpayers will ultimately take measures to reduce their BEMTA exposure and therefore ultimately pay taxes at or as close to the regular rate as possible. Accordingly, while there is no credit under the Act such as the one that existed under the AMT regime, we believe that the similarities between the two systems are sufficient to allow BEAT taxpayers to apply the existing AMT guidance in ASC 740 and measure deferred taxes at the 21 percent statutory tax rate. (See ASC 740-10-30-8 through 30-12 and ASC 740-10-55-31 through 55-33.)

In January 2018, the FASB staff issued a [Q&A](#) stating that companies should measure deferred taxes without regard to BEAT (i.e., should continue to measure deferred taxes at the regular tax rate), with any payment of incremental BEAT reflected as a period expense.

Impact of BEAT on the Realizability Assessment of Certain DTAs

In the calculation of the BEMTA, certain credits and NOLs may not be available to reduce the BEMTA. Consequently, the actual economic benefit received from utilizing a credit loss or NOL may be less than the DTA (before reduction for any valuation allowance) for that particular tax attribute and, in some cases, may result in no cash tax savings at all because, without the attribute, the entity would have paid more regular tax and less BEMTA.

6.2 If an entity expects to be subject to BEMTA and the incremental economic benefit it expects to realize for certain tax credits and NOLs is less than the corresponding DTAs, how should the entity take this into consideration when evaluating the realizability of its DTAs? [Added March 20, 2018]

The FASB staff Q&A that addresses the broader accounting implications of BEAT states that an entity “would not need to evaluate the effect of potentially paying BEAT in future years on the realization of [DTAs].” The DTAs are measured in accordance with the regular tax system, and any utilization of NOLs or tax credits would reduce the regular tax liability even if additional BEMTA is owed.

Corporate AMT

The corporate AMT has been repealed for tax years beginning after December 31, 2017. Taxpayers with AMT credit carryforwards that have not yet been used may claim a refund in future years for those credits even though no income tax liability exists.¹³ Companies can continue using AMT credits to offset any regular income tax liability in years 2018 through 2020, with 50 percent of remaining AMT credits refunded in each of the 2018, 2019, and 2020 tax years and all remaining credits refunded in tax year 2021.

7.1 If a valuation allowance has been recorded on the DTA for AMT credit carryforwards, should the valuation allowance be released?

Yes. Since the AMT credit will now be fully refundable regardless of whether there is a future income tax liability before AMT credits, the benefit of the AMT credit will be realized. Therefore, any valuation allowance should be released, and an income tax benefit should be recognized.

7.2 Now that existing AMT credit carryovers are refundable, how should an entity present the AMT credits in the balance sheet?

Because an entity may either apply an AMT credit carryforward against its future income tax liability or receive a refund if it never has taxable income, we would accept either presentation as long as it is accompanied by appropriate disclosure.

7.3 If the amount is presented as a receivable, and given that it will be collected over a period of longer than 12 months, should the amount be discounted? [Amended January 19, 2018]

No. As discussed in [FAQ 3.2](#), ASC 740 prohibits discounting, but only in the context of DTAs and DTLs. Accordingly, in the absence of explicit guidance in ASC 740, we believe that ASC 835-30 would need to be considered, and in accordance with our conclusion above regarding the deemed repatriation transition tax, we do not believe that the amount, even if presented as a receivable, should be discounted.

In January 2018, the FASB staff issued a [Q&A](#) stating that, in a manner similar to the Board's conclusion regarding the one-time deemed repatriation transition tax, refundable AMT carryforward credits should not be discounted.

¹³ Note that taxpayers should consider whether other limitations (e.g., IRC Section 383, “Special Limitations on Certain Excess Credits, Etc.,”) apply to their ability to claim a refund of AMT.

Non-ASC 740 Topics Affected by Tax Reform

Non-GAAP Financial Measures

8.1 May companies adjust their non-GAAP financial measures related to the impact of tax reform? [Amended March 20, 2018]

Non-GAAP financial measures are commonly used, since many registrants assert that such measures are meaningful and provide valuable insight into the information that management considers important in running the business. While many non-GAAP financial measures are expressed on a pretax basis (e.g., EBITDA), others are expressed on a post-tax basis (e.g., adjusted net income, adjusted EPS). For example, registrants may seek to adjust post-tax non-GAAP measures related to the impact of tax reform.

Registrants may also elect to make non-GAAP adjustments related to discrete amounts that affect income from, for example, (1) the adjustment of deferred taxes upon the change in corporate tax rates and (2) the recognition of incremental tax expense related to foreign earnings previously considered to be indefinitely reinvested abroad and not subject to U.S. taxation (the deemed repatriation tax). If such adjustments are accompanied by the disclosures required by SEC Regulation G and Regulation S-K, Item 10(e), and are not misleading as described in Section 100 of the SEC's May 2016 [Compliance and Disclosure Interpretations](#) (C&DIs), the adjustments for tax reform may be permissible depending on the registrant's specific facts and circumstances. If a registrant includes an adjustment for the impact of tax reform in its non-GAAP measures, it should ensure that the adjustment is for the total impact of tax reform and not just for select provisions (i.e., no cherry picking). For example, if a registrant adjusts its non-GAAP measure to remove the deemed repatriation transition tax, it must also adjust its non-GAAP measure for the adjustment to deferred taxes for the change in tax rates.

Some registrants may also consider adjustments that attempt to depict a "normalized" tax rate between comparable periods to enhance comparability of periods before and after tax reform (i.e., adjustments in which the new tax rate is applied to periods before enactment). However, such non-GAAP measures may be considered misleading and may be deemed an individually tailored accounting principle since they may not reflect different tax strategies, tax assertions, or other actions that a registrant may have taken if the lower tax rate had applied to all periods presented (e.g., increased compensation, increased research and development).

For more information, see Sections 3.7.2 and 4.3 of Deloitte's [A Roadmap to Non-GAAP Financial Measures](#).

Form 8-K Filing Requirements and Considerations

8.2 Will the Act trigger any Form 8-K filing requirements or other Form 8-K considerations?

For certain taxpayers, there may be a material reduction in DTAs and a corresponding charge to net income as a result of the Act. Registrants have questioned whether this would be considered a material impairment, which would trigger the requirement to file a Form 8-K under Item 2.06.¹⁴ The SEC recently issued [C&DI Question 110.02](#), which clarifies that reduction of a DTA as a result of the rate change would not be considered an impairment. C&DI Question 110.02 also acknowledges that the Act may affect an entity's assessment of whether its DTAs will be realized and notes that if the measurement date approach prescribed by SAB 118 is applied, the entity may still disclose the impairment in its next periodic report in accordance with Item 2.06 of Form 8-K.

¹⁴ SEC Form 8-K, Item 2.06, "Material Impairments."

Note that notwithstanding the above, a registrant may decide on the basis of its specific facts and circumstances to file a Form 8-K under another item (e.g., Item 8.01¹⁵) to disclose the Act's material effects.

Article 11¹⁶ Pro Forma Financial Information

8.2A Can registrants elect to reflect the Act as a material event for historical periods in Article 11 pro forma financial information? [Added June 20, 2018]

At the March 13, 2018, CAQ SEC Regulations Committee joint [meeting](#) with the SEC staff, the SEC staff discussed the appropriateness of reflecting the impact of the Act on historical periods (i.e., pre-enactment periods) as a material event in pro forma information presented in accordance with SEC Regulation S-X, Rule 11-01(a)(8). The staff indicated at the meeting that registrants are encouraged to discuss their specific facts and circumstances regarding such pro forma financial presentation with the SEC Division of Corporation Finance, Office of the Chief Accountant. In a subsequent panel discussion at the 2018 Baruch College Financial Reporting Conference in May 2018, a member of the SEC staff indicated that such pro forma adjustments may not be appropriate because, for example, they may not reflect alternative judgments, tax strategies, or other actions that a registrant may have taken if the lower tax rate had applied to historical periods.

Compensation and Share-Based Payment Awards

Changes to IRC Section 162(m)

IRC Section 162(m) limits the tax deductibility of certain types of compensation paid to the CEO as well as a company's four other highest paid officers (referred to collectively as the "covered employees"). Specifically, only the first \$1 million in compensation, whether cash or stock-based, paid to a covered employee is deductible for tax purposes in a given year. Compensation that is performance-based has not historically been subject to this limitation.

The Act modifies IRC Section 162(m) by (1) expanding which employees are considered covered employees by including the chief financial officer, (2) providing that if an individual is a covered employee for a taxable year beginning after December 31, 2016, the individual remains a covered employee for all future years, and (3) removing the exceptions for commissions and performance-based compensation. These changes do not apply to compensation stemming from contracts entered into on or before November 2, 2017, unless such contracts were materially modified on or after that date. Compensation agreements entered into and share-based payment awards granted after this date will be subject to the revised terms of IRC Section 162(m).

8.3 Do the changes to IRC Section 162(m) affect the accounting for deferred taxes related to share-based payment awards issued to covered employees?

Yes. The DTA recorded for share-based payment awards granted after November 2, 2017, could be less than what would have been recorded under prior law. For example, since the Act eliminates the exclusion of performance-based compensation, deferred taxes may be recorded only on awards granted after November 2, 2017, to the extent that performance-based compensation will not be limited.

We generally do not expect DTAs related to share-based payment awards that arose on or before November 2, 2017, to be affected by the Act, but companies are encouraged to consult with their accounting and tax advisers if questions arise.

¹⁵ SEC Form 8-K, Item 8.01, "Other Events."

¹⁶ SEC Regulation S-X, Article 11, "Pro Forma Financial Information."

8.4 Do the changes to IRC Section 162(m) affect the accounting policy used to account for deferred taxes in cases in which it is expected that some or all compensation paid to an employee will be limited by IRC Section 162(m)?

No. We believe that there are three approaches commonly applied in practice regarding the accounting for deferred taxes in cases in which compensation is expected to be limited by IRC Section 162(m). These approaches are as follows:

- *Deductible compensation is allocated to cash compensation first* — A DTA would not be recorded for stock-based compensation if cash compensation is expected to exceed the limit.
- *Deductible compensation is allocated to earliest compensation recognized for financial statement purposes* — Because stock-based compensation is typically expensed over a multiple-year vesting period but deductible when fully vested or exercised, and cash-based compensation is generally deductible in the period it is expensed for financial statement purposes, stock-based compensation is generally considered the earliest compensation recognized for financial statement purposes, and a DTA for stock-based compensation would be recorded up to the deductible limit.
- *Limitation is allocated pro rata between stock-based compensation and cash compensation* — A partial DTA may result on the basis of the expected ratio of stock-based compensation to cash compensation.

The choice of which approach to apply is a policy election that should be applied consistently. While the Act modifies IRC Section 162(m), we believe that the above approaches remain acceptable. Accordingly, companies should continue to apply the accounting policy they have previously elected.

8.5 If an entity modifies a compensation agreement, must it comply with the Act's updated IRC Section 162(m) limitations?

It depends. The Act contains explicit wording indicating that material modifications made to a compensation agreement on or after November 2, 2017, will cause the agreement to become subject to the updated requirements of IRC Section 162(m). Judgment may be required in the determination of whether a modification is material. Further, if a modified compensation agreement is related to a share-based payment award, companies will need to consider whether the modification guidance in ASC 718-20 should be applied.

Modifications made before November 2, 2017, may also result in a tax consequence. While modifications made before November 2, 2017, will not cause compensation to be subject to the revised requirements in IRC Section 162(m), the language in IRC Section 162(m) that existed before the Act's revisions indicates that as a result of any modification to a performance-based award, the award will become subject to the legacy IRC Section 162(m) limitations on deductibility.

Companies should be mindful of these potential outcomes when deciding how future compensation agreements will be structured or modified.

Awards With Performance Conditions

8.6 For share-based payment awards with performance conditions that are based on financial statement metrics, should a probability assessment be performed on the enactment date?

Yes. Financial statement metrics may change as a result of the Act, which may affect the probability that certain performance conditions will be met. Accordingly, performance conditions that are based on financial statement metrics should be reassessed. For example, compensation cost recognized for a share-based payment award with a performance

condition tied to earnings and whose vesting was probable before the enactment date would be reversed if it is no longer probable that the award will vest as of the enactment date (see [FAQ 1.3](#)). However, in performing the probability assessment, entities should consider whether an award's existing terms require an adjustment to performance targets as a result of "one-time" or unusual events, which might be the case with tax law changes.

Implications of Individual Statutory Rate Changes

An entity may "net-share settle" its share-based payment awards to meet its statutory tax withholding obligation related to the awards. If the entity has adopted ASU 2016-09,¹⁷ ASC 718 specifies that such provision does not, by itself, result in liability classification for the rewards as long as (1) the entity has a statutory obligation to withhold taxes on the employee's behalf and (2) the amount withheld does not exceed the maximum statutory tax rates in the employee's applicable jurisdiction(s). In circumstances in which the amount withheld exceeds the *maximum* statutory tax rate, ASC 718 requires the entity to classify the awards as liabilities. If the entity has not adopted ASU 2016-09, the amount withheld cannot exceed the *minimum* statutory requirement.

Effective January 1, 2018, the Act lowers individual tax rates. On January 11, 2018, the IRS published updated withholding tables and guidance, including withholding on supplemental income, and instructed entities to use the 2018 withholding tables as soon as possible but not later than February 15, 2018. Before implementing the 2018 withholding tables, an entity is instructed to continue to use the tables and rates in effect before enactment (i.e., the 2017 withholding tables).

8.6A Does the change in individual tax rates affect the statutory tax rates used in an entity's assessment of the amount that can be withheld when share-based payment awards are net-share settled? [Added January 19, 2018]

Yes. When an entity net-share settles its share-based payment awards to meet its statutory tax withholding obligation, such withholdings should be decreased to reflect the reduction in tax rates in effect on January 1, 2018 (e.g., from 39.6 percent to 37 percent). Accordingly, entities should implement the updated 2018 withholding tables as soon as possible to reduce, and thereby align with the Act, tax rates for awards that are net-share settled on or after January 1, 2018.

Certain Hedge Accounting Strategies

8.7 Does the change in tax law affect an entity's hedging strategies?

If an entity is hedging foreign currency risk on an after-tax basis, as allowed under ASC 815-20-25-3(b)(2)(vi), any change in tax rates applicable to the hedging instrument could disrupt the balance of any related hedging relationship.

For example, assume that Entity ABC's functional currency is the U.S. dollar (USD). Entity ABC has a subsidiary whose functional currency is the euro (EUR), and ABC has a USD/EUR forward contract designated as a hedge of EUR 65 million of its net investment in the foreign subsidiary. The forward contract has a notional amount of EUR 100 million because ABC had a tax rate of 35 percent, and it had designated that it was hedging on an after-tax basis.

Now assume that ABC's tax rate changes to 21 percent as a result of a change in tax law. When the tax law becomes effective, the changes in fair value of the derivative on an after-tax basis will be based on 79 percent of the notional amount of the forward (i.e., EUR 79 million), compared with the designated hedged item, which is a EUR 65 million net investment in a foreign subsidiary. Entity ABC is now overhedged.

¹⁷ FASB Accounting Standards Update No. 2016-09, *Compensation — Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*.

An entity should consider how this affects assessments of hedge effectiveness and measurements of ineffectiveness. In addition, it should consider whether it wants to dedesignate the existing hedging relationships, rebalance any existing hedges, and designate new hedging relationships.

Leveraged Leases

8.8 What is the Act's effect on the accounting treatment for leveraged leases?

When a change in income tax rates is enacted, an entity should recalculate leveraged leases from inception and record any differences in current-period earnings. In accordance with ASC 840-30-35-41, the entity would record the effect of the tax rate change on a leveraged lease "in the first accounting period ending on or after the date on which the legislation effecting a rate change becomes law."

8.8A Is a lessor required to recalculate the effective tax rate in a leveraged lease arrangement on the basis of the revised cash flows that result from the change in corporate tax rates and use that rate to record the tax effects of leveraged lease income allocated to future periods (after tax reform)? [Added January 19, 2018]

Yes. Recalculating the effective tax rate in the leveraged lease is consistent with ASC 840-30. Because the income or loss from the arrangement will be taxed or benefited, for U.S. federal income tax purposes, at a 35 percent rate for a portion of the life of the arrangement and a 21 percent rate for the remainder, the effective tax rate in the lease will most likely not equal the lessor's statutory income tax rate. Therefore, the tax effect of pretax leveraged lease income allocated to future periods will most likely not equal pretax leveraged lease income multiplied by the lessor's statutory rate.

Fair Value and Hypothetical Liquidation at Book Value Considerations

8.9 What income tax rate should an entity use when performing fair value measurements as of December 31, 2017?

When tax rates are an input in a fair value measurement (e.g., when the income approach is used on an after-tax basis), an entity should generally use the same assumption a market participant would use about the income tax rate that will be in effect when the projected cash flows are received. That rate is typically the statutory tax rate unless there is substantial evidence that another tax rate should be used. For additional information, see 820-10-35 (Q&A 44A), *Income Tax Rate Used in Valuation Techniques*, in Deloitte's *FASB Accounting Standards Codification Manual* (available to subscribers of the [Deloitte Accounting Research Tool](#) (DART)).

8.10 Should a company that applies the hypothetical liquidation at book value (HLBV) for an equity method investment or the allocation of earnings to a noncontrolling interest consider the effects of enacted changes in tax rates before the date the enacted changes become effective?

No. Unlike a fair value measurement, the HLBV method is an approach to allocate earnings on the basis of how an investee (or subsidiary) would allocate current-period earnings to an equity method investor (or noncontrolling interest holder) **if it were to liquidate** at a particular point in time (i.e., as of a balance sheet date). Therefore, if an investee (or subsidiary) were to liquidate as of a balance sheet date before tax reform is effective (e.g., December 31, 2017, for calendar-year-end entities), the tax rates applied in the determination of the liquidation waterfall would not take into account new enacted rates that are not yet effective. Once the enacted rates become effective, a company applying the HLBV method will need to carefully consider the allocation provisions in contracts to determine the impact that those new rates have on the application of HLBV.

8.11 How should a company assess impairment of equity method investments in pass-through entities? [Added January 19, 2018]

Some equity method investments are in pass-through entities in which a significant portion of the benefits received by an investor is related to tax credits and other tax benefits (e.g., accelerated pass-through tax losses). In many cases (e.g., pass-through entities that generate solar and wind credits), the equity method investor applies HLBV in recognizing earnings. Although we believe that the impact of tax reform should not be reflected in HLBV before the effective rates affect the contractual waterfall in liquidation (see [FAQ 8.10](#)), an equity method investor must consider whether tax reform results in an other-than-temporary impairment (OTTI) under ASC 323. In accordance with [FAQ 8.9](#), the future impact of the change in tax rates could result in a change to a market participant's view of the fair value of the investment. An entity should consider all facts and circumstances in performing an analysis of OTTI; however, the expected impact of applying HLBV in future periods is not necessarily an indication of an impairment of the investment.

Investments in Qualified Affordable Housing Projects

Investors in qualified affordable housing projects (QAHPs) also invest in pass-through entities primarily for the tax credits and other tax benefits. If certain criteria are met, the investor may apply the proportional amortization method (PAM) under ASC 323-740, which results in proportional amortization of the investment balance in each period on the basis of the proportion of the total estimated tax benefit allocated to the entity in that period rather than the application of the equity method. The calculation of the proportional amortization frequently includes the total estimated other tax benefits¹⁸ expected to be received by the investor over the life of the investment. The criteria that must be met for an investor to apply PAM must be reevaluated upon the occurrence of either a change in the nature of the investment or a change in the relationship with the investee that could cause the entity to no longer meet the conditions. Given that the Act changes corporate tax rates, the tax benefits to be received by entities holding QAHP investments may be affected.

8.12 Is an investor in a QAHP that accounts for its investment by using the PAM required to reevaluate the conditions for applying PAM as a result of the change in corporate tax rate? [Added January 19, 2018]

No. Although a change in tax rates may affect whether the criteria in ASC 323-740-25-1 are met after the initial investment, we do not believe that the change in tax rate represents either a change in the nature of the investment or a change in the relationship with the investee, as those terms are contemplated in ASC 323-740-25-1C. Therefore, an entity is not required to reassess whether it is still appropriate to apply PAM solely because of the change in tax rates.

8.13 If an investor is not using the practical expedient to amortize its QAHP investment, how does the change in corporate tax rate affect amortization? [Added January 19, 2018]

When the total expected tax benefit (tax credits and other tax benefits received) changes, amortization of the investment must be revised to ensure that cumulative amortization over the life of the investment equals the initial carrying amount (less any residual value). The change in corporate tax rate will generally reduce the benefit of "other" tax benefits (i.e., tax benefits other than credits) to be allocated to a QAHP investor in the future (i.e., the pass-through losses in the future will now benefit the investor at a 21 percent, instead of a 35 percent, tax rate). If an investor has not elected to use the practical expedient, the proportion of benefits already allocated to the investor will increase in relation to the total expected

¹⁸ In accordance with ASC 323-740-35-4, "as a practical expedient, an investor is permitted to amortize the initial cost of the investment in proportion to only the tax credits . . . if the investor reasonably expects that doing so would produce a measurement that is substantially similar to the measurement that would result." If the practical expedient was applied, the change in effective tax rates may not affect the calculation of proportional amortization.

tax credits and other tax benefits. As a result, we believe that there are two acceptable approaches for adjusting amortization.

Under the first approach, the investor would record a cumulative catch-up adjustment to the carrying amount of the investment on the basis of the amount of tax credits and other tax benefits that have been allocated to the investor in relation to the revised amount of total expected tax benefits. This approach is consistent with the guidance in ASC 323-740, which requires that the initial cost of the investment be amortized in proportion to the tax credits and other benefits that have been allocated to the investor.

Under the second approach, the investor would adjust amortization prospectively. This treatment is consistent with accounting for a change in estimate that does not affect the carrying amount of an asset or liability but alters the subsequent accounting for existing or future assets or liabilities under ASC 250.

An investor should consider whether it has, in effect, made a policy election in prior periods when adjusting amortization to take into account changes in expected tax benefits due to factors other than changes in tax rates. If so, using a different approach to account for the change in tax rate would be a change in accounting principle that would need to be assessed for preferability.

8.14 Is an investor required to assess its QAHP investments for impairment as a result of the change in the corporate tax rate? [Added January 19, 2018]

If the investor concludes that the change in corporate tax rate indicates that it is more likely than not that the carrying amount of the investment will not be realized, the investor would be required to assess its QAHP investments for impairment. This may be the case, for example, if a significant portion of the investor's yield relied on "other" tax benefits whose value declined as a result of the rate change. We believe that when this assessment is performed, the carrying amount of the investment, after any cumulative catch-up is considered (see [FAQ 8.13](#)), would be compared with the undiscounted amount of the remaining expected tax credits and other tax benefits in the evaluation of whether it is more likely than not the carrying amount will not be realized.

8.15 In the measurement of an impairment of a QAHP investment, should future tax benefits be discounted? [Added January 19, 2018]

Yes. As stated in ASC 323-740-35-6, the "impairment loss shall be measured as the amount by which the carrying amount of an investment exceeds its fair value." Fair value should take into account discounting of the future tax benefits expected to be received.

8.16 If an impairment of a QAHP investment is recorded, should it be recorded in pretax income (loss) or as a component of income tax expense? [Added January 19, 2018]

ASC 323-740 does not specify where in the income statement an impairment charge related to a QAHP investment should be recorded. Under the proportional amortization method, the amortization of the cost of the investment is netted against the tax benefits received within the income tax expense line. An impairment is a recognition of the fact that the unamortized cost of acquiring the benefits exceeds the remaining expected benefits, but it does not change the nature of the initial investment as an investment in tax credits and other tax benefits. Accordingly, we believe that the impairment would be recorded as a component of income tax expense.

Goodwill Impairment

8.17 What income tax rate should an entity use in testing goodwill for impairment when the testing date is before December 22, 2017? [Added January 19, 2018]

Even though goodwill impairment tests are generally performed after the designated goodwill impairment testing date but before the financial statements are issued, an entity should test goodwill for impairment by using facts and circumstances that existed as of the testing date. Therefore, the information used for a test before December 22, 2017, should be limited to information that was available as of that date.

8.18 What impact, if any, does the enactment of the Act have on an entity's assessment of goodwill recoverability? [Added January 19, 2018]

Goodwill is tested for impairment annually and between annual tests when an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. While enactment of a new tax law is not one of the examples of events or changes in circumstances listed in ASC 350-20-35-3C, those examples are not all-inclusive. An entity should consider its specific facts and circumstances in determining whether, as a result of enactment of the Act, it might become more likely than not that the fair value of one or more of the entity's reporting units is less than the carrying amount of the reporting unit(s). For example, if a reporting unit includes a significant DTL, enactment of the Act could result in a reduction of the DTL, thereby increasing the carrying value of the reporting unit. However, the enactment of the Act could also result in an increase in the fair value of the reporting unit. An entity should exercise judgment in determining whether enactment of the Act represents a triggering event.

Foreign Currency Implications of Withholding Tax Liabilities

As discussed in [FAQs 3.5](#), [3.5A](#), and [3.6](#), as a result of the Act, some entities may change their intent to indefinitely reinvest foreign earnings and, in some instances, a liability may need to be recorded for estimated withholding taxes. While foreign withholding taxes are generally considered a liability of the investor rather than the investee (i.e., are attributable to the investor's outside basis difference), such taxes will ultimately be payable to the foreign government in local currency and, provided that the investor and investee have different functional currencies, represent foreign-currency-denominated liabilities of the investor.

8.19 How should a U.S. parent account for fluctuations in the value of a non-USD-denominated, foreign withholding tax liability related to earnings of a *first-tier* foreign subsidiary (or foreign corporate joint venture that is essentially permanent in duration) (the "first-tier foreign subsidiary") that are not reinvested indefinitely? [Added March 20, 2018]

The amount of a non-USD-denominated, foreign withholding tax liability will change as a result of fluctuations in the corresponding exchange rate between the U.S. parent (i.e., the USD) and the applicable local currency of the first-tier foreign subsidiary. Because the U.S. parent is the primary obligor, such a liability is not recorded by the first-tier foreign subsidiary and is therefore not subject to translation. Accordingly, the impact of fluctuations between the reporting currency of the U.S. parent and the functional currency of the first-tier foreign subsidiary should be recorded through continuing operations of the U.S. parent as the related liability is remeasured in each reporting period in accordance with ASC 830-20.

8.20 How should a first-tier foreign subsidiary (or foreign corporate joint venture that is essentially permanent in duration) account for fluctuations in the value of a foreign withholding tax liability related to earnings of a *second-tier* foreign subsidiary (or foreign corporate joint venture that is essentially permanent in duration) (the “second-tier foreign subsidiary”) that are not indefinitely reinvested when the first-tier foreign subsidiary has the same local and functional currency as that of the second-tier foreign subsidiary, which is not the reporting currency? [Added June 20, 2018]

Because the first-tier foreign subsidiary and the second-tier foreign subsidiary have the same functional currency, the amount of the withholding tax liability on the functional currency books of the first-tier foreign subsidiary will not change as a result of exchange rate fluctuations. Accordingly, the related liability would not be remeasured in each reporting period, and the first-tier foreign subsidiary would not record transaction gain or loss in accordance with ASC 830-20. However, because the first-tier foreign subsidiary is the primary obligor, such a liability is recorded by the first-tier foreign subsidiary and is therefore subject to translation. Accordingly, the impact of fluctuations between the reporting currency of the U.S. parent and the functional currency of the first-tier foreign subsidiary should be recorded as a cumulative translation adjustment (CTA) through OCI.

8.21 How should a reporting entity account for fluctuations in the value of a foreign withholding tax liability related to earnings of a *second-tier* foreign subsidiary (or foreign corporate joint venture that is essentially permanent in duration) that are not indefinitely reinvested when the first-tier foreign subsidiary has a functional currency that is different from (1) the functional currency of the second-tier foreign subsidiary and (2) the reporting currency? [Added June 20, 2018]

The amount of a foreign withholding tax liability denominated in the local currency of the second-tier foreign subsidiary will change as a result of fluctuations in the corresponding exchange rate between the applicable local currencies of the first-tier foreign subsidiary and the second-tier foreign subsidiary. Accordingly, the impact of fluctuations between the functional currencies of the first-tier foreign subsidiary and the second-tier foreign subsidiary should be recorded through continuing operations of the first-tier foreign subsidiary as the related liability is remeasured in each reporting period in accordance with ASC 830-20. In addition, because the first-tier foreign subsidiary is the primary obligor, such a liability is recorded by the first-tier foreign subsidiary and is therefore subject to translation. Accordingly, the impact of fluctuations between the reporting currency of the U.S. parent and the functional currency of the first-tier foreign subsidiary should be recorded as a CTA through OCI.

Separate-Company Financial Statements

9.1 In applying the separate-return approach to allocate income taxes to the separate financial statements of a member of a U.S. consolidated tax return group, how should a company account for provisions of the Act that are calculated on a consolidated tax return basis (e.g., the deemed repatriation transition tax, GILTI, BEAT)? [Added January 19, 2018]

The member should record the tax expense attributable to the various provisions of the Act as if it had not been a member of the U.S. consolidated tax return group. However, depending on the facts and circumstances, it may be appropriate to apply related-party and affiliated group rules that are relevant regardless of whether an entity makes an election to file a consolidated tax return.

For more information on the separate-return approach, see Section 4.49 of Deloitte’s [A Roadmap to Accounting for Income Taxes](#).

Disclosure Considerations

10.1 What forward-looking disclosures should registrants consider in Management's Discussion and Analysis (MD&A) about the impact of tax reform? [Added January 19, 2018]

Material amounts recorded in the current year related to tax reform would typically be discussed and analyzed as part of a registrant's MD&A. In addition, SEC Regulation S-K, Item 303,¹⁹ requires SEC registrants to disclose in their MD&A any known trends, events, or uncertainties that are reasonably likely to have a material effect on their liquidity, capital resources, or results of operations. Therefore, registrants should consider disclosing in MD&A, to the extent such disclosures are material, the impact of the changes in tax law on future periods in addition to the current period. Such disclosures may include:

- The impact of changes in the effective tax rate on future results of operations.
- The impact of other new provisions (e.g., GILTI, FDII, BEAT) on future results of operations.
- The existence and nature of uncertainties related to those aspects of the Act for which the registrant either (1) recorded provisional amounts or (2) was unable to record a provisional amount because the registrant did not have the necessary information available, prepared, or analyzed to complete its accounting for the change in tax law.
- The implications of paying the required one-time deemed repatriation transition tax on liquidity and capital resources.
- Potential changes in the determination of indefinitely reinvested foreign earnings and the impact of additional cash that may become available for domestic operations.
- The impact that changes in tax rates or other impacts of tax reform could have on contractual agreements, such as debt covenants.

Registrants that provide forward-looking earnings guidance will also need to consider the impact of tax reform on such guidance.

10.2 What incremental disclosures are required when an entity adopts a measurement period approach as permitted by SAB 118? [Added January 19, 2018]

In addition to the disclosures required by ASC 740, SAB 118 requires companies to disclose "information about the material financial reporting impacts of the Act for which the accounting under [ASC 740 as of the reporting date] is incomplete." These disclosures include:

- (a) Qualitative disclosures of the income tax effects of the Act for which the accounting is incomplete;
- (b) Disclosures of items reported as provisional amounts;
- (c) Disclosures of existing current or deferred tax amounts for which the income tax effects of the Act have not been completed;
- (d) The reason why the initial accounting is incomplete;
- (e) The additional information that is needed to be obtained, prepared, or analyzed in order to complete the accounting requirements under ASC Topic 740;
- (f) The nature and amount of any measurement period adjustments recognized during the reporting period;
- (g) The effect of measurement period adjustments on the effective tax rate; and
- (h) When the accounting for the income tax effects of the Act has been completed.

¹⁹ SEC Regulation S-K, Item 303, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

We would expect items (a) through (e), as well as item (h), to be included in a company's disclosures in the first financial statements issued that include the period in which the Act was enacted (e.g., financial statements for the year ended December 31, 2017, for calendar-year companies). Items (f) and (g) will be relevant in subsequent periods to the extent that a company records adjustments during the measurement period, and items (a) through (e) and (h) should be updated in each reporting period until the company has completed its accounting for the income tax effects of the Act.

The examples below illustrate elements that may apply to a particular entity's compliance with the incremental disclosure requirements of SAB 118. However, the examples are not all-inclusive and do not take into account any other disclosure requirements in ASC 740. See Chapter 6 of Deloitte's *A Roadmap to Accounting for Income Taxes* for additional information regarding disclosures required by ASC 740.

Examples

[Optional disclosures depending on applicability]

[Simple description of Tax Act] On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act makes broad and complex changes to the U.S. tax code, including, but not limited to, (1) reducing the U.S. federal corporate tax rate from 35 percent to 21 percent; (2) requiring companies to pay a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries; (3) generally eliminating U.S. federal income taxes on dividends from foreign subsidiaries; (4) requiring a current inclusion in U.S. federal taxable income of certain earnings of controlled foreign corporations; (5) eliminating the corporate alternative minimum tax (AMT) and changing how existing AMT credits can be realized; (6) creating the base erosion anti-abuse tax (BEAT), a new minimum tax; (7) creating a new limitation on deductible interest expense; and (8) changing rules related to uses and limitations of NOL carryforwards created in tax years beginning after December 31, 2017.

[OR]

[Simple description of Tax Act applicable to a fiscal year company] On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act makes broad and complex changes to the U.S. tax code that will affect our fiscal year ending September 30, 2018, including, but not limited to, (1) reducing the U.S. federal corporate tax rate, (2) requiring a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries that is payable over eight years, and (3) bonus depreciation that will allow for full expensing of qualified property. The Tax Act reduces the federal corporate tax rate to 21 percent in the fiscal year ending September 30, 2018. Section 15 of the Internal Revenue Code stipulates that our fiscal year ending September 30, 2018, will have a blended corporate tax rate of 24.53 percent, which is based on the applicable tax rates before and after the Tax Act and the number of days in the year.

[OR]

[Detailed description of Tax Act distinguishing elements applicable to 2017 and those applicable to 2018] On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act makes broad and complex changes to the U.S. tax code that will affect 2017, including, but not limited to, (1) requiring a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries that is payable over eight years and (2) bonus depreciation that will allow for full expensing of qualified property.

The Tax Act also establishes new tax laws that will affect 2018, including, but not limited to, (1) reduction of the U.S. federal corporate tax rate; (2) elimination of the corporate alternative minimum tax (AMT); (3) the creation of the base erosion anti-abuse tax (BEAT), a new minimum tax; (4) a general elimination of U.S. federal income taxes on dividends from foreign subsidiaries; (5) a new provision designed to tax global intangible low-taxed income (GILTI), which allows for the possibility of using foreign tax credits (FTCs) and a deduction of up to 50 percent to offset the income tax liability (subject to some limitations); (6) a new limitation on deductible interest expense; (7) the repeal of the domestic production activity deduction; (8) limitations on the deductibility of certain executive compensation; (9) limitations on the use of FTCs to reduce the U.S. income tax liability; and (10) limitations on NOLs generated after December 31, 2017, to 80 percent of taxable income.

Examples (continued)

[Description of SAB 118] The SEC staff issued SAB 118, which provides guidance on accounting for the tax effects of the Tax Act. SAB 118 provides a measurement period that should not extend beyond one year from the Tax Act enactment date for companies to complete the accounting under ASC 740. In accordance with SAB 118, a company must reflect the income tax effects of those aspects of the Act for which the accounting under ASC 740 is complete. To the extent that a company's accounting for certain income tax effects of the Tax Act is incomplete but it is able to determine a reasonable estimate, it must record a provisional estimate in the financial statements. If a company cannot determine a provisional estimate to be included in the financial statements, it should continue to apply ASC 740 on the basis of the provisions of the tax laws that were in effect immediately before the enactment of the Tax Act.

[Initial recording of impact of Tax Act] In connection with our initial analysis of the impact of the Tax Act, we have recorded a discrete net tax expense [or benefit] of \$XX in the period ending December 31, 2017. This net expense [or benefit] primarily consists of a net expense [or benefit] for the corporate rate reduction of \$XX and a net expense for the transition tax of \$XX. For various reasons that are discussed more fully below, we have not completed our accounting for the income tax effects of certain elements of the Tax Act. If we were able to make reasonable estimates of the effects of elements for which our analysis is not yet complete, we recorded provisional adjustments. If we were not yet able to make reasonable estimates of the impact of certain elements, we have not recorded any adjustments related to those elements and have continued accounting for them in accordance with ASC 740 on the basis of the tax laws in effect before the Tax Act.

[Completed elements] Our accounting for the following elements of the Tax Act is complete.

Reduction of U.S. federal corporate tax rate: The Act reduces the corporate tax rate to 21 percent, effective January 1, 2018. Consequently, we have recorded a decrease related to DTAs and DTLs of \$XX and \$XX, respectively, with a corresponding net adjustment to deferred income tax expense (or benefit) of \$XX for the year ended December 31, 2017.

[Insert additional elements for items the company may also consider complete.]

[AND/OR]

[Incomplete elements] Our accounting for the following elements of the Tax Act is incomplete. However, we were able to make reasonable estimates of certain effects and, therefore, recorded provisional adjustments as follows:

Reduction of US federal corporate tax rate: The Tax Act reduces the corporate tax rate to 21 percent, effective January 1, 2018. For certain of our DTAs and DTLs, we have recorded a provisional decrease of \$XX and \$XX, respectively, with a corresponding net adjustment to deferred income tax expense [or deferred tax benefit] of \$XX for the year ended December 31, 2017. While we are able to make a reasonable estimate of the impact of the reduction in corporate rate, it may be affected by other analyses related to the Tax Act, including, but not limited to, our calculation of deemed repatriation of deferred foreign income and the state tax effect of adjustments made to federal temporary differences.

Deemed Repatriation Transition Tax: The deemed repatriation transition tax (Transition Tax) is a tax on previously untaxed accumulated and current earnings and profits (E&P) of certain of our foreign subsidiaries. To determine the amount of the Transition Tax, we must determine, in addition to other factors, the amount of post-1986 E&P of the relevant subsidiaries, as well as the amount of non-U.S. income taxes paid on such earnings. We are able to make a reasonable estimate of the Transition Tax and recorded a provisional Transition Tax obligation of \$XX. However, we are continuing to gather additional information to more precisely compute the amount of the Transition Tax.

Valuation allowances: The company must assess whether its valuation allowance analyses are affected by various aspects of the Tax Act (e.g., deemed repatriation of deferred foreign income, GILTI inclusions, new categories of FTCs). Since, as discussed herein, the company has recorded provisional amounts related to certain portions of the Tax Act, any corresponding determination of the need for or change in a valuation allowance is also provisional.

Cost recovery: While we have not yet completed all of the computations necessary or completed an inventory of our 2017 expenditures that qualify for immediate expensing, we have recorded a provisional benefit of \$XX based on our current intent to fully expense all qualifying expenditures. This resulted in a decrease of approximately \$XX to our current income tax payable and a corresponding increase in our DTLs of approximately \$XX (after considering the effects of the reduction in income tax rates).

Examples (continued)

[AND/OR]

[Incomplete elements] Our accounting for the following elements of the Tax Act is incomplete, and we were not yet able to make reasonable estimates of the effects. Therefore, no provisional adjustments were recorded.

Global intangible low taxed income (GILTI): The Tax Act creates a new requirement that certain income (i.e., GILTI) earned by controlled foreign corporations (CFCs) must be included currently in the gross income of the CFCs' U.S. shareholder. GILTI is the excess of the shareholder's "net CFC tested income" over the net deemed tangible income return, which is currently defined as the excess of (1) 10 percent of the aggregate of the U.S. shareholder's pro rata share of the qualified business asset investment of each CFC with respect to which it is a U.S. shareholder over (2) the amount of certain interest expense taken into account in the determination of net CFC-tested income.

Because of the complexity of the new GILTI tax rules, we are continuing to evaluate this provision of the Tax Act and the application of ASC 740. Under U.S. GAAP, we are allowed to make an accounting policy choice of either (1) treating taxes due on future U.S. inclusions in taxable income related to GILTI as a current-period expense when incurred (the "period cost method") or (2) factoring such amounts into a company's measurement of its deferred taxes (the "deferred method"). We selected the deferred method. Our calculation of the deferred balance with respect to the new GILTI tax rules will depend, in part, on analyzing our global income to determine whether we expect to have future U.S. inclusions in taxable income related to GILTI and, if so, what the impact is expected to be. Because whether we expect to have future U.S. inclusions in taxable income related to GILTI depends on a number of different aspects of our estimated future results of global operations, we are not yet able to reasonably estimate the effect of this provision of the Tax Act. Therefore, we have not made any adjustments related to potential GILTI tax in our financial statements.

[OR]

Because of the complexity of the new GILTI tax rules, we are continuing to evaluate this provision of the Tax Act and the application of ASC 740. Under U.S. GAAP, we are allowed to make an accounting policy choice of either (1) treating taxes due on future U.S. inclusions in taxable income related to GILTI as a current-period expense when incurred (the "period cost method") or (2) factoring such amounts into a company's measurement of its deferred taxes (the "deferred method"). Our selection of an accounting policy with respect to the new GILTI tax rules will depend, in part, on analyzing our global income to determine whether we expect to have future U.S. inclusions in taxable income related to GILTI and, if so, what the impact is expected to be. Because whether we expect to have future U.S. inclusions in taxable income related to GILTI depends on a number of different aspects of our estimated future results of global operations, we are not yet able to reasonably estimate the effect of this provision of the Tax Act. Therefore, we have not made any adjustments related to potential GILTI tax in our financial statements and have not made a policy decision regarding whether to record deferred taxes on GILTI.²⁰

Valuation allowances: The company must assess whether valuation allowances assessments are affected by various aspects of the Tax Act (e.g., deemed repatriation of deferred foreign income, GILTI inclusions, new categories of FTCs). Since, as discussed herein, the company has recorded no amounts related to certain portions of the Tax Act, any corresponding determination of the need for or change in a valuation allowance has not been completed and no changes to valuation allowances as a result of the Tax Act have been recorded.

IFRS Considerations

11.1 May an entity that reports under IFRS® Standards apply the guidance in SAB 118? [Added January 19, 2018]

As indicated in footnote 6 of SAB 118, the SEC will allow a foreign private issuer (FPI) reporting under IFRS Standards to apply the guidance in the SAB when accounting for the effects of the Act.

²⁰ See [FAQ 4.9](#) for additional information.

However, we do not believe that non-FPIs reporting under IFRS Standards may apply the guidance in SAB 118 because SABs are not authoritative guidance under IFRS Standards. Nevertheless, we support the preliminary view of many stakeholders that “SAB 118-like” accounting may be achieved for at least those provisions of the Act for which reliable estimates can be made by applying existing IFRS guidance. For example, although an entity may need to use judgment in accounting for certain aspects of the Act, if a reliable estimate can be made, the entity should recognize such amounts and, if necessary, adjust those estimates over time as more information becomes available and provide accompanying disclosures. It is uncertain at this time, however, whether current IFRS guidance supports accounting similar to that under SAB 118, which permits entities to exclude provisional amounts “for those specific income tax effects for which a reasonable estimate cannot be determined.” In addition, entities should consider providing appropriate disclosures on the basis of their specific situation.

While the answer to this FAQ reflects our views at this time, we understand that IFRS stakeholders are continuing to meet with their regulators, auditing firms, and other oversight bodies to determine whether and, if so, how entities that report under IFRS Standards may navigate the challenges associated with applying existing IFRS guidance to the requirements in the Act. Accordingly, our views are subject to change on the basis of possible additional guidance or further developments in practice.

Interim Reporting Considerations

The tax provision for interim periods related to ordinary income (or loss) is computed by using an estimated AETR.

Certain items or events are specifically excluded from the estimated AETR and, therefore, the related tax effects are recognized discretely (i.e., tax effects are excluded from the numerator and underlying pretax book income or expense, if any, is excluded from the denominator).

Items or events excluded from the AETR calculation may include:

- Significant and unusual or infrequently occurring items (see ASC 740-270-30-8).
- Out-of-period adjustments.
- Certain loss jurisdictions (see ASC 740-270-30-36(a)).
- Certain jurisdictions for which an entity is unable to reliably estimate income (or loss) or the related tax (or benefit) (see ASC 740-270-30-36(b)).
- Certain components of pretax income that are not estimable (ASC 740-270-30-17).
- Any item reported net of tax (discontinued operations/OCI/other tax effects in equity).
- Tax effects (excess or deficiency) of exercised or vested share-based payment awards.

12.1 How should the Act be considered when an entity is estimating its AETR for an interim period after the first annual period after enactment (i.e., the quarter ending March 31, 2018, for calendar-year entities)? [Added March 20, 2018]

All provisions of the Act (e.g., BEAT, GILTI, Section 163(j)) related to ordinary income should be considered and estimated as part of an entity's estimated AETR. See Section 9.01 of Deloitte's [A Roadmap to Accounting for Income Taxes](#) for more information.

12.2 What if the entity is unable to reliably estimate the current-year impact of a provision of the Act on its AETR? [Added March 20, 2018]

An entity that is unable to reliably estimate the current-year impact of a provision of the Act should apply the guidance in ASC 740-270-25-3, under which such an impact would be reported discretely. For more information, see Section 9.06 of Deloitte's [A Roadmap to Accounting for Income Taxes](#).

12.3 For Act-related matters for which the accounting was not completed in the period of enactment, how should additional information obtained by an entity during the measurement period be accounted for under SAB 118? [Added March 20, 2018]

SAB 118 states:

During the measurement period, an entity may need to reflect adjustments to its provisional amounts upon obtaining, preparing, or analyzing additional information about facts and circumstances that existed as of the enactment date that, if known, would have affected the income tax effects initially reported as provisional amounts. Further, an entity may also need to report additional tax effects during the measurement period, based on obtaining, preparing, or analyzing additional information about facts and circumstances that existed as of the enactment date that was not initially reported as provisional amounts. . . .

Any provisional amounts or adjustments to provisional amounts included in an entity's financial statements during the measurement period should be included in income from continuing operations as an adjustment to tax expense or benefit in the reporting period the amounts are determined.

Therefore, if, after the period of enactment, an entity obtains information that allows it to finalize, update, or make an initial reasonable estimate of the tax effects of the Act, an adjustment should be recorded to income tax expense/benefit as a discrete item in that reporting period. In other words, the entity should update its accounting for the tax effects of the Act — on the basis of the best information available at the end of each reporting period — for Act-related matters that were not completed in the period of enactment in each reporting period within the measurement period.

12.4 During the measurement period allowed under SAB 118 (which is not to exceed one year), how should an entity account for interpretive or other guidance issued by a tax authority (e.g., the IRS) that clarifies how certain provisions of the Act should be applied between the balance sheet date and the date financial statements are issued or are available to be issued? [Added March 20, 2018]

Under ASC 740, an entity would not normally consider new information that is received after the balance sheet date, but that was not available as of the balance sheet date, as discussed in paragraph B38 of Interpretation 48 (not codified in ASC 740), which states, in part:

[T]he Board decided that recognition and measurement should be based on all information available at the reporting date and that a subsequent change in facts and circumstances should be recognized in the period in which the change occurs. Accordingly, a change in facts subsequent to the reporting date but prior to the issuance of the financial statements should be recognized in the period in which the change in facts occurs.

Given the unique facts and circumstances associated with the Act, however, which result in SAB 118 requiring the recognition of provisional amounts during the measurement period for items that are still open and for which a reasonable estimate can be made, we believe that it would also be acceptable to incorporate such new information into an entity's provisional amounts.

Notwithstanding the aforementioned exception to the normal rule, new information that constitutes a change in tax law would still be reflected in the period in which the new law is enacted.

12.5 What incremental disclosures does SAB 118 require entities to provide in periods after the enactment period of the Act? [Added March 20, 2018]

In addition to the disclosures required by ASC 740, SAB 118 requires entities to disclose “information about the material financial reporting impacts of the Act for which the accounting under [ASC 740 as of the reporting date] is incomplete.” See [FAQ 10.2](#) for additional discussion and a complete listing of the required disclosures.

While SAB 118 does not explicitly state whether such disclosures pertain to annual financial statements, quarterly financial statements, or both, we note that all registrants were required to provide such disclosures in the period of enactment and, provided that items remain “provisional” or “incomplete” in subsequent filings, we believe that entities will need to refresh their disclosures on a quarterly basis.

Moreover, SEC Regulation S-X, Rule 10-01(a)(5), states:

The interim financial information shall include disclosures either on the face of the financial statements or in accompanying footnotes sufficient so as to make the interim [financial] information presented not misleading. Registrants may presume that users of the interim financial information have read or have access to the audited financial statements for the preceding fiscal year and that the adequacy of additional disclosure needed for a fair presentation, except in regard to material contingencies, may be determined in that context. Accordingly, footnote disclosure which would substantially duplicate the disclosure contained in the most recent annual report to security holders or latest audited financial statements, such as a statement of significant accounting policies and practices, details of accounts which have not changed significantly in amount or composition since the end of the most recently completed fiscal year, and detailed disclosures prescribed by Rule 4-08 of this Regulation, may be omitted. **However, disclosure shall be provided where events subsequent to the end of the most recent fiscal year have occurred which have a material impact on the registrant.** Disclosures should encompass, for example, significant changes since the end of the most recently completed fiscal year in such items as: accounting principles and practices; estimates inherent in the preparation of financial statements; status of long-term contracts; capitalization including significant new borrowings or modification[s] of existing financing arrangements; and the reporting entity resulting from business combinations or dispositions. **Notwithstanding the above, where material contingencies exist, disclosure of such matters shall be provided even though a significant change since year end may not have occurred.** [Emphasis added]

Accordingly, we believe the following:

1. Items that were disclosed as complete in a prior Form 10-K (or Form 10-Q) do not need to be repeated in subsequent Form 10-Q filings; however, an item reported as complete in a prior Form 10-Q would generally be repeated in the entity's next Form 10-K filing.
2. Items that were disclosed as provisional or incomplete (Buckets 2 and 3) and, hence, are considered “open” would generally be treated as more akin to “material contingencies.” Accordingly, we believe that the relevant SAB 118 disclosures would need to be updated or refreshed (or both) as necessary in follow-on filings for these items until the accounting for such items is completed. In other words, entities should still, at a minimum, continue to denote those items for which the accounting remains provisional or incomplete in future filings, regardless of whether a significant change in the status of such items has occurred since the prior filing date.

The following examples illustrate these concepts:

Examples

Bucket 2: Items for Which the Accounting Is Provisional

For elements of the Act that were previously disclosed as being provisional (for which entities were able to make reasonable estimates and recorded provisional adjustments) but that are now determined to be complete without any further adjustment to the provisional amounts previously recorded:

[Our accounting for the following elements of the Act is complete:

Deemed Repatriation Transition Tax: The deemed repatriation transition tax (the “Transition Tax”) is a tax on certain previously untaxed accumulated and current earnings and profits (E&P) of our foreign subsidiaries. Consequently, we recorded a Transition Tax obligation of \$XX, with a corresponding adjustment to income tax expense of \$XX for the year ended December 31, 2017. No changes have been made to these adjustments, and our accounting for the transition tax is now complete.

Examples (continued)

Insert additional elements for items the company may also consider complete.

Further, see the disclosure guidelines above for disclosures required in subsequent periods.]

For elements of the Act that were previously disclosed as being provisional (for which entities were able to make reasonable estimates and recorded provisional adjustments), for which incremental measurement adjustments were recognized during the reporting period, and that are now determined to be complete:

[Our accounting for the following elements of the Act is complete.

Deemed Repatriation Transition Tax: The deemed repatriation transition tax (the “Transition Tax”) is a tax on certain previously untaxed accumulated and current earnings and profits (E&P) of our foreign subsidiaries. We were able to reasonably estimate the Transition Tax and recorded a provisional Transition Tax obligation of \$XX, with a corresponding adjustment of \$XX to income tax expense for the year ended December 31, 2017. On the basis of revised E&P computations that were completed during the reporting period, we recognized an additional measurement-period adjustment of \$XX to the Transition Tax obligation, with a corresponding adjustment of \$XX to income tax expense during the period. The effect of the measurement-period adjustment on the 2018 effective tax rate was approximately XX percent. The Transition Tax, which has now been determined to be complete, resulted in recording a total Transition Tax obligation of \$XX, with a corresponding adjustment of \$XX to income tax expense.

Insert additional elements for items the company may also consider complete.

Further, see the disclosure guidelines above for disclosures required in subsequent periods.]

For elements of the Act that were previously disclosed as being provisional (for which entities were able to make reasonable estimates and recorded provisional adjustments) and for which incremental measurement adjustments were recognized during the reporting period but the element is still determined to be provisional:

[Our accounting for the following elements of the Act is incomplete. However, we were able to reasonably estimate certain effects and, therefore, recorded provisional adjustments as follows:

Deemed Repatriation Transition Tax: The deemed repatriation transition tax (the “Transition Tax”) is a tax on certain previously untaxed accumulated and current earnings and profits (E&P) of our foreign subsidiaries. We were able to reasonably estimate the Transition Tax and recorded an initial provisional Transition Tax obligation of \$XX, with a corresponding adjustment of \$XX to income tax expense for the year ended December 31, 2017. On the basis of revised E&P computations that were calculated during the reporting period, we recognized an additional measurement-period adjustment of \$XX to the Transition Tax obligation, with a corresponding adjustment of \$XX to income tax expense during the period. The effect of the measurement-period adjustment on the 2018 effective tax rate was approximately XX percent. A total Transition Tax obligation to date of \$XX has been recorded, with a corresponding adjustment of \$XX to income tax expense. However, we are continuing to gather additional information to more precisely compute the amount of the Transition Tax, and our accounting for this item is not yet complete because [insert reasons why the accounting is not yet complete]. We expect to complete our accounting within the prescribed measurement period.

Insert additional elements for items the company may also consider provisional.

In addition, see the disclosure guidelines above for disclosures required in subsequent periods.]

For elements of the Act that were previously disclosed as being provisional (for which entities were able to make reasonable estimates and recorded provisional adjustments) and for which no incremental measurement adjustments were recognized during the reporting period and the element is still determined to be provisional:

[Our accounting for the Act is incomplete. As noted at year-end [in the prior quarter], however, we were able to reasonably estimate certain effects and, therefore, recorded provisional adjustments associated with the deemed repatriation transition tax [and *Insert any additional elements for items the company may also consider provisional.*]

Examples (continued)

We have not made any additional measurement-period adjustments related to these items during the quarter, because [insert reasons why the accounting is not yet complete]. However, we are continuing to gather additional information to complete our accounting for these items and [expect to complete our accounting within the prescribed measurement period.

In addition, see the disclosure guidelines above for disclosures required in subsequent periods.]

Bucket 3: Items for Which No Estimates Could Be Recorded

[Our accounting for the Act is incomplete. As noted at year-end [in the prior quarter], we were not yet able to reasonably estimate the effects for GILTI. Therefore, no provisional adjustments were recorded.

Because of the complexity of the new GILTI tax rules, we are continuing to evaluate this provision of the Act and the application of ASC 740. Under U.S. GAAP, we are allowed to make an accounting policy choice of either (1) treating taxes due on future U.S. inclusions in taxable income related to GILTI as a current-period expense when incurred (the “period cost method”) or (2) factoring such amounts into a company’s measurement of its deferred taxes (the “deferred method”). Our selection of an accounting policy related to the new GILTI tax rules will depend, in part, on analyzing our global income to determine whether we expect to have future U.S. inclusions in taxable income related to GILTI and, if so, what the impact is expected to be. Because whether we expect to have future U.S. inclusions in taxable income related to GILTI depends on a number of different aspects of our estimated future results of global operations, we are not yet able to reasonably estimate the long-term effects of this provision of the Act. Therefore, we have not recorded any potential deferred tax effects related to GILTI in our financial statements and have not made a policy decision regarding whether to record deferred taxes on GILTI or use the period cost method. We have, however, included an estimate of the estimated 2018 current GILTI impact in our AETR for 2018. We expect to complete our accounting within the prescribed measurement period.]

12.6 What interim disclosures should registrants consider related to the impact of the Act in complying with ASC 740-270 interim disclosure requirements? [Added March 20, 2018]

The Act makes broad and complex changes to the U.S. tax code, including, but not limited to, reducing the U.S. federal corporate tax rate from 35 percent to 21 percent. The reduction in the U.S. federal corporate rate may significantly affect the customary relationship between income tax expense and pretax accounting income. ASC 740-270-50-1 states:

Application of the requirements for accounting for income taxes in interim periods may result in a significant variation in the customary relationship between income tax expense and pretax accounting income. The reasons for significant variations in the customary relationship between income tax expense and pretax accounting income shall be disclosed in the interim period financial statements if they are not otherwise apparent from the financial statements or from the nature of the entity’s business.

The examples below illustrate an entity’s compliance with the interim disclosure requirements of ASC 740-270-50-1 in interim periods following the first annual period after the Act. However, the examples are not all-inclusive and do not take into account any other interim presentation requirements in ASC 740. See Chapter 9 of Deloitte’s [A Roadmap to Accounting for Income Taxes](#) for additional considerations related to interim presentation and disclosures.

Examples

[Our total income tax expense from continuing operations was \$XX for the three months ended March 31, 2018, compared with \$XX for the same period in 2017. The decrease in income tax expense for the three months ended March 31, 2018, compared with the same period in 2017, was primarily affected by the Act, which reduced the U.S. federal corporate income tax rate from 35 percent to 21 percent effective January 1, 2018. We also recorded an additional tax expense [benefit] of \$XX associated with a measurement-period adjustment in the period related to the Transition Tax obligation of \$XX, and recognized incremental tax expense of \$XX and \$XX for the GILTI and BEAT provisions, respectively, of the Tax Act that were effective for the first time during 2018.

OR

Our effective income tax rate was XX percent for the three months ended March 31, 2018, compared with XX percent for the same period in 2017. The decrease in the effective tax rates for the three months ended March 31, 2018, compared with the same period in 2017, was primarily affected by the Tax Act, which reduced the U.S. federal corporate income tax rate from 35 percent to 21 percent effective January 1, 2018. We also recorded an additional tax expense [benefit] of \$XX associated with a measurement-period adjustment in the period related to the Transition Tax obligation and recognized incremental tax expense of \$XX and \$XX for the GILTI and BEAT provisions, respectively, of the Tax Act that were effective for the first time during 2018.]

12.7 Should an entity exclude ordinary losses in foreign subsidiaries from the estimation of its AETR under ASC 740-270-30-36(a) if the entity concludes that it is not more likely than not that the entity will realize the tax benefits of losses in those foreign jurisdictions, but those losses will provide tax benefits for U.S. tax purposes by reducing the entity's GILTI inclusion? [Added June 20, 2018]

We believe that there are two acceptable views.

Under one view, both the loss from the foreign subsidiary and the corresponding U.S. tax benefit related to the reduction in the GILTI inclusion would be contemplated in the estimation of the AETR. ASC 740-270-30-36(b) states, in part:

The tax (or benefit) related to ordinary income (or loss) in a jurisdiction may not be limited to tax (or benefit) in that jurisdiction. It might also include tax (or benefit) in another jurisdiction that results from providing taxes on unremitted earnings, foreign tax credits, and so forth.

Accordingly, because there is a benefit in the U.S. jurisdiction, ordinary losses and the related U.S. benefit derived by reduced GILTI inclusion would be included in the overall AETR.

Under the alternative view, however, the U.S. tax benefit related to the reduction in GILTI inclusion would be included in the estimation of the AETR, but the ordinary loss from the foreign subsidiary would not. ASC 740-270-30-36(a) states:

If in a separate jurisdiction an entity anticipates an ordinary loss for the fiscal year or has an ordinary loss for the year to date for which, in accordance with [ASC] 740-270-30-30 through 30-33, no tax benefit can be recognized, the entity shall exclude ordinary income (or loss) in that jurisdiction and the related tax (or benefit) from the overall computations of the estimated annual effective tax rate and interim period tax (or benefit). A separate estimated annual effective tax rate shall be computed for that jurisdiction and applied to ordinary income (or loss) in that jurisdiction in accordance with the methodology otherwise required by [ASC 740-270].

Under this second view, because the guidance in ASC 740-270-30-36 appears to suggest application on a jurisdiction-by-jurisdiction basis, the ordinary loss from the loss jurisdiction and the related tax (or benefit) in that separate jurisdiction would be excluded. However, the U.S. tax benefit related to the reduction in GILTI inclusion would be included in the estimation of the AETR unless the U.S. jurisdiction is also a loss jurisdiction.

ASU 2018-02

On February 14, 2018, the FASB issued ASU 2018-02 to address industry concerns related to the application of ASC 740 to certain provisions of the Act. Specifically, some constituents in the banking and insurance industries had expressed concerns about the requirement in ASC 740 that the effect of a change in tax laws or rates on DTAs and DTLs be included in income from continuing operations. That guidance applies even in situations in which the tax effects were initially recognized directly in OCI at the previous rate, resulting in “stranded” amounts in AOCI related to the income tax rate differential.

13.1 To the extent that deferred tax balances that are attributable to items of pretax comprehensive income or loss other than continuing operations (e.g., discontinued operations, OCI, or items charged or credited directly to equity) are adjusted as discussed in FAQ 1.2, what impact, if any, does ASU 2018-02 have on where the adjustment for the effect of the tax rate change is recorded? [Amended and renumbered from FAQ 1.2A on June 20, 2018]

None. The adjustment for the tax effects of changes in tax laws or rates is still allocated to income from continuing operations, even after the issuance of ASU 2018-02. However, the ASU allows an entity to elect a one-time reclassification from AOCI to retained earnings of “stranded” tax effects resulting from the Act. The amount of the reclassification includes (1) the effect of the change in the U.S. federal corporate income tax rate on the gross deferred tax amounts and related valuation allowances, if any, on the date of enactment of the Act related to items remaining in AOCI and (2) other income tax effects of the Act on items remaining in AOCI that an entity elects to reclassify. The effects of the change in the U.S. federal corporate income tax rate on gross valuation allowances that were originally charged to income from continuing operations are not included.

For example, assume that before the enactment date of the Act, an entity recognized a \$1,000 loss in OCI in connection with a derivative used in cash flow hedging activities. No further changes in the fair value of the hedge occur after that date. The forecasted transactions will not occur until after the enactment date. Because there was no tax basis in the derivative, the entity also recognized a \$350 DTA and recorded a corresponding entry to OCI. On the enactment date of the Act, the entity reduced the DTA by \$140 and recognized a corresponding increase in income tax expense, equal to the temporary difference of \$1,000 multiplied by 14 percent. Upon adopting the ASU and electing to make the reclassification, the entity would then recognize a one-time reclassification to move the effect of the rate reduction from AOCI to retained earnings. The entries are summarized in the table below.

	Derivative Liability	AOCI	DTA	Net Income	Retained Earnings
Derivative loss	\$ (1,000)	\$ 1,000			
Related tax effect		(350)	\$ 350		
Reduction in statutory rate			(140)	\$ 140	\$ 140
Reclassification under ASU 2018-02		140			(140)
Final balance	<u>\$ (1,000)</u>	<u>\$ 790</u>	<u>\$ 210</u>	<u></u>	<u></u>

Note that while the first three entries would have been recorded on or before the enactment date and are not affected by the adoption of the ASU, the reclassification entry would only be recorded upon the adoption of ASU 2018-02 if the entity elects to make the reclassification. The reclassification entry would be recorded directly in the statement of changes in stockholders' equity and is not included in the statement of changes in OCI.

13.2 Is the adoption of ASU 2018-02 elective? [Added June 20, 2018]

No. All companies are required to adopt ASU 2018-02. However, upon the adoption of the ASU, certain provisions in the ASU are required and others are elective.

For example, a company can *elect* to reclassify the income tax effects of the Act on items in AOCI to retained earnings as described in [FAQ 13.1](#) above. Under ASC 220-10-45-12A, if an entity elects to reclassify the income tax effects of the Act, the amount of the reclassification includes:

- a. The effect of the change in the U.S. federal corporate income tax rate on the gross deferred tax amounts and related valuation allowances, if any, at the date of enactment of the Tax Cuts and Jobs Act related to items remaining in accumulated other comprehensive income. . . .
- b. Other income tax effects of the Tax Cuts and Jobs Act on items remaining in accumulated other comprehensive income that an entity elects to reclassify, subject to the disclosures in [ASC] 220-10-50-2(b).

Accordingly, if a company elects to make a reclassification entry, it would be required to reclassify amounts prescribed in (a) but would not be required to reclassify amounts prescribed in (b).

Regardless of whether an election is made to reclassify income tax effects of the Act, however, all companies are *required* to disclose the following upon adoption of the ASU:

- The company's accounting policy related to releasing income tax effects from AOCI (e.g., the portfolio approach or the security-by-security approach).²¹
- Whether the company has elected to reclassify, to retained earnings in the statement of stockholders' equity, the stranded tax effects in AOCI related to the Act.
- If the company has elected to reclassify to retained earnings the stranded tax effects in AOCI related to the Act, what the reclassification encompasses (whether it only includes the change in the federal corporate tax rate or whether it also includes other changes resulting from the Act that affect AOCI).

The ASU is effective for all entities for fiscal years beginning after December 15, 2018, including interim periods therein. Earlier application is permitted in financial statements that have not yet been issued or made available for issuance. Upon adoption, an entity would apply this guidance to each period in which the effect of the Act (or portion thereof) is recorded and may apply it either (1) retrospectively as of the date of enactment²² or (2) as of the beginning of the period of adoption.

13.3 What is an example of “[o]ther income tax effects of the Tax Cuts and Jobs Act” within the meaning of ASC 220-10-45-12A(b) for an entity that has elected to reclassify income tax effects of the Act from AOCI to retained earnings in accordance with ASU 2018-02? [Added June 20, 2018]

Items classified as other income tax effects of the Act might include, for example, the effect of certain international tax provisions. In some cases, an entity may not have been indefinitely reinvested in the outside basis difference in its foreign subsidiary and, accordingly, recorded a DTL related to the outside basis difference measured in a manner consistent with laws in effect before the deemed repatriation transition tax. When the DTL was initially recorded,

²¹ For more information on the portfolio approach and security-by-security approach, see Section 7.18 of Deloitte's [A Roadmap to Accounting for Income Taxes](#).

²² If a registrant elects to apply the guidance **retrospectively** after it files its annual financial statements in its Form 10-K (e.g., if the retrospective adoption is elected in the first quarter of 2018 Form 10-Q filing for a calendar-year entity) and subsequently files a new or amended registration statement that incorporates by reference the interim financial statements that reflect the impact of the adoption, the registrant must consider the need to retrospectively revise its annual financial statements that are incorporated by reference in that new or amended registration statement (i.e., the annual financial statements in its Form 10-K for the year ended December 31, 2017). This requirement does not apply to a registrant that chooses to (1) apply the new guidance as of the beginning of the period of adoption or (2) early adopt the new guidance in its annual financial statements that include the period of enactment (e.g., the annual financial statements in its 2017 Form 10-K for a calendar-year entity).

a portion may have been recorded through OCI as the tax effects related to the translation of the underlying assets and liabilities of the foreign subsidiary. Because of tax reform, the measurement of the tax effects related to the outside basis difference may have changed as a result, in whole or in part, of the deemed inclusion of previously untaxed post-1986 foreign E&P, offset by a deduction designed to generally result in an effective U.S. federal income tax rate on such E&P of either 15.5 percent or 8 percent depending on the SFC's aggregate foreign cash position. The remeasurement of the portion of the DTL that remains in AOCI would be an example of other income tax effects of the Act on items remaining in AOCI that an entity may elect to reclassify in accordance with ASC 220-10-45-12A(b).

13.4 ASC 220-10-50-1 states that an “entity shall disclose a description of the accounting policy for releasing income tax effects from accumulated other comprehensive income.” Are the disclosure requirements under ASC 220-10-50-1 applicable only to stranded taxes, or are they applied more broadly to the tax effect of other items in AOCI? [Added June 20, 2018]

The disclosure requirements in ASC 220-10-50-1 are applicable only to stranded taxes. Stranded tax commonly results from changes in valuation allowances or changes in tax laws, tax rates, or tax status. See Section 7.18 of Deloitte's *A Roadmap to Accounting for Income Taxes* for more information about the release of stranded income tax effects from AOCI.

13.5 If an entity initially adopts ASU 2018-02 by using provisional amounts in accordance with SAB 118, what impact do subsequent changes to those provisional amounts have on the entity's initial-adoption entries? [Added June 20, 2018]

Subsequent changes to provisional amounts will not affect the entity's initial-adoption entries; rather, the entity would need to record additional adjustments to the reclassification in subsequent periods. The FASB acknowledged in paragraph BC23 of ASU 2018-02 that if an entity recorded provisional estimates for an item under SAB 118, and additional information related to facts or circumstances that existed as of the date of enactment is obtained during the measurement period, adjustments to those provisional estimates could result in the recording of the reclassification adjustment contemplated by ASU 2018-02 in multiple reporting periods.

13.6 If an entity adopts ASU 2018-02 prospectively in a period *after* the period that includes the enactment date, is the amount of the reclassification adjustment based on the amount that remained at enactment, or is it based on the amount that remains at the time of adoption? [Added June 20, 2018]

The amount of the reclassification adjustment is based on the amount that remains at the time of adoption. For example, assume that before enactment, an entity holds an AFS security for which an unrealized loss of \$1,000 has been recorded in AOCI, resulting in a corresponding tax effect of \$350 that is also recorded in AOCI. Upon enactment, the entity records an entry in the amount of \$140 ($\$1,000 \times (35\% - 21\%)$) to reduce the DTA related to the unrealized loss with a corresponding debit to tax expense to reflect the difference between the pre-enactment corporate tax rate of 35 percent and the new corporate tax rate of 21 percent.

In the first quarter of 2018, after the enactment date, the entity sells the AFS security, resulting in the reversal of the remaining \$210 DTA balance and, before application of either the security-by-security approach or portfolio approach, reversal of \$210 of tax benefit recorded in OCI. During the second quarter of 2018 and after the sale of the AFS security, the entity adopts ASU 2018-02 and elects to prospectively reclassify stranded tax effects from AOCI to retained earnings.

If the entity had made an accounting policy election to use the security-by-security approach to account for deferred taxes associated with unrealized gains and losses recorded in OCI, the

amount of the reclassification under ASU 2108-02 recorded in the second quarter of 2018 would be \$0 because the entire tax effect associated with the AFS security would have been removed from AOCI when the security was sold.

Alternatively, if the entity had made an accounting policy election to use the portfolio approach to account for deferred taxes associated with unrealized gains and losses recorded in OCI, \$140 would be reclassified from AOCI to retained earnings upon adoption of ASU 2018-02. This is because under the portfolio approach, tax effects associated with an individual security in a portfolio are not removed from AOCI until the disposal of the last security in the portfolio.

13.7 How does the existence of a valuation allowance in current or prior periods affect the reclassification under ASU 2018-02 of income tax effects of the Act related to “items remaining in accumulated other comprehensive income” on the date of enactment? [Added June 20, 2018]

If a DTA for which the offsetting amount would otherwise be recorded to AOCI requires a valuation allowance at the time it is recorded, there is no net amount recorded in AOCI because the valuation allowance is also recorded as an entry to AOCI. Consequently, upon enactment there would be no stranded tax effect in AOCI related to the item that gave rise to the DTA. The following examples illustrate the impact of valuation allowances on the reclassification of stranded tax effects under ASU 2018-02:

Examples

Valuation Allowance Recorded Before Tax Effects

Assume that in year 1, before the enactment date of the Act, an entity with a full valuation allowance against its DTAs recognized a \$100 loss in OCI in connection with an AFS security held as a short-term investment. The entity records a DTA equal to \$35 (the \$100 unrealized loss on the AFS security multiplied by the corporate tax rate of 35 percent). Because the entity has a full valuation allowance against its DTAs, it does not record a net tax benefit in OCI but instead records an increase in the valuation allowance of \$35. The entries for year 1 are as follows:

	AFS Security	AOCI	DTA	Valuation Allowance	Retained Earnings	Continuing Operations
Unrealized loss on AFS security	(100)	100	35	(35)	—	—

During year 2, the entity determines that the valuation allowance is no longer needed and releases it through continuing operations by debiting the valuation allowance and crediting tax benefit (i.e., continuing operations) in the amount of \$35. The Act is enacted in year 3, and the entity remeasures its DTA related to the AFS security by using the new lower corporate tax rate of 21 percent to credit the DTA and debit tax expense (i.e., continuing operations) in the amount of \$14 (\$100 unrealized loss on the AFS security multiplied by the difference in tax rates of 14 percent (35 percent minus 21 percent)).

Examples (continued)

The entity adopts ASU 2018-02 as of January 1 of year 4. The amount remaining in AOCI related to the AFS security as of the date of enactment is \$0. This is because when the tax effects of the changes in value of the AFS security occurred, the entity had a full valuation allowance recorded. Accordingly, no amount is reclassified from AOCI to retained earnings under ASU 2018-02. The entries for years 2, 3, and 4 are as follows:

	AFS Security	AOCI	DTA	Valuation Allowance	Retained Earnings	Continuing Operations
Release of the valuation allowance				35		(35)
Enactment			(14)			14
ASU 2018-02		0			0	
Total (years 1, 2, 3, and 4)	(100)	100	21	0	0	(21)

Valuation Allowance Recorded After Tax Effects

Assume the same facts as in the previous example, except that the valuation allowance is not recorded until the beginning of year 2 and is not released before enactment.

In year 1, the entity records the \$35 DTA and corresponding tax benefit in OCI related to the \$100 unrealized loss on the AFS security. The entries for year 1 are as follows:

	AFS Security	AOCI	DTA	Valuation Allowance	Retained Earnings	Continuing Operations
Unrealized loss on AFS security	(100)	100			—	—
		(35)	35			

In year 2, the entity determines that a full valuation allowance is needed and accordingly credits the valuation allowance in the amount of \$35 with an offsetting entry to tax expense (i.e., the amount is not “backwards traced” to AOCI). In year 3, the Act is enacted, and the entity remeasures its DTA related to the AFS security by using the new lower corporate tax rate of 21 percent to credit the DTA and debit the valuation allowance in the amount of \$14. The entity adopts ASU 2018-02 as of January 1 of year 4. In doing so, it determines that upon enactment, the stranded tax effect related to the AFS security is \$14. This is because although the entity recorded a valuation allowance against the DTA related to the AFS security in year 2, the tax effect related to the AFS security that was recorded in OCI (and thus remained in AOCI as of enactment) was \$35. Consequently, a debit of \$14 is made to AOCI, and a credit of \$14 is made to retained earnings to reclassify the stranded tax effects remaining in AOCI as of enactment. The entries for years 2, 3, and 4 are as follows:

	AFS Security	AOCI	DTA	Valuation Allowance	Retained Earnings	Continuing Operations
Full valuation allowance recorded				(35)		35
Enactment			(14)	14		
ASU 2018-02		14			(14)	
Total (years 1, 2, 3, and 4)	(100)	79	21	(21)	(14)	35

13.8 Do the adoptions of ASU 2018-02 and ASU 2016-01²³ affect each other? [Added June 20, 2018]

Yes, the adoptions of ASU 2018-02 and ASU 2016-01 affect each other.

ASU 2016-01 requires entities to remeasure equity securities with readily determinable fair values (and those without readily determinable fair values upon the occurrence of certain events) to fair value each period and is effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods therein. Upon adoption, an entity is required to record a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. Consequently, entities with equity securities that were classified as AFS before adoption will reclassify amounts from AOCI to retained earnings by means of the cumulative-effect adjustment recorded upon adoption.

As noted previously, ASU 2018-02 allows entities to reclassify certain stranded tax effects related to the Act and is effective for annual periods beginning after December 15, 2018, and interim periods therein, with early adoption permitted. Upon adoption, an entity may elect to reclassify stranded tax effects from AOCI to retained earnings. This reclassification may be performed prospectively (as of the beginning of the period of adoption) or retrospectively (to each period in which the effect of the change in tax rates is recognized).

Because both ASU 2018-02 and ASU 2016-01 may affect amounts previously recorded in AOCI, the impact that the adoption of one ASU has on the adoption of the other will depend on (1) the order in which the ASUs are adopted, (2) the entity's existing policies for releasing stranded tax effects, and (3) the entity's choice of adoption with respect to ASU 2018-02.

For example, if ASU 2016-01 is adopted before ASU 2018-02 and the entity elects to adopt ASU 2018-02 prospectively, certain stranded tax effects may have already been reclassified into retained earnings because the entity's existing policy was to release stranded tax effects by using a security-by-security approach (i.e., those specific effects will not remain in AOCI when ASU 2018-02 is adopted and, accordingly, will not be affected by ASU 2018-02). However, an entity may still elect to reclassify other tax effects of the Act in accordance with ASC 220-10-45-12A(a) (e.g., effect of rate change on deferred tax amounts related to debt securities) or ASC 220-10-45-12A(b) *in addition* to those previously reclassified by means of the cumulative-effect adjustment recorded upon adoption of ASU 2016-01.

Alternatively, if ASU 2018-02 is adopted before ASU 2016-01 (or is adopted after ASU 2016-01, but the entity elects to adopt ASU 2018-02 on a retrospective basis) and the entity has elected to reclassify stranded tax effects from AOCI, the tax effects remaining in AOCI that would be reclassified upon adoption of ASU 2016-01 would generally be limited to the tax effect of the pretax gain or loss on the equity security at the new 21 percent statutory tax rate.

If the two ASUs are adopted simultaneously, companies should decide on which ASU was adopted first since that determination will affect the resulting disclosures.

²³ FASB Accounting Standards Update No. 2016-01, *Financial Instruments — Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*.

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