Income Taxes

Introduction

The accounting for income taxes under ASC 740 is sometimes very specific and can be complex. The overall objective of accounting for income taxes is to reflect (1) the amount an entity currently owes to tax authorities and (2) a deferred tax asset (DTA) or deferred tax liability (DTL) for the tax effects of the transactions or events that have occurred but that have not yet been reflected in a tax return or vice versa (also referred to as “basis differences” or “temporary differences”). A DTA will be recorded for items that will result in future tax deductions (sometimes referred to as a benefit), and DTLs are recorded for items that will result in the inclusion of future taxable income in an entity’s tax return. This balance sheet approach is used to calculate temporary differences that, in effect, take into account the total tax that would be payable (or receivable) if all of an entity’s assets and liabilities were realized at their carrying value at a specific time (the reporting date).

In accordance with ASC 740, the critical event for recognition of a DTA is the event that gives rise to the deductible temporary difference or tax credit or net operating loss (NOL) carryforward. Once that event occurs, those tax benefits should be recognized subject to a realizability assessment. In effect, earning taxable income in future years is treated as a confirmation of realizability and not as a prerequisite to asset recognition. At the same time, management should consider future events to record those DTAs at amounts that are more likely than not to be realized in future tax returns. In the case of DTLs, ASC 740 requires an entity to include in its balance sheet an obligation for the tax consequences of taxable temporary differences even when losses are expected in future years.

The following is a brief summary of deferred tax accounting, in general, under ASC 740:

- DTLs are recognized for future taxable amounts.
- DTAs are recognized for future deductions and operating loss and tax credit carryforwards.
- The marginal tax rate is used to measure DTAs and DTLs.
- A valuation allowance is recognized to reduce DTAs to the amounts that are more likely than not to be realized.
- The amount of the valuation allowance is based on all available positive and negative evidence about the future.
- Deferred tax expense or benefit is computed as the difference between the beginning and ending balance of the net DTA or DTL for the period.
- Before the adoption of ASU 2015-17, DTAs and DTLs are classified as current or noncurrent in accordance with the classification of the related asset or liability for financial reporting purposes. Upon adoption, ASU 2015-17 requires entities to present DTAs and DTLs as noncurrent in a classified balance sheet.
- The effects of changes in rates or laws are recognized on the date of enactment.
Industry Issues

The discussions and examples below contain guidance on income tax matters that frequently affect life sciences entities. The guidance cited is not intended to be all-inclusive or comprehensive; rather, it provides targeted considerations related to the application of ASC 740 that are most relevant to the industry.

For more information about the topics summarized below, see Deloitte’s A Roadmap to Accounting for Income Taxes (the “Income Taxes Roadmap”).

Scope Considerations

The scope of ASC 740 is limited to “taxes based on income” when income is determined after revenues and gains are reduced by some amount of expenses and losses allowed by the jurisdiction. Therefore, a tax based solely on revenues would not be within the scope of ASC 740 because the taxable base amount is not reduced by any expenses. A tax based on gross receipts, revenue, or capital should be accounted for under other applicable literature (e.g., ASC 450). In contrast, a tax whose base takes into account both income and expenses is within the scope of ASC 740. Common questions for life sciences entities include whether the MDET and certain R&D credits are within the scope of ASC 740.

Whether the MDET Is Within the Scope of ASC 740

The MDET is a 2.3 percent excise tax on sales of certain medical devices imposed by the Patient Protection and Affordable Care Act of 2010 and IRC Section 4191. The tax applies to sales of medical devices on or after January 1, 2018.

Question

Is the MDET within the scope of ASC 740?

Answer

No. Since the MDET in its current form is based solely on a percentage of total sales (i.e., the applicable rate is applied to total sales, which are not reduced by any expenses), it is not within the scope of ASC 740.

Whether Refundable Tax Credits for Qualifying R&D Are Within the Scope of ASC 740

To promote innovation and spending in their tax jurisdictions, governments frequently provide tax credits to entities with qualifying R&D expenditures. Sometimes these credits ultimately depend on taxable income, in which case the credits are generally recognized as a reduction of income tax regardless of whether they are accounted for under the flow-through method or the deferral method (as described in ASC 740-10-25-45 and 25-46). However, certain tax jurisdictions provide refundable credits for qualifying R&D that do not depend on an entity’s ongoing tax status or tax position (e.g., an entity may receive a refund despite being in a taxable loss position).

Question

Are refundable tax credits, as described above, within the scope of ASC 740 and accordingly classified within income tax expense (benefit) in the financial statements?
**Answer**

If realization of the tax credits does not depend on an entity's generation of future taxable income or an entity's ongoing tax status or tax position, the credits are not considered to be an element of income tax accounting under ASC 740. Thus, even if the credit claims are filed in connection with a tax return, the refunds are not considered to be part of income taxes and therefore are not within the scope of ASC 740. In such cases, an entity would not record the credits as a reduction of income tax expense; rather, the entity should determine the credits' classification on the basis of their nature.

When determining the classification of these credits, an entity may consider them to be a form of government grant or assistance. An entity may look to paragraphs 24 and 29 of IAS 20 for guidance on government grants. Under paragraph 24, an entity presents government grants related to assets “either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.” Further, paragraph 29 states, “Grants related to income are presented as part of profit or loss, either separately or under a general heading such as ‘Other Income’; alternatively, they are deducted in reporting the related expense.”

In rare circumstances, a tax law may change the way a tax credit is realized. For example, a jurisdiction may have historically required that a credit be realized on the tax return as a reduction in taxes payable but subsequently changes the law so that the credit can be realized without an entity's first incurring a tax liability (i.e., the credit amount becomes refundable but was not when it arose). In this situation, an entity would generally continue to apply ASC 740 to the credits recognized at the time of the law change. Any new refundable credits earned after the tax law change would be accounted for in accordance with the guidance in this Q&A.

**Intra-Entity Transfers of IP**

Life sciences entities often develop IP such as drug formulas, trade secrets, know-how, and other proprietary information. This IP may be developed in one jurisdiction but subsequently transferred to a subsidiary in another jurisdiction. Such transfers are often tax-motivated, and both the initial and subsequent accounting for them has historically been complex.

In October 2016, as part of its simplification initiative, the FASB issued ASU 2016-16, which removes the prohibition on recording the current and deferred tax effects of intra-entity transfers of assets other than inventory (the accounting for inventory transfers will remain unchanged). The ASU is intended to reduce the complexity of U.S. GAAP and diversity in practice related to accounting for the tax consequences of certain types of intra-entity asset transfers, including those involving IP.

Under ASC 740-10-25-3(e) before the adoption of ASU 2016-16, a reporting entity is prohibited from immediately recognizing the deferred income tax effects of intra-entity transfers of assets and requires taxes paid on intra-entity profits to be accounted for in accordance with ASC 810-10. ASC 810-10-45-8 before the adoption of ASU 2016-16 states, “If income taxes have been paid on intra-entity profits on assets remaining within the consolidated group, those taxes shall be deferred or the intra-entity profits to be eliminated in consolidation shall be appropriately reduced.” This guidance on intra-entity transfers of assets is applicable to transfers of IP.
Under ASU 2016-16, the selling (transferring) entity is required to recognize any current tax expense or benefit upon transfer of the asset. Similarly, the purchasing (receiving) entity is required to recognize a DTA or DTL, as well as the related deferred tax benefit or expense, upon receipt of the asset. An entity measures the resulting DTA or DTL by (1) computing the difference between the tax basis of the asset in the buyer’s jurisdiction and the asset’s financial reporting carrying value in the consolidated financial statements and (2) multiplying such difference by the enacted tax rate in the buyer’s jurisdiction.

The example below compares the income tax accounting for intra-entity transfers of assets other than inventory under legacy U.S. GAAP with that under ASU 2016-16.

Example

Consider the following:

<table>
<thead>
<tr>
<th>Parent</th>
<th>Sells IP with a book basis of $0</th>
</tr>
</thead>
<tbody>
<tr>
<td>Subsidiary A (Tax Rate = 30%)</td>
<td>Subsidiary B (Tax Rate = 10%)</td>
</tr>
<tr>
<td>Pays $100 million</td>
<td></td>
</tr>
</tbody>
</table>

Under legacy U.S. GAAP, Subsidiary A recognizes on its tax return a gain of $100 million on the sale of IP to Subsidiary B, which is equal to the proceeds received ($100 million) less the financial reporting carrying value of the IP (zero). However, in accordance with ASC 740-10-25-3(e), A is prohibited from recognizing the current tax expense associated with that $100 million gain. Therefore, upon the sale, A would record the following journal entry for the tax effects:

Prepaid taxes 30,000,000
Current taxes payable 30,000,000

Further, B receives a tax basis in the IP of $100 million, which is equal to the amount that it paid to A. This tax basis is greater than the carrying value of the IP in the consolidated financial statements (zero), which would generally result in a DTA. However, in accordance with ASC 740-10-25-3(e), B is prohibited from recognizing the DTA (benefit) associated with its tax-over-book basis difference. Therefore, B would not record any tax entries associated with this transaction.

Under ASU 2016-16, since the exception to recognizing current and deferred taxes on intra-entity transfers of assets other than inventory is removed, A is required to recognize the current tax expense associated with the taxable gain on the sale of the IP by recording the following journal entry:

Current tax expense 30,000,000
Current taxes payable 30,000,000

In addition, B is required to recognize the deferred tax effects associated with its purchase of the IP by recording the following journal entry:

DTA 10,000,000
Deferred tax benefit 10,000,000
**Interim Reporting Considerations**

ASU 2016-16 does not explicitly state whether the tax effects of intra-entity transfers of assets other than inventory should be recognized as discrete items or included in the estimated annual effective tax rate for interim reporting purposes. Paragraph BC13 of the ASU states, in part:

> Because of the variety of intra-entity asset transfers, the Board did not want to preclude an entity from making its own assessment about how to treat an intra-entity asset transfer for purposes of the estimate. The Board also agreed with stakeholders who indicated that if the Board had decided that all intra-entity asset transfers should be treated similarly for purposes of the estimate, it would have created an exception to the model in Topic 740. The Board’s view is that it would not be unusual for entities following the guidance to conclude that many intra-entity transfers of assets other than inventory would be treated as discrete items for purposes of the computation. However, the Board understands from stakeholders’ input that because the nature of, frequency of, and ability to estimate these transfers vary among entities, there are circumstances in which an entity could conclude that the transaction should be included in the computation of the estimated annual effective tax rate. The Board understands that an entity will need to apply judgment on the basis of the facts and circumstances to conclude whether the tax consequences of an intra-entity asset transfer other than inventory should be included in the computation of the estimated annual effective tax rate or treated as a discrete item in the interim period in which the transfer occurs.

**Connecting the Dots**

Entities should carefully consider all of the provisions and exceptions in ASC 740-270 to determine whether the tax effects of intra-entity asset transfers are appropriately treated for interim reporting.

**Effective Date and Transition**

For PBEs, ASU 2016-16 is effective for annual periods beginning after December 15, 2017, and interim periods therein. For all other entities, the ASU is effective for annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019. Early adoption is permitted.

Entities should apply the amendments in ASU 2016-16 on a modified retrospective basis, recognizing the effects in retained earnings as of the beginning of the year of adoption.

**Transfer Pricing**

Many life sciences entities are global and operate legal entities in multiple countries. This may simply be due to the size and scale of the business or may be the result of regulatory requirements. For example, life sciences entities are frequently required to have regulatory approval to manufacture or distribute product in each country in which its products are manufactured or sold. Similarly, CROs are often required to perform R&D services on different patient populations in multiple geographical locations. Because of the global nature of many life sciences entities, income tax accounting issues regarding the use of transfer pricing for intra-entity and related-party transactions arise. Generally, transfer pricing is the pricing used for transfers of tangible property, intangible property, services, or financing between affiliated entities in different tax jurisdictions. These transactions include transfers between domestic or international entities, such as (1) U.S. to foreign, (2) foreign to foreign, (3) U.S. to U.S., and (4) U.S. state to state.

The general transfer pricing principle is that the pricing of a related-party transaction should be consistent with the pricing of similar transactions between independent entities under similar circumstances (i.e., an arm’s-length transaction). Transfer pricing tax regulations are intended to prevent entities from using intra-entity charges to evade taxes by inflating or deflecting the profits of a particular jurisdiction in which the larger consolidated group does business.
An entity’s exposure to transfer pricing primarily occurs when the entity includes in its tax return the benefit received from a related-party transaction that was not conducted as though it was at arm’s length. An unrecognized tax benefit (UTB) results when one of the related parties reports either lower revenue or higher costs than it can sustain (depending on the type of transaction). While a benefit is generally more likely than not to result from such a transaction (e.g., some amount will be allowed as an interest deduction, royalty expense, or cost of goods sold), the amount of benefit is often uncertain because of the subjectivity of valuing the related-party transaction. Because of the variety and complexity of global tax regimes, transfer pricing arrangements often result in uncertain tax positions. Identifying, recognizing, and measuring uncertain tax positions may require management to make significant judgments that often have a material impact on the consolidated financial statements.

The requirements of ASC 740 in the context of transfer pricing arrangements, including related considerations, are outlined below.

**Determining the Unit of Account**

Before applying the recognition and measurement criteria, an entity must identify all material uncertain tax positions and determine the appropriate unit of account for assessment. A tax position encompasses “[a]n allocation or a shift of income between jurisdictions” (i.e., a transfer pricing arrangement). Therefore, intra-entity and related-party transactions under transfer pricing arrangements are within the scope of ASC 740.

Further, tax positions related to transfer pricing generally should be evaluated individually, since two entities and two tax jurisdictions are involved in each transaction. Such an evaluation should be performed even when the transaction is supported by a transfer pricing study prepared by one of the entities. Generally, there would be at least two units of account. For example, the price at which one entity will sell goods to another entity will ultimately be the basis the second entity will use to determine its cost of goods sold. See Section 3.30 of Deloitte’s *Income Taxes Roadmap* for more information about determining the unit of account.

**Recognition**

ASC 740-10-25-6 indicates that the threshold for recognition has been met “when it is more likely than not, based on the technical merits, that the position will be sustained upon examination.” While an entity should apply the recognition threshold and guidance in ASC 740 to tax positions in a transfer pricing arrangement, such tax positions will generally meet the recognition threshold if a transaction has taken place to generate the tax positions and some level of benefit will therefore be sustained. For example, assume that a U.S. parent entity receives a royalty for the use of intangibles by a foreign subsidiary that results in taxable income for the parent and a tax deduction for the foreign subsidiary. The initial tax filing (income in the receiving jurisdiction and expense/deduction in the paying jurisdiction) typically meets the more-likely-than-not recognition threshold on the basis of its technical merits, since a transaction between two parties has occurred. However, because there are two entities and two tax jurisdictions involved, the tax jurisdictions could question whether the income is sufficient, whether the deduction is excessive, or both. Such factors should be considered during the measurement phase as part of the determination of what the tax jurisdictions are more likely than not to accept on the basis of the technical merits.
Measurement

After an entity has assessed the recognition criteria in ASC 740 and has concluded that it is more likely than not that the tax position taken will be sustained upon examination, the entity should measure the associated tax benefit. This measurement should take into account all relevant information, including tax treaties and arrangements between tax authorities. As discussed above, each tax position should be assessed individually and a minimum of two tax positions should be assessed for recognition and measurement in each transfer pricing transaction.

For measurement purposes, ASC 740-10-30-7 requires that the tax benefit be based on the amount that is more than 50 percent likely to be realized upon settlement with a tax jurisdiction “that has full knowledge of all relevant information.” Intra-entity or transfer pricing assessments present some unique measurement-related challenges that are based on the existence of tax treaties or other arrangements (or the lack of such arrangements) between two tax jurisdictions.

Measurement of uncertain tax positions is typically based on facts and circumstances. The following are some general considerations (not all-inclusive):

- **Transfer pricing studies** — An entity will often conduct a transfer pricing study with the objective of documenting the appropriate arm's-length pricing for the transactions. The entity should consider the following when using a transfer pricing study to support the tax positions taken:
  - The qualifications and independence of third-party specialists involved (if any).
  - The type of study performed (e.g., benchmarking analysis, limited or specified method analysis, U.S. documentation report, Organisation for Economic Co-operation and Development (OECD) report).
  - The specific transactions and tax jurisdictions covered in the study.
  - The period covered by the study.
  - The reasonableness of the model(s) and the underlying assumptions used in the study (i.e., comparability of companies or transactions used, risks borne, any adjustments made to input data).
  - Any changes in the current environment, including new tax laws in effect.

- **Historical experience** — An entity should consider previous settlement outcomes of similar tax positions in the same tax jurisdictions. Information about similar tax positions, in the same tax jurisdictions, that the entity has settled in previous years serves as a good indicator of the expected settlement of current positions.

- **Applicability of tax treaties or other arrangements** — An entity should consider whether a tax treaty applies to a particular tax position and, if so, how the treaty would affect the negotiation and settlement with the tax authorities involved.

- **Symmetry of positions** — Even though each tax position should be evaluated individually for appropriate measurement, if there is a high likelihood of settlement through “competent authority” procedures under the tax treaty or other agreement, an entity should generally use the same assumptions about such a settlement to measure both positions (i.e., the measurement assumptions are similar, but the positions are not offset). Under the terms of certain tax treaties entered into by the United States and other foreign jurisdictions, competent authority is a mutual-agreement procedure between countries that is designed to relieve companies of double taxation created by transfer pricing adjustments to previously filed returns.
An entity should carefully consider whether the tax jurisdictions involved strictly follow the arm's-length principle. For example, Brazil has a mandated statutory margin that may or may not equate to what is considered arm's length by another reciprocal taxing jurisdiction. Other jurisdictions that may not strictly follow the arm's-length principle include China and India. In such situations, it may be inappropriate for an entity to assume symmetry of positions when measuring the positions.

**Presentation**

UTBs that result from transfer pricing arrangements may give rise to balance sheet presentation issues. For example, an entity with a transfer pricing arrangement may not be able to fully recognize a tax benefit in one jurisdiction but may recognize a tax benefit in the related party's jurisdiction on the basis of the assertion that the entity has competent-authority procedures available and will request that those procedures be applied if one of the tax authorities were to propose an adjustment. As noted above, competent authority is a mutual-agreement procedure between countries that is designed to relieve companies of double taxation created by transfer pricing adjustments to previously filed tax returns. Typically, double-tax cases are resolved under the principles of the transfer pricing guidelines established by the OECD. If an entity elects to take a tax issue to a competent authority for resolution, the manner in which the double-taxation issue is resolved is at the discretion of the respective jurisdictions' competent authorities. To avoid double taxation, one tax authority makes an adjustment (i.e., reduces a cost and increases taxable income) that would require a consistent transfer pricing adjustment (i.e., reducing revenue and decreasing taxable income) in the related party's tax jurisdiction. However, there is no guarantee that an agreement between the jurisdictions will be reached and that double taxation will be avoided.

Sometimes, if two governments follow the OECD's transfer pricing guidelines to resolve substantive issues related to transfer pricing transactions between units of the same entity, an asset could be recognized in one jurisdiction because of the application of competent-authority procedures, and a liability could be recognized for UTBs from another tax jurisdiction that arose because transactions between the entity's affiliates were not considered to be at arm's length.

In such cases, an entity should present the liability for UTBs and the tax benefit on a gross basis in its balance sheet. In addition, a public entity would only include the gross liability for UTBs in the tabular reconciliation disclosure. However, in the disclosure required by ASC 740-10-50-15A(b), the public entity would include the liability for UTBs and the tax benefit on a net basis in the amount of UTBs that, if recognized, would affect the effective tax rate.

For a more detailed discussion of income tax accounting issues related to transfer pricing, see Chapters 4 and 5 of Deloitte's Income Taxes Roadmap.

**Research and Development**

For many life sciences entities, R&D activities represent a significant focus and expenditure. Beyond the above-mentioned scope considerations related to refundable R&D tax credits, these activities may result in various income tax accounting impacts that should be accounted for in accordance with ASC 740. For example, R&D cost-sharing agreements may affect an entity's accounting for the income tax effects of share-based payments. In addition, an entity may acquire R&D assets in a business combination that result in the creation of temporary differences. These issues are summarized below.
R&D Cost-Sharing Arrangements

A reporting entity may enter into an arrangement with a related entity (typically a foreign subsidiary) to share the cost of developing certain intangible assets. Under such an arrangement, which is often referred to as a cost-sharing arrangement, one company bears expenses on behalf of another company and is subsequently reimbursed for those costs. The shared costs may include the cost of share-based payments issued to employees of the reporting entity. Regarding the tax impact of the sharing of share-based payment costs, the discussion document for the FASB Statement 123(R) Resource Group's July 23, 2005, meeting states, in part:

U.S. tax regulations specify the expenses that must be included in a pool of shared costs; such expenses include costs related to stock-based compensation awards granted in tax years beginning after August 26, 2003.

The tax regulations provide two methods for determining the amount and timing of share-based compensation that is to be included in the pool of shared costs: the “exercise method” and the “grant method.” Under the exercise method, the timing and amount of the allocated expense is based on the intrinsic value that the award has on the exercise date. Companies that elect to follow the grant method use grant-date fair values that are determined based on the amount of U.S. GAAP compensation costs that are to be included in a pool of shared costs. Companies must include such costs in U.S. taxable income regardless of whether the options are ultimately exercised by the holder and result in an actual U.S. tax deduction.

Cost-sharing agreements affect the U.S. company’s accounting for the income tax effects of share-based compensation. Companies should consider the impact of cost-sharing arrangements when measuring, on the basis of the tax election they have made or plan to make, the initial DTA and the amount of any future excess tax amount.

The following example, which is reproduced from the discussion document for the FASB Statement 123(R) Resource Group's July 23, 2005, meeting, illustrates the accounting for the tax effects of cost-sharing arrangements that involve share-based payments:

Company A, which is located in the United States, enters into a cost-sharing arrangement with its subsidiary, Company B, which is located in Switzerland. Under the arrangement, the two companies share costs associated with the research and development of certain technology. Company B reimburses Company A for 30 percent of the research-and-development costs incurred by Company A. The U.S. tax rate is 40 percent. Cumulative book compensation for a fully vested option is $100 for the year ending on December 31, 2006. The award is exercised during 2007, when the intrinsic value of the option is $150.

The tax accounting-impact is as follows:

**Exercise method:** On December 31, 2006, Company A records $28 as the deferred tax asset related to the option ($100 [book compensation expense] × 70% [percentage not subject to reimbursement] × 40% [tax rate]). When, in 2007, the option is exercised, any net tax benefit that exceeds the deferred tax asset is an excess tax benefit and credited to [additional paid-in capital (APIC)]. The company is entitled to a U.S. deduction [while the discussion document describes this as the deduction, the calculation is actually the tax benefit] (net of the inclusion) of $42 ($150 [intrinsic value when the option is exercised] × 70% [percentage not reimbursed] × 40%). Accordingly, $14 ($42 – $28) would be recorded in APIC.

**Grant method:** The cost-sharing impact is an increase of currently payable U.S. taxes each period; however, in contrast to the exercise method, the cost-sharing method should have no direct impact on the carrying amount of the U.S. deferred tax asset related to share-based compensation. If there was $100 of stock-based compensation during 2006, the impact on the December 31, 2006, current tax provision would be $12 ($100 [book compensation expense] × 30% [percentage reimbursed] × 40%). If the stock-based charge under [ASC 718] is considered a deductible temporary difference, a deferred tax asset also should be recorded in 2006 for the financial statement expense, in the amount of $40 ($100 [book compensation expense] × 40%). The net impact on the 2006 income statement is a tax benefit of $28 ($40 – $12). At settlement, the excess tax deduction of $20 ($50 × 40%) would be recorded in APIC.

After the adoption of ASU 2016-09, any excess tax benefits under each method described above ($14 under the exercise method example and $20 under the grant method example) would be recorded as a credit to tax expense rather than to APIC.
**R&D Assets Acquired in a Business Combination**

Acquired R&D assets will be separately recognized and measured at their acquisition-date fair values. ASC 350-30-35-17A states that an R&D asset acquired in a business combination must be considered to be an indefinite-lived intangible asset until completion or abandonment of the associated R&D efforts. Once the R&D efforts are complete or abandoned, an entity should apply the guidance in ASC 350 to determine the useful life of the R&D assets and should amortize these assets accordingly in the financial statements. If the project is abandoned, the asset would be written off if it has no alternative use.

In accordance with ASC 740, deferred taxes should be recorded for temporary differences related to acquired R&D assets as of the business combination’s acquisition date. As with all acquired assets and assumed liabilities, an entity must compare the amount recorded for an R&D intangible asset with its tax basis to determine whether a temporary difference exists. If the tax basis of the R&D intangible asset is zero, as it will be in a typical nontaxable business combination, a DTL will be recorded for that basis difference.

**Valuation Allowances and Tax-Planning Strategies**

A life sciences entity that has recurring losses or other negative evidence must consider all available evidence, both positive and negative, to determine whether a valuation allowance against its DTAs is needed. In assessing positive and negative evidence, an entity must consider the following four possible sources of taxable income discussed in ASC 740-10-30-18:

1. “Future reversals of existing taxable temporary differences.”
2. “Future taxable income exclusive of reversing temporary differences and carryforwards.”
3. “Taxable income in prior carryback year(s) if carryback is permitted under the tax law.”
4. “Tax-planning strategies” (e.g., switching from deducting R&D costs to capitalizing and amortizing the costs for tax purposes).

This analysis can be quite complex depending on the entity's facts and circumstances. Significant judgment is often required, particularly in the evaluation of items (2) and (4) above. It is difficult to assert that the entity will have future taxable income exclusive of reversing taxable temporary differences when it has cumulative losses in recent years. Further, tax-planning strategies must meet certain criteria to be treated as a source of taxable income, and evaluation of those criteria is often not straightforward.

For a detailed discussion of income tax accounting issues related to valuation allowances, see Chapter 4 of Deloitte's *Income Taxes Roadmap*. For a discussion of tax-planning strategies in particular, see Sections 4.29 through 4.34 of that Roadmap.

**Prescription Drug Fees**

The Patient Protection and Affordable Care Act, as amended by the Health Care and Education Affordability Reconciliation Act, imposed an annual fee, payable to the U.S. Treasury, on the pharmaceutical manufacturing industry for each calendar year beginning on or after January 1, 2011. The amount of the fee to be paid by a given entity is based on the entity's branded prescription drug (BPD) sales for the preceding year as a percentage of the industry's BPD sales for the same period. Under current U.S. tax law, the fee is not tax deductible and will therefore result in a permanent

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1 Although this tax-planning strategy has been used by life sciences entities in the past, such entities should keep in mind that the Tax Cuts and Jobs Act (described below) includes important changes to the deductibility of research costs. Specifically, that legislation requires companies to spread the cost of research over 5 years rather than allowing them to deduct it all immediately. Moreover, costs related to research conducted offshore will be amortized over 15 years. This particular rule does not become effective until 2021, unlike many other provisions that became effective on January 1, 2018.
difference between an entity’s income for financial reporting purposes and its taxable income. This permanent difference will result in an increase in the entity’s overall effective tax rate.

**Tax Reform**

On December 22, 2017, President Trump signed into law the tax legislation commonly known as the Tax Cuts and Jobs Act (the “Act”). Under ASC 740, 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.

Shortly after enactment, however, the SEC staff issued SAB 118, 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, as might be the case for the effect of rate changes on DTAs and DTLs. For matters that have not been completed, the entity would recognize provisional amounts to the extent that they are reasonably estimable, adjust them over time as more information becomes available, and disclose this information in its financial statements.

While only SEC registrants are subject to SAB 118, the FASB in January 2018 issued a Staff Q&A stating that the FASB staff would not object if private companies and NFPs apply SAB 118.

The following provisions of the Act are most likely to be relevant to life sciences entities:

- **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.

- **Modification of NOL carryforwards** — The Act modifies aspects of current law regarding NOL carryforwards. Under current law, NOLs generally have a carryback period of 2 years and a carryforward period of 20 years. 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.

- **Deemed repatriation transition tax (IRC Section 965)** — A U.S. shareholder of a specified foreign corporation (SFC) 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.

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2 SFCs include 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.
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 liability interest free over a period of up to eight years.

- **Global intangible low-taxed income (GILTI)** — 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 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 (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 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 deduction is permitted to a domestic corporation in an amount equal 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 as a result of the inclusion of the GILTI amount in income (“IRC Section 787 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) 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 (and will be less if the corporation is also entitled to an FDII deduction).

- **Deduction for FDII** — The Act allows a domestic corporation a deduction for a portion of its 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.

- **Base erosion anti-abuse tax (BEAT)** — 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).

- **Corporate alternative minimum tax (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. 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.

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.
• **Modified or repealed deductions** — Various provisions of previous tax law related to deductions have been modified or repealed, including the following:
  
  - **Capital expensing** — Previous law included provisions for the deduction of qualifying property purchases and the depreciation of capital assets. The Act permits 100 percent immediate expensing for qualified property through 2022, which is phased down each subsequent year through 2026 (80 percent in 2023, 60 percent in 2024, 40 percent in 2025, 20 percent in 2026).
  
  - **Business interest payments** — Previous law generally permitted deductions for business interest payments, with some limits in IRC Section 163(j). The Act limits deductions to business interest income plus 30 percent of adjusted taxable income.
  
  - **Manufacturing deduction** — Previous law under IRC Section 199 provided for a 9 percent deduction equal to the lesser of qualified production activity income or taxable income. The Act repeals this deduction.
  
  - **Orphan drug credit** — The Act halves the credit for research on rare diseases, known as the orphan drug credit.
  
  - **Research and experimentation (R&E) expenses** — Previous law permitted immediate expensing of R&E costs. The Act requires R&E costs to be amortized over 5 years for R&E activities performed in the United States (or 15 years for R&E activities performed outside the United States).

For responses to frequently asked questions about how an entity should account for the tax effects of the Act in accordance with ASC 740, see Deloitte’s January 3, 2018, *Financial Reporting Alert* (last updated on January 19, 2018). For discussion of other matters related to the income tax accounting consequences of the Act’s provisions, see Deloitte’s January 12, 2018; January 30, 2018; and February 12, 2018 (last updated on February 16, 2018), *Financial Reporting Alert* newsletters.

**SEC Comment Letter Themes Related to Income Taxes**

The SEC staff’s comments about income taxes continue to focus on (1) the potential tax and liquidity ramifications related to the repatriation of foreign earnings, (2) valuation allowances, (3) disclosures related to the income tax rate, (4) tax effects of significant or unusual transactions that occurred during the period, and (5) noncompliance with disclosure requirements (e.g., omission of required disclosures).

Further, the SEC staff continues to ask registrants to provide early-warning disclosures to help financial statement users understand these items and how they potentially affect the financial statements. The SEC staff also continues to issue comments on non-GAAP measures with a particular focus on the income tax impact of the adjustments made to the GAAP measures. For additional information about non-GAAP measures, see the *Non-GAAP Measures* section.

At the 2014, 2015, and 2016 AICPA Conferences on Current SEC and PCAOB Developments, the staff stated that boilerplate language should be avoided with respect to income tax disclosures within MD&A and that approaches more conducive to effective disclosure would include:

- Using the income tax rate reconciliation as a starting point and describing the details of the material items.
- Discussing significant foreign jurisdictions, including statutory rates, effective rates, and the current and future impact of reconciling items.
- Providing meaningful disclosures about known trends and uncertainties, including expectations regarding the countries where registrants operate.
New Accounting Standards

Reclassification of Certain Tax Effects From Accumulated Other Comprehensive Income

Background

Stakeholders raised a narrow-scope financial reporting issue that arose as a consequence of the Tax Cuts and Jobs Act (the “Act”). Some constituents 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 in the reporting period that contains the enactment date of the change. 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 accumulated other comprehensive income (AOCI) related to the income tax rate differential.

In February 2018, the FASB issued ASU 2018-02 to address concerns related to the application of ASC 740. The amendments in the ASU allow a reclassification from AOCI to retained earnings for stranded tax effects resulting from the Act. The ASU affects any entity that (1) is required to apply the guidance in ASC 220 and (2) has items of OCI for which the related tax effects are presented in OCI as required under U.S. GAAP.

Key Provisions of ASU 2018-02

Upon adopting ASU 2018-02, an entity is required to disclose:

- Its accounting policy related to releasing income tax effects from AOCI (e.g., the portfolio approach or the security-by-security approach⁴).
- Whether it has elected to reclassify, to retained earnings in the statement of stockholders’ equity, the stranded tax effects in AOCI related to the Act.
- If it 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). Other effects might include, for example, the income tax effects of accounting for foreign subsidiaries when a DTL had previously been recorded for an excess of the amount for financial reporting over the tax basis in the investments.

Effective Date and Transition

The guidance in the ASU is effective for fiscal years beginning after December 15, 2018, including interim periods therein, and early adoption is permitted. An entity will 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 enactment or (2) as of the beginning of the period of adoption. The Board decided to permit early adoption for PBEs for which financial statements have not yet been issued and for all other entities for which financial statements have not yet been made available for issuance.

For additional information about ASU 2018-02, see Deloitte’s February 12, 2018, Financial Reporting Alert (last updated on February 16, 2018).

⁴ For more information about the portfolio approach and the security-by-security approach, see Section 7.18 of Deloitte’s Income Taxes Roadmap.
Balance Sheet Classification of Deferred Taxes

Background

In November 2015, the FASB issued ASU 2015-17, which requires entities to present DTAs and DTLs as noncurrent in a classified balance sheet. The ASU simplifies the legacy guidance, which requires entities to separately present DTAs and DTLs as current and noncurrent in a classified balance sheet.

For additional information about ASU 2015-17, see Deloitte's November 30, 2015, Heads Up.

Key Provisions of ASU 2015-17

Under legacy guidance (ASC 740-10-45-4), entities are required to “separate deferred tax liabilities and assets into a current amount and a noncurrent amount. Deferred tax liabilities and assets shall be classified as current or noncurrent based on the classification of the related asset or liability for financial reporting.” Stakeholder feedback indicated that the separate presentation of deferred taxes as current or noncurrent provided little useful information to financial statement users and resulted in additional costs to preparers. Therefore, the FASB issued ASU 2015-17 to simplify the presentation of deferred taxes in a classified balance sheet. Netting of DTAs and DTLs by tax jurisdiction will still be required under the new guidance.

Noncurrent balance sheet presentation of all deferred taxes eliminates the requirement to allocate a valuation allowance on a pro rata basis between gross current and noncurrent DTAs, which constituents also identified as an issue contributing to complexity in accounting for income taxes.

Effective Date and Transition

The effective dates of ASU 2015-17 are as follows:

- For PBEs, the ASU became effective for annual periods beginning after December 15, 2016, and interim periods therein.
- For entities other than PBEs, the ASU is effective for annual reporting periods beginning after December 15, 2017, and interim reporting periods within annual reporting periods beginning after December 15, 2018.

The Board decided to allow all entities to early adopt ASU 2015-17. Therefore, the ASU can be adopted by all entities for any interim or annual financial statements that have not been issued. In addition, entities are permitted to apply the amendments either prospectively or retrospectively.

In the period in which ASU 2015-17 is adopted, an entity will need to disclose “the nature of and reason for the change in accounting principle.” If the new guidance is applied prospectively, the entity should disclose that prior balance sheets were not retrospectively adjusted. However, if the new presentation is applied retrospectively, the entity will need to disclose the quantitative effects of the change on the prior balance sheets presented.
On the Horizon

Background
In July 2016, the FASB issued a proposed ASU on the disclosure framework for income taxes that would modify or eliminate certain disclosure requirements related to income taxes as well as establish new requirements. The proposal is part of the FASB's disclosure framework project, which, as noted on the Board's related Project Update Web page, is intended to “improve the effectiveness of disclosures in the notes to financial statements by clearly communicating the information that is most important to users of each entity's financial statements.”

For additional information about the proposed ASU, see Deloitte's July 29, 2016, Heads Up.

Key Provisions of the Proposed ASU

Scope
Although many of the proposed amendments would apply to all entities that are subject to income taxes, some of them would apply only to PBEs.

Indefinitely Reinvested Foreign Earnings
The proposed ASU would require all entities to explain any change to an indefinite reinvestment assertion made during the year, including the circumstances that caused such change in assertion. All entities would also be required to disclose the amount of earnings for which there was a change in assertion made during the year. In addition, all entities would be required to disclose the aggregate of cash, cash equivalents, and marketable securities held by their foreign subsidiaries.

Such information is intended to give financial statement users information that will help them predict the likelihood of future repatriations and the associated income tax consequences related to foreign indefinitely reinvested earnings.

Unrecognized Tax Benefits
The proposed ASU would modify the disclosure requirements for a PBE related to UTBs. It would add a requirement for entities to disclose, in the tabular reconciliation of the total amount of UTBs required by ASC 740-10-50-15A(a), settlements disaggregated by those that have been (or will be) settled in cash and those that have been (or will be) settled by using existing DTAs (e.g., settlement by using existing NOL or tax credit carryforwards).

A PBE would also be required to provide a breakdown (i.e., a mapping) of the amount of total UTBs shown in the tabular reconciliation by the respective balance-sheet lines on which such UTBs are recorded. If a UTB is not included in a balance-sheet line, such amount would be disclosed separately. In addition, a PBE would be required to disclose the total amount of UTBs that are offset against existing DTAs for NOL and tax credit carryforwards.

Under the guidance currently in ASC 740-10-50-15(d), all entities must disclose details of tax positions for which it is reasonably possible that the total amount of UTBs will significantly increase or decrease in the next 12 months. The proposed ASU would eliminate this disclosure requirement.

ASC 740-10-55-217 (as amended) would provide an example of the applicability of these disclosure requirements.
Operating Loss and Tax Credit Carryforwards

Currently, entities are required to disclose the amount and expiration dates of operating losses and tax credit carryforwards for tax purposes. Historically, there has been diversity in practice related to this disclosure requirement. The proposed ASU would reduce this diversity by requiring a PBE to disclose the total amount of:

- Federal, state, and foreign gross NOL and tax credit carryforwards (i.e., not tax effected) by period of expiration for each of the first five years after the reporting date and a total for any remaining years.
- Federal, state, and foreign DTAs related to NOL and tax credit carryforwards (i.e., tax effected) before any valuation allowance.

As discussed previously, a PBE would also be required to disclose the total amount of UTBs that are offset against existing DTAs for NOL and tax credit carryforwards.

In addition, the proposed ASU would modify the disclosure requirement related to NOL and tax credit carryforwards for entities other than PBEs. An entity other than a PBE would be required to disclose the total gross amounts of federal, state, and foreign NOL and tax credit carryforwards (i.e., not tax effected) along with their expiration dates.

ASC 740-10-55-218 through 55-222 (as amended) would provide an example of the applicability of these disclosure requirements.

Rate Reconciliation

ASC 740-10-50-12 currently requires a PBE to disclose a reconciliation of the reported amount of income tax expense (or benefit) from continuing operations to the amount of income tax expense (or benefit) that would result from multiplying the pretax income (or loss) from continuing operations by the domestic federal statutory tax rate.

The proposed ASU would amend the requirement for a PBE to disclose the income tax rate reconciliation in a manner consistent with SEC Regulation S-X, Rule 4-08(h). As amended, ASC 740-10-50-12 would continue to require a PBE to disclose a reconciliation of the reported amount of income tax expense (or benefit) from continuing operations to the amount of income tax expense (or benefit) that would result from multiplying the pretax income (or loss) from continuing operations by the domestic federal statutory tax rate. However, the amendment would modify the requirement to disaggregate and separately present components in the rate reconciliation that are greater than or equal to 5 percent of the tax at the statutory rate in a manner consistent with the requirement of Rule 4-08(h).

Government Assistance

As a result of deliberations on its November 2015 proposed ASU on government assistance, the FASB decided to require an entity to disclose certain information related to assistance received from a governmental unit that reduces the entity’s income taxes. Accordingly, the July 2016 proposed ASU on income tax disclosure requirements would require all entities that receive income tax–related government assistance to disclose a “description of a legally enforceable agreement with a government, including the duration of the agreement and the commitments made with the government under that agreement and the amount of benefit that reduces, or may reduce, its income tax burden.” This disclosure requirement would apply only when the government determined whether, under such agreement, the entity would receive assistance and, if so, how much it would receive even if it met the applicable eligibility requirements.
In the absence of a specific agreement between the entity and the government, the entity would not be required to disclose this information if the entity obtained the government assistance because it met eligibility requirements that apply to all taxpayers.

**Other Income Tax Disclosure Requirements**

The proposed ASU would require all entities to disclose the following:

- The amount of pretax income (or loss) from continuing operations disaggregated by foreign and domestic amounts.
- The amount of income tax expense (or benefit) from continuing operations disaggregated by foreign and domestic amounts.
- The amount of income taxes paid disaggregated by foreign and domestic amounts. A further disaggregation would be required for any country that is significant to the total amount of income taxes paid.
- An enacted tax law change if it is probable that such change would have an effect on the entity in the future.

In addition, the proposed ASU would require PBEs to explain any valuation allowance recognized or released during the year along with the corresponding amount.

**Connecting the Dots**

The proposed ASU on income tax disclosure requirements is also aligned with the FASB's proposed ASU on assessing the materiality of disclosures, which would allow an entity to consider materiality when assessing income tax disclosure requirements. For additional information about the proposed ASU on assessing the materiality of disclosures, see Deloitte's September 28, 2015, *Heads Up.*

**Effective Date and Transition**

The proposed ASU would be applied prospectively. The FASB will determine an effective date for the final guidance after it has considered feedback from stakeholders.
Appendix A — Glossary of Standards and Other Literature

The standards and other literature below were cited or linked to in this publication.

**AICPA Literature**

Accounting and Valuation Guide *Assets Acquired to Be Used in Research and Development Activities*

AICPA Issues Paper, *Identification and Discussion of Certain Financial Accounting and Reporting Issues Concerning LIFO Inventories*

AICPA Technical Questions and Answers, Q&A paragraph 2260.03, “Other Assets; Legal Expenses Incurred to Defend Patent Infringement Suit”

**FASB Accounting Standards Updates (ASUs)**


ASU 2018-01, *Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842*

ASU 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*

ASU 2017-11, *Earnings per Share (Topic 260); Distinguishing Liabilities From Equity (Topic 480); Derivatives and Hedging (Topic 815): (Part I) Accounting for Certain Financial Instruments With Down Round Features, (Part II) Replacement of the Indefinite Deferral for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests With a Scope Exception*

ASU 2017-09, *Compensation — Stock Compensation (Topic 718): Scope of Modification Accounting*

ASU 2017-07, *Compensation — Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*

ASU 2017-05, *Other Income — Gains and Losses From the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets*

ASU 2017-04, *Intangibles — Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*

ASU 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business*
ASU 2016-20, *Technical Corrections and Improvements to Topic 606, Revenue From Contracts With Customers*


ASU 2016-17, *Consolidation (Topic 810): Interests Held Through Related Parties That Are Under Common Control*

ASU 2016-16, *Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory*


ASU 2016-13, *Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*

ASU 2016-12, *Revenue From Contracts With Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*

ASU 2016-11, *Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting*

ASU 2016-10, *Revenue From Contracts With Customers (Topic 606): Identifying Performance Obligations and Licensing*

ASU 2016-09, *Compensation — Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*

ASU 2016-08, *Revenue From Contracts With Customers (Topic 606): Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net)*

ASU 2016-02, *Leases (Topic 842)*


ASU 2015-14, *Revenue From Contracts With Customers (Topic 606): Deferral of the Effective Date*

ASU 2015-02, *Consolidation (Topic 810): Amendments to the Consolidation Analysis*


ASU 2014-16, *Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity — a consensus of the FASB Emerging Issues Task Force*

ASU 2014-10, **Development Stage Entities (Topic 915): Elimination of Certain Financial Reporting Requirements, Including an Amendment to Variable Interest Entities Guidance in Topic 810, Consolidation**

ASU 2014-09, **Revenue From Contracts With Customers (Topic 606)**

ASU 2014-02, **Intangibles — Goodwill and Other (Topic 350): Accounting for Goodwill — a consensus of the Private Company Council**

ASU 2011-06, **Other Expenses (Topic 720): Fees Paid to the Federal Government by Health Insurers — a consensus of the FASB Emerging Issues Task Force**

ASU 2010-27, **Other Expenses (Topic 720): Fees Paid to the Federal Government by Pharmaceutical Manufacturers — a consensus of the FASB Emerging Issues Task Force**

ASU 2010-20, **Receivables (Topic 310): Disclosures About the Credit Quality of Financing Receivables and the Allowance for Credit Losses**

ASU 2009-13, **Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements — a consensus of the FASB Emerging Issues Task Force**

**FASB Accounting Standards Codification (ASC) Topics**

ASC 205, **Presentation of Financial Statements**

ASC 210, **Balance Sheet**

ASC 220, **Income Statement — Reporting Comprehensive Income**

ASC 230, **Statement of Cash Flows**

ASC 235, **Notes to Financial Statements**

ASC 250, **Accounting Changes and Error Corrections**

ASC 260, **Earnings per Share**

ASC 280, **Segment Reporting**

ASC 320, **Investments — Debt and Equity Securities**

ASC 321, **Investments — Equity Securities**

ASC 323, **Investments — Equity Method and Joint Ventures**

ASC 325, **Investments — Other**

ASC 326, **Financial Instruments — Credit Losses**

ASC 330, **Inventory**

ASC 350, **Intangibles — Goodwill and Other**

ASC 360, **Property, Plant, and Equipment**

ASC 410, **Asset Retirement and Environmental Obligations**
Appendix A — Glossary of Standards and Other Literature

ASC 420, Exit or Disposal Cost Obligations
ASC 450, Contingencies
ASC 470, Debt
ASC 480, Distinguishing Liabilities From Equity
ASC 505, Equity
ASC 605, Revenue Recognition
ASC 606, Revenue From Contracts With Customers
ASC 610, Other Income
ASC 715, Compensation — Retirement Benefits
ASC 718, Compensation — Stock Compensation
ASC 720, Other Expenses
ASC 730, Research and Development
ASC 740, Income Taxes
ASC 805, Business Combinations
ASC 808, Collaborative Arrangements
ASC 810, Consolidation
ASC 815, Derivatives and Hedging
ASC 820, Fair Value Measurement
ASC 825, Financial Instruments
ASC 830, Foreign Currency Matters
ASC 840, Leases
ASC 842, Leases
ASC 845, Nonmonetary Transactions
ASC 915, Development Stage Entities
ASC 958, Not-for-Profit Entities
ASC 985, Software
Proposed FASB Accounting Standards Updates (Proposed ASUs)
Proposed ASU 2018-200, Leases (Topic 842): Targeted Improvements


FASB Proposed Accounting Standards Update 2017-280, Consolidation (Topic 812): Reorganization


Proposed ASU 2017-220, Compensation — Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting

Proposed ASU 2017-210, Inventory (Topic 330): Disclosure Framework — Changes to the Disclosure Requirements for Inventory

Proposed ASU 2017-200, Debt (Topic 470): Simplifying the Classification of Debt in a Classified Balance Sheet (Current Versus Noncurrent)


Proposed ASU 2015-340, Government Assistance (Topic 832): Disclosures by Business Entities About Government Assistance

Proposed ASU 2015-310, Notes to Financial Statements (Topic 235): Assessing Whether Disclosures Are Material

Other FASB Proposal

FASB Statements (Pre-Codification Literature)
Statement No. 167, Amendments to FASB Interpretation No. 46(R)

Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements — an amendment of ARB No. 51

Statement No. 141(R), Business Combinations

FASB Interpretations (Pre-Codification Literature)
FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109

FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities
**FASB Concepts Statements**
No. 5, *Recognition and Measurement in Financial Statements of Business Enterprises*

No. 6, *Elements of Financial Statements*

**EITF Issues (Pre-Codification Literature)**
Issue 09-4, “Seller Accounting for Contingent Consideration”

Issue 08-1, “Revenue Arrangements With Multiple Deliverables”

Issue 04-5, “Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights”

Issue 01-9, “Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)”

Issue 01-8, “Determining Whether an Arrangement Contains a Lease”

Issue 00-21, “Revenue Arrangements With Multiple Deliverables”

**PCAOB Auditing Standard**

**SEC C&DI Topic**
Non-GAAP Financial Measures

**SEC Interpretive Release**
33-10403, *Updates to Commission Guidance Regarding Accounting for Sales of Vaccines and Bioterror Countermeasures to the Federal Government for Placement Into the Pediatric Vaccine Stockpile or the Strategic National Stockpile*

**SEC Regulation G**
“Conditions for Use of Non-GAAP Financial Measures”

**SEC Regulation S-K**
Item 10(e), “General; Use of Non-GAAP Financial Measures in Commission Filings”

Item 103, “Business; Legal Proceedings.”

**SEC Regulation S-X**
Rule 3-05, “Financial Statements of Businesses Acquired or to Be Acquired”

Rule 3-09, “Separate Financial Statements of Subsidiaries Not Consolidated and 50 Percent or Less Owned Persons”

Rule 3-14, “Special Instructions for Real Estate Operations to Be Acquired”
Rule 4-08(g), “General Notes to Financial Statements; Summarized Financial Information of Subsidiaries Not Consolidated and 50 Percent or Less Owned Persons”

Rule 4-08(h), “General Notes to Financial Statements; Income Tax Expense”

**SEC Staff Accounting Bulletins (SABs)**

SAB Topic 1.M, “Financial Statements; Materiality”

SAB Topic 5.Y, “Miscellaneous Accounting; Accounting and Disclosures Relating to Loss Contingencies”

SAB Topic 11.A, “Miscellaneous Disclosure; Operating-Differential Subsidies”

SAB Topic 13, “Revenue Recognition”

SAB Topic 13.A.4, “Revenue Recognition; Selected Revenue Recognition Issues; Fixed or Determinable Sales Price”

SAB Topic 13.B, “Revenue Recognition; Disclosures”

SAB 116, “Staff Accounting Bulletin No. 116”

SAB 118, codified as SEC Staff Accounting Bulletin Topic 5.EE, “Miscellaneous Accounting; Income Tax Accounting Implications of the Tax Cuts and Jobs Act”

**Internal Revenue Code (IRC)**

IRC Section 78, “Gross Up for Deemed Paid Foreign Tax Credit”

IRC Section 163(j), “Interest; Limitation on Business Interest”

IRC Section 199, “Income Attributable to Domestic Production Activities”

IRC Section 383, “Special Limitations on Certain Excess Credits, Etc.”

IRC Section 787, “Termination of Private Foundation Status”

IRC Section 965, “Treatment of Deferred Foreign Income Upon Transition to Participation Exemption System of Taxation”

IRC Section 4191, “Medical Devices”

**International Standards**

IFRS 16, *Leases*

IFRS 15, *Revenue From Contracts With Customers*

IFRS 11, *Joint Arrangements*

IFRS 3, *Business Combinations*

IAS 20, *Accounting for Government Grants and Disclosure of Government Assistance*
## Appendix B — Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>AFS</td>
<td>available for sale</td>
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<tr>
<td>AICPA</td>
<td>American Institute of Certified Public Accountants</td>
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<tr>
<td>AMT</td>
<td>alternative minimum tax</td>
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<tr>
<td>AOCl</td>
<td>accumulated other comprehensive income</td>
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<td>API</td>
<td>active pharmaceutical ingredient</td>
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<td>APIC</td>
<td>additional paid-in capital</td>
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<td>ASC</td>
<td>FASB Accounting Standards Codification</td>
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<td>ASU</td>
<td>FASB Accounting Standards Update</td>
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<td>BCF</td>
<td>beneficial conversion feature</td>
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<td>BEAT</td>
<td>base erosion anti-abuse tax</td>
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<td>BEMTA</td>
<td>base erosion minimum tax amount</td>
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<td>BPD</td>
<td>branded prescription drug</td>
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<td>BOLI</td>
<td>bank-owned life insurance</td>
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<td>CAM</td>
<td>critical audit matter</td>
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<tr>
<td>C&amp;DI</td>
<td>SEC Compliance and Disclosure Interpretation</td>
</tr>
<tr>
<td>CECL</td>
<td>current expected credit loss</td>
</tr>
<tr>
<td>CFC</td>
<td>controlled foreign corporation</td>
</tr>
<tr>
<td>CODM</td>
<td>chief operating decision maker</td>
</tr>
<tr>
<td>COLI</td>
<td>corporate-owned life insurance</td>
</tr>
<tr>
<td>CRO</td>
<td>contract research organization</td>
</tr>
<tr>
<td>CTA</td>
<td>cumulative translation adjustment</td>
</tr>
<tr>
<td>DCPs</td>
<td>disclosure controls and procedures</td>
</tr>
<tr>
<td>DTA</td>
<td>deferred tax asset</td>
</tr>
<tr>
<td>DTL</td>
<td>deferred tax liability</td>
</tr>
<tr>
<td>EBITDA</td>
<td>earnings before interest, taxes, depreciation, and amortization</td>
</tr>
<tr>
<td>EITF</td>
<td>FASB Emerging Issues Task Force</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>E&amp;P</td>
<td>earnings and profits</td>
</tr>
<tr>
<td>EPS</td>
<td>earnings per share</td>
</tr>
<tr>
<td>EU</td>
<td>European Union</td>
</tr>
<tr>
<td>FAQ</td>
<td>frequently asked question</td>
</tr>
<tr>
<td>FASB</td>
<td>Financial Accounting Standards Board</td>
</tr>
<tr>
<td>FDA</td>
<td>Food and Drug Administration</td>
</tr>
<tr>
<td>FDII</td>
<td>foreign derived intangible income</td>
</tr>
<tr>
<td>FIFO</td>
<td>first in, first out</td>
</tr>
<tr>
<td>FIN</td>
<td>FASB Interpretation Number (superseded)</td>
</tr>
<tr>
<td>FOB</td>
<td>free on board</td>
</tr>
<tr>
<td>GAAP</td>
<td>generally accepted accounting principles</td>
</tr>
<tr>
<td>GILTl</td>
<td>global intangible low-taxed income</td>
</tr>
<tr>
<td>GPO</td>
<td>group purchasing organization</td>
</tr>
<tr>
<td>IAS</td>
<td>International Accounting Standard</td>
</tr>
<tr>
<td>IASB</td>
<td>International Accounting Standards Board</td>
</tr>
<tr>
<td>IFRS</td>
<td>International Financial Reporting Standard</td>
</tr>
<tr>
<td>IIR</td>
<td>investigator-initiated research</td>
</tr>
<tr>
<td>IP</td>
<td>intellectual property</td>
</tr>
<tr>
<td>IPO</td>
<td>initial public offering</td>
</tr>
<tr>
<td>IPR&amp;D</td>
<td>in-process research and development</td>
</tr>
<tr>
<td>IRC</td>
<td>Internal Revenue Code</td>
</tr>
<tr>
<td>IRS</td>
<td>Internal Revenue Service</td>
</tr>
<tr>
<td>IT</td>
<td>information technology</td>
</tr>
<tr>
<td>LIFO</td>
<td>last in, first out</td>
</tr>
<tr>
<td>LLC</td>
<td>limited liability company</td>
</tr>
<tr>
<td>Abbreviation</td>
<td>Description</td>
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<tr>
<td>--------------</td>
<td>--------------------------------------------------</td>
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<tr>
<td>LP</td>
<td>limited partnership</td>
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<tr>
<td>M&amp;A</td>
<td>merger and acquisition</td>
</tr>
<tr>
<td>MD&amp;A</td>
<td>Management’s Discussion and Analysis</td>
</tr>
<tr>
<td>MDET</td>
<td>medical device excise tax</td>
</tr>
<tr>
<td>MSL</td>
<td>medical science liaison</td>
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<tr>
<td>NFP</td>
<td>not-for-profit entity</td>
</tr>
<tr>
<td>NOL</td>
<td>net operating loss</td>
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<tr>
<td>OCI</td>
<td>other comprehensive income</td>
</tr>
<tr>
<td>OEM</td>
<td>original equipment manufacturer</td>
</tr>
<tr>
<td>OECD</td>
<td>Organisation for Economic Co-operation and Development</td>
</tr>
<tr>
<td>PBE</td>
<td>public business entity</td>
</tr>
<tr>
<td>PCAOB</td>
<td>Public Company Accounting Oversight Board</td>
</tr>
<tr>
<td>PCC</td>
<td>Private Company Council</td>
</tr>
<tr>
<td>PCD asset</td>
<td>purchased financial asset with credit deterioration</td>
</tr>
<tr>
<td>PRV</td>
<td>priority review voucher</td>
</tr>
<tr>
<td>PTRS</td>
<td>probability of technical and regulatory success</td>
</tr>
<tr>
<td>Q&amp;A</td>
<td>question and answer</td>
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<tr>
<td>R&amp;D</td>
<td>research and development</td>
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<tr>
<td>R&amp;E</td>
<td>research and experimentation</td>
</tr>
<tr>
<td>REMS</td>
<td>risk evaluation and mitigation strategy</td>
</tr>
<tr>
<td>ROU</td>
<td>right-of-use</td>
</tr>
<tr>
<td>SAB</td>
<td>SEC Staff Accounting Bulletin</td>
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<tr>
<td>SEC</td>
<td>Securities and Exchange Commission</td>
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<td>SFC</td>
<td>specified foreign corporation</td>
</tr>
<tr>
<td>SIFMA</td>
<td>Securities Industry and Financial Markets Association</td>
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<tr>
<td>T.D.</td>
<td>Treasury Decision</td>
</tr>
<tr>
<td>TRG</td>
<td>transition resource group</td>
</tr>
<tr>
<td>UTB</td>
<td>unrecognized tax benefit</td>
</tr>
<tr>
<td>VIE</td>
<td>variable interest entity</td>
</tr>
<tr>
<td>WAC</td>
<td>wholesaler acquisition cost</td>
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</tbody>
</table>
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