FASB proposal

Improvements to income tax disclosures

March 16, 2023

Enhanced jurisdictional and other disaggregated disclosures for the effective tax rate reconciliation and income taxes paid

Source and applicability

- Proposed ASU, Improvements to Income Tax Disclosures
- All entities subject to income taxes

Fast facts, impacts, actions

The proposed amendments would enhance income tax disclosures to address investor requests for more information about the tax risks and opportunities present in an entity's worldwide operations. The proposed ASU's two primary enhancements would disaggregate existing income tax disclosures.

	Public business entities	Other entities
Effective tax rate reconciliation for annual periods	Disclose a tabular reconciliation using both percentages and amounts, broken out into specific categories with certain reconciling items above a 5% threshold further broken out by nature and/or jurisdiction.	Qualitatively disclose the nature and effect of significant differences between the statutory tax rate in the jurisdiction (country) of domicile and the effective tax rate by specific categories of reconciling items, including other individual jurisdictions.
Income taxes paid	Disclose in annual and interim periods income taxes paid (net of refunds received) year-to-date, broken out between federal (national), state and foreign. Disclose in annual periods the income taxes paid (net of refunds received) to an individual jurisdiction when more than 5% of the total.	

Additional discussion is provided herein about these and other disclosure enhancements and changes in the proposed ASU. Comments on the proposal are due to the FASB no later than May 30, 2023.

We expect the final income tax disclosure enhancements to be directionally consistent with the proposal. Now is the time for an entity to understand the effects these enhancements would have on their existing disclosure processes and related controls, and to determine whether providing feedback to the FASB is warranted.

Proposed enhancements and other changes

Replacing ‘public entity’ with ‘public business entity’

The proposed ASU would replace the term ‘public entity’ used in the current income tax disclosure requirements with the term ‘public business entity.’ An entity that is not considered a public entity, but meets the definition of a public business entity (PBE), would be subject to:

- the enhancements and other changes in the proposed ASU applicable to PBEs; and
- other income tax disclosure requirements not affected by the proposed ASU currently applicable to public entities, such as the requirement to disclose temporary differences and carryforwards that give rise to a significant portion of deferred tax liabilities and assets.

Introducing new and enhanced disclosures

The following table summarizes the new and enhanced income tax disclosure requirements included in the proposed ASU.

Disclosure	PBEs/other entities	Annual/interim
Effective tax rate reconciliation		
Tabular reconciliation of statutory tax[1] and reported tax using both percentages and amounts, broken out into specific categories with certain reconciling items above a 5% threshold further broken out by nature and/or jurisdiction, along with: • qualitative description of the jurisdictions that make up the majority of the reconciling item for state and local taxes; and • additional information about certain individual reconciling items that exceed the 5% threshold (e.g. nature, effect, significant year-over-year changes) Additional information about and an example of the tabular reconciliation is provided below.	PBEs only	Annual
Description of any year-to-date reconciling items that significantly change the estimated annual effective tax rate compared to the effective tax rate of the prior annual reporting period	PBEs only	Interim
Qualitative discussion of the nature and effect of significant differences between the statutory tax rate and the effective tax rate by specific categories of reconciling items[2] and by individual jurisdictions (see example in paragraph 740-10-55-233 of the proposed ASU)	Other entities only	Annual
Income taxes paid		
Income taxes paid (net of refunds received) year-to-date, broken out between federal (national), state and foreign	Both	Annual and interim
Income taxes paid (net of refunds received) to an individual jurisdiction when the amount exceeds 5% of the total income taxes paid (net of refunds received)	Both	Annual

Disclosure	PBEs/other entities	Annual/interim
Other disaggregated amounts		
Income (or loss) from continuing operations before income taxes, broken out between domestic and foreign[3]	Both	Annual
Income tax expense (or benefit) from continuing operations, broken out between federal (national), state and foreign[3, 4]	Both	Annual

Notes:

1. The proposed ASU indicates that the applicable statutory federal (national) income tax rate in the jurisdiction (country) of domicile would be used in the tabular reconciliation. However, in paragraph BC21 of the proposed ASU, the FASB notes that "an entity domiciled in a jurisdiction with no or minimal statutory tax rates, but has significant business activities in other jurisdictions with higher statutory tax rates" may use a higher federal (national) tax rate to provide more relevant and meaningful information in the reconciliation. We believe this is generally consistent with Regulation S-X 210.4-08(h)(2), which indicates the statutory tax rate should normally be the rate in the jurisdiction of domicile.
2. The same categories are used for this purpose as are used by PBEs in the tabular reconciliation.
3. Disclosure of similar information is already required by SEC regulations.
4. Income taxes on foreign earnings imposed by the jurisdiction (country) of domicile would be presented with the other income taxes imposed by the jurisdiction (country) of domicile.

Removing disclosures

The proposed ASU would remove disclosure requirements for all entities related to:

- reasonably possible significant changes in the total amount of unrecognized tax benefits within 12 months of the reporting date; and
- the cumulative amount of each type of temporary difference for which a deferred tax liability has not been recognized (due to the exception to recognizing deferred taxes related to subsidiaries and corporate joint ventures).

Tabular rate reconciliation for PBEs

The proposed ASU would require disclosure of a tabular reconciliation between the following two amounts and the related rates for each annual reporting period:

- the statutory tax (i.e. expected tax), which would be calculated by multiplying the income or loss from continuing operations by the statutory tax rate in the jurisdiction (country) of domicile; and
- the reported tax (i.e. effective tax), which would be the reported amount of income tax expense (or benefit) from continuing operations.

The objective of this reconciliation would be to provide information about what causes the difference between the expected tax and the reported tax, which is particularly relevant when an entity operates in various jurisdictions. The objective is principally focused on providing insight into the nature and magnitude of the factors giving rise to the difference between the expected tax and reported tax.

While public entities are currently required to disclose reconciling items in amounts **or** percentages, the proposed ASU would require disclosure of amounts **and** percentages. In addition, while entities subject to SEC regulations are currently required to disclose reconciling items using a 5% threshold, the proposed ASU would provide incremental disaggregation guidance, including about how to apply the 5% threshold.

Reconciling items

The proposed ASU includes specific guidance on the reconciling items that would be required in the tabular reconciliation of the expected tax to the reported tax. The first layer of this guidance breaks out the reconciling items into specific categories, and the second layer further breaks out the reconciling items based on a 5% threshold.

<table>
<tr><th>Categories</th><th>5% threshold</th></tr>
<tr><td>Reconciling items related to taxes in the jurisdiction (country) of domicile would be broken out into the following categories:
• state and local income tax, net of federal (national) income tax effect;[1]
• new tax laws enacted;
• effect of cross-border tax laws;[2]
• tax credits;
• valuation allowances;
• nontaxable or nondeductible items; and
• unrecognized tax benefits changes.

In addition, reconciling items arising in foreign jurisdictions would be separately disclosed.</td><td>The 5% threshold is met when a reconciling item is greater than or equal to 5% of the expected tax. Only the following reconciling items are subject to the 5% threshold.
• Reconciling items meeting the 5% threshold in the effect of cross-border tax laws, tax credits, and nontaxable or nondeductible items categories would be separately disclosed by their nature [3, 4].
• Reconciling items not within any of the categories listed at left would be separately disclosed by their nature[3].
• Each foreign jurisdiction that meets the 5% threshold would be disclosed by jurisdiction.
• Reconciling items within a foreign jurisdiction meeting the 5% threshold would be separately disclosed by jurisdiction and nature[3], even if the foreign jurisdiction itself does not meet the 5% threshold.</td></tr>
<tr><td colspan="2">Notes:
1. Includes income taxes imposed at the state or local level in the jurisdiction (country) of domicile.
2. Includes the effect of incremental income taxes imposed by the jurisdiction (country) of domicile on income earned abroad or by foreign subsidiaries.
3. When identifying reconciling items by their nature, an entity would consider their fundamental or essential characteristics. Examples of these characteristics include the event giving rise to, or the activity associated with, the reconciling item.
4. Further disaggregation of the reconciling items in the state and local income tax, new tax laws enacted, valuation allowances and unrecognized tax benefits changes categories would not be required.</td></tr>
</table>

The 5% threshold for reconciling items would not eliminate the need for judgment to be exercised in categorizing those reconciling items presented. The FASB indicates in paragraph BC17 of the proposed ASU that an entity would need to assess whether the disclosure objective is met when judgment is applied in the categorization process.

Detailed example

Provided below is an example of what the effective tax rate reconciliation could look like under the proposed ASU. This example is for illustrative purposes only. The information presented would be subject to materiality considerations and based on entity-specific facts and circumstances. The example is based on the example presented in the proposed ASU and therefore is subject to change based on the final ASU. It assumes the jurisdiction (country) of domicile is the US, and so the US federal statutory income tax rate is reconciled to the entity's effective tax rate. For ease of illustration, the example assumes the reporting entity is only required to present one comparative period in its financial statements.

	Year 2		Year 1	
	Amount	**Percent**	**Amount**	**Percent**
US federal statutory income tax rate	2,520	21.0%	2,100	21.0%
Domestic				
State and local income taxes, net of federal effect	400	3.3%	350	3.5%
Tax credits				
• Research	(250)	-2.1%	(240)	-2.4%
• Other	(20)	-0.2%	(15)	-0.2%
Nondeductible and tax-exempt items, net	60	0.5%	60	0.6%
Cross-border taxes				
• Global intangible low-taxed income	180	1.5%	180	1.8%
• Other	10	0.1%	15	0.2%
Changes in unrecognized tax benefits	200	1.7%	(400)	-4.0%
Excess tax benefits on share-based payments	(400)	-3.3%	(410)	-4.1%
Other	50	0.4%	(40)	-0.4%
Foreign				
United Kingdom				
Enactment of new tax laws	-	-	300	3.0%
Nondeductible and tax-exempt items, net	150	1.3%	120	1.2%
Other	100	0.8%	90	0.9%
Ireland				
Rate differential	(350)	-2.9%	(280)	-2.8%
Other	10	0.1%	5	0.1%
China				
Change in valuation allowance	5	0.0%	(300)	-3.0%
Other	20	0.2%	25	0.2%
Singapore	(150)	-1.3%	(120)	-1.2%
Other foreign jurisdictions	(300)	-2.5%	(20)	-0.2%
Total	**2,235**	**18.6%**	**1,420**	**14.2%**

For many PBEs, preparation of the tabular reconciliation could be a significant undertaking. Reviewing the preceding example and the example in paragraph 740-10-55-231 of the proposed ASU and considering the reconciling items that would be needed for a specific entity based on its own facts and circumstances may help crystalize the effort involved.

Transition and effective date

The proposed amendments would be applied retrospectively to all prior periods presented.

The proposed ASU does not include an effective date or indicate whether early adoption would be allowed. The FASB has specifically asked constituents to comment on both for consideration in their final deliberations.

Next steps

The FASB is expected to redeliberate issues identified in the comments received and then determine whether it should proceed with issuing a final ASU. While it is difficult to predict the timing for a final ASU, it is possible that one could be issued before the end of 2023.

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