



# Accounting for Income Taxes Quarterly Updates

**October 2021**



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## **Accounting considerations of tax proposals for budget reconciliation legislation**

KPMG recently issued a [report](#) that provides a summary and analysis of legislation approved by the House Ways and Means Committee on tax proposals contributing to the Build Back Better Act moving through the House. The Ways and Means Committee recommendations will be packaged together with recommendations from other committees for subsequent consideration by the House. Included in the KPMG report are selected areas of accounting for income taxes considerations that may be impacted by the House Ways and Means Committee proposals.

Previously, KPMG issued a [report](#) on the analysis and observations of the Biden Administration's tax proposals provided in the *General Explanations of the Administration's Fiscal Year 2022 Revenue Proposals* (Green Book) prepared by the Department of the Treasury and released in May 2021, including selected areas of accounting for income taxes considerations.

As a reminder, the tax effects of changes in tax laws and rates are generally reflected in the financial statements beginning with the period that includes the date of enactment. Refer to sections 5 and 10 of the [KPMG Handbook, Accounting for income taxes](#), for additional discussion on the accounting for changes in tax laws or rates in interim and annual periods.

## **Tax Sound Bites on accounting for pass-through entity taxes**

In recent years certain state and local governments have enacted pass-through entity taxes designed as a workaround of federal limitations on the deductibility of state and local taxes for individuals. The imposition of these taxes at the entity level raises the question of whether the taxes are within the scope of ASC 740, *Income Taxes*, at the entity level or whether the pass-through entity taxes are attributable to the entities' owners. Refer to the [Tax Sound Bites](#) article *The Varying Accounting Treatment for State and Local Pass-through Entity Taxes* for analysis over the Connecticut, New York State, New York City, and Wisconsin pass-through entity taxes which are considered representative of the differing regimes for pass-through entity taxes.

## **Updates to the KPMG Accounting for income taxes handbook**

KPMG recently updated its handbook, [Accounting for income taxes](#), to add interpretive guidance on several accounting for income taxes matters, including the 2021 UK super-deduction, ASU 2020-06 (convertible debt) transition, and acceptable approaches for determining how much of a deferred tax asset is realizable when forecasting future taxable income.

A brief summary of the revisions since the April 2021 edition are reflected in the preface within the publication.



### Upcoming accounting for income taxes training

WNT's Accounting for Income Taxes group will be holding the Current Developments in Accounting for Income Taxes 2021 KLEARN on October 26th. This two-hour course will cover a discussion of SEC and PCAOB comments on income taxes and recently issued and proposed accounting standards updates impacting accounting for income taxes, amongst other items of interest on accounting for income taxes. This session will be available for playback. Please note this course is required to meet the training requirements as part of the Lead Specific Team Member – Income Taxes (LSTM-IT) designation for supporting the audit practice.

Registration and course information may be found on [Focus](#).



# Updates on accounting & auditing matters

## Practice aid: Who is Who – KPMG specialist vs. specific team member

The *Who is Who* practice aid highlighting considerations when evaluating whether an individual with specialized skill or knowledge working on an audit is a KPMG specialist, a specific team member (STM), or not a member of the engagement team, consistent with the revised methodology announced in [PPL 20-008](#), was updated in August. The revised practice aid clarifies that professionals involved in the audit evaluating intercompany pricing methods as part of EVS – Transfer pricing should be designated as STMs.

## IFRS® Standards updates

KPMG’s International Standards Group (ISG) has published *Insights into IFRS*, 18th edition. This edition includes new guidance on Deferred Tax related to Assets and Liabilities arising from a Single Transaction – Amendments to IAS 12

## Remember recent pronouncements

Professionals should be mindful of certain recently updated US GAAP standards, listed by order of required application.

Updated Standard	Brief Description of Standard	Public Business Entities Effective Date	Other Entities Effective Date
ASU 2018-09, <i>Codification Improvements</i>	Clarifies, corrects errors in, and makes improvements to several income taxes related matters	Generally, fiscal years beginning after December 15, 2018	Generally, fiscal years beginning after December 15, 2019
ASU 2017-04, <i>Simplifying the Test for Goodwill Impairment</i>	Provides guidance, amongst others, on the income tax effects from tax deductible goodwill when measuring goodwill impairment loss	Annual and interim impairment tests for periods beginning after December 15, 2019 for SEC filers other than smaller reporting companies	Annual and interim impairment tests for periods beginning after December 15, 2022
ASU 2019-12, <i>Simplifying the Accounting for Income Taxes</i>	Removes specific exceptions to the general principles of ASC 740 and improves financial statement preparers’ application of income tax-related guidance and simplifies GAAP for certain income tax items	Fiscal years beginning after December 15, 2020, and interim periods within those fiscal years	Fiscal years beginning after December 15, 2021, and interim periods within fiscal years beginning after December 15, 2022

Engagement teams should be mindful of the recently updated IFRS Standards.

Updated Standard	Brief Description of Standard	Effective Date
<i>Deferred Tax related to Assets and Liabilities arising from a Single Transaction (Amendments to IAS 12)</i>	Narrows the scope of the initial recognition exemption so that it does not apply to transactions that give rise to equal and offsetting temporary differences (for example, leases and decommissioning provisions)	Annual reporting periods beginning on or after January 1, 2023, with earlier application permitted

and modified guidance on the interim accounting for prior year tax expense, changes in tax rates, nontaxable income and changes in estimates of the recoverability of deferred tax assets. To learn more or for details on how to order the book, visit the [web article](#).

## KPMG DPP quarterly releases

KPMG DPP published the following accounting and financial reporting developments releases:

— [Quarterly Outlook – September 2021](#)

Watch for the following accounting and financial reporting development to be released on Alex:

— Quarterly Reminders Practice Aid (9/21)



## On the horizon

### **FASB adds Investments in Tax Credit Structures project to its technical agenda**

At a [September agenda prioritization meeting](#), the Financial Accounting Standards Board (FASB or the Board) decided to add a project to its technical agenda on investments in tax credit structures. The Board decided the project, EITF 21-A, *Accounting for Investments in Tax Credit Structures Using the Proportional Amortization Method*, will be addressed by the Emerging Issues Task Force (EITF) and is intended to expand the proportional amortization method to investments in tax credits other than low income housing tax credit (LIHTC) investments. Additionally, the project is expected to evaluate whether the current criteria for an investment to be accounted for using the proportional amortization method are also operable for investments in tax credit structures other than LIHTC structures.

### **FASB projects**

The FASB's [Disclosure Review: Income Taxes](#) project continues to be in the revised exposure draft redeliberations stage after the Board directed the staff in February 2020 to perform research and additional outreach on potential alternatives to disclose certain disaggregated income taxes information and to perform additional research on other proposed amendments.

In June 2021, as part of a broader [invitation to comment](#), the FASB asked investors and other financial statement users for information about whether income taxes should be a top priority for the FASB to consider requiring greater disaggregation and asked preparers what requests or questions are received about disaggregation of income taxes. [Comments](#) were due on September 22, 2021.



In May 2021, the Board [instructed](#) the FASB staff to prepare a final ASU for vote by written ballot related to its [Government Assistance \(Topic 832\): Disclosures by business entities about government assistance](#) project. The Board decided that the disclosures should apply to a business entity that has accounted for a transaction with a government by analogizing to a grant or contribution accounting model and that the amendments should be effective for fiscal years beginning after December 15, 2021 for all business entities, with early adoption permitted. The amendments would require disclosures identifying the nature of the government assistance, the accounting policy used, the line items on the balance and income statement affected by the assistance, and significant terms and conditions of the assistance.

### **IASB projects**

In July 2021, the International Accounting Standards Board (IASB) published the Exposure Draft [Subsidiaries without Public Accountability: Disclosures](#), which sets out the IASB's proposals for a new IFRS Standard that would permit eligible subsidiaries to apply IFRS Standards with reduced disclosure requirements in the financial statements, including those related to income taxes.

The deadline for submitting comments on the Exposure Draft is January 31, 2022. The IASB will consider feedback on the Exposure Draft in developing the new standard.



## Questions from the field

### **How are deferred taxes recognized for liabilities assumed in a taxable business combination?**

In a taxable business combination, the tax bases of assets acquired and liabilities assumed are generally stepped up to fair value at the acquisition date for both financial statement and income tax purposes. Although the recognized amount for both financial statement purposes and income tax purposes may be stepped up, the amounts assigned to the individual assets and liabilities may differ in certain circumstances. For example, this may occur when the tax law does not recognize a liability for a contingent obligation that is required to be recognized under ASC 805, *Business Combinations*. As a result, questions arise related to whether deferred taxes should be recognized for assumed liabilities. The answer will typically depend on the circumstance as liabilities will generally fall into one of the following categories.

#### *Liabilities with a tax basis equal to the financial statement carrying amount at acquisition*

For liabilities where the financial statement carrying amount and the tax basis are the same at the acquisition date and are not expected to result in future deductions when settled, no deferred taxes are provided because no temporary difference exists at the acquisition date.

#### *Liabilities with no tax basis at acquisition (deductible when paid)*

Some liabilities of the acquired entity recognized for financial reporting purposes have no tax basis as of the acquisition date and are expected to result in a future deduction for income tax purposes when settled. Therefore, a deferred tax asset should be established for these liabilities that will become deductible when paid.

#### *Liabilities with no tax basis at acquisition (capitalized when paid)*

Some liabilities of the acquired entity recognized for financial reporting purposes as of the acquisition date, such as liabilities for anticipated settlement of litigation and environmental matters, have no tax basis at the acquisition date. These liabilities may not result in an immediate deduction when they are settled, but instead will be considered additional consideration for the business and result in additional tax basis in the assets acquired, such as goodwill, other intangibles or fixed assets, and provide additional amortization or depreciation deductions. Instead of recognizing a deferred tax asset for these liabilities, we believe the acquisition-date financial statement carrying amount of these liabilities should be characterized as tax-deductible goodwill when determining the amount of first and second components of goodwill, even if settlement is expected to result in additional tax basis in an asset other than goodwill.

Refer to paragraphs 6.086 and 6.079 of the KPMG Handbook, [Accounting for income taxes](#), for additional detail.



## How are deferred taxes recognized for pass-through subsidiaries?

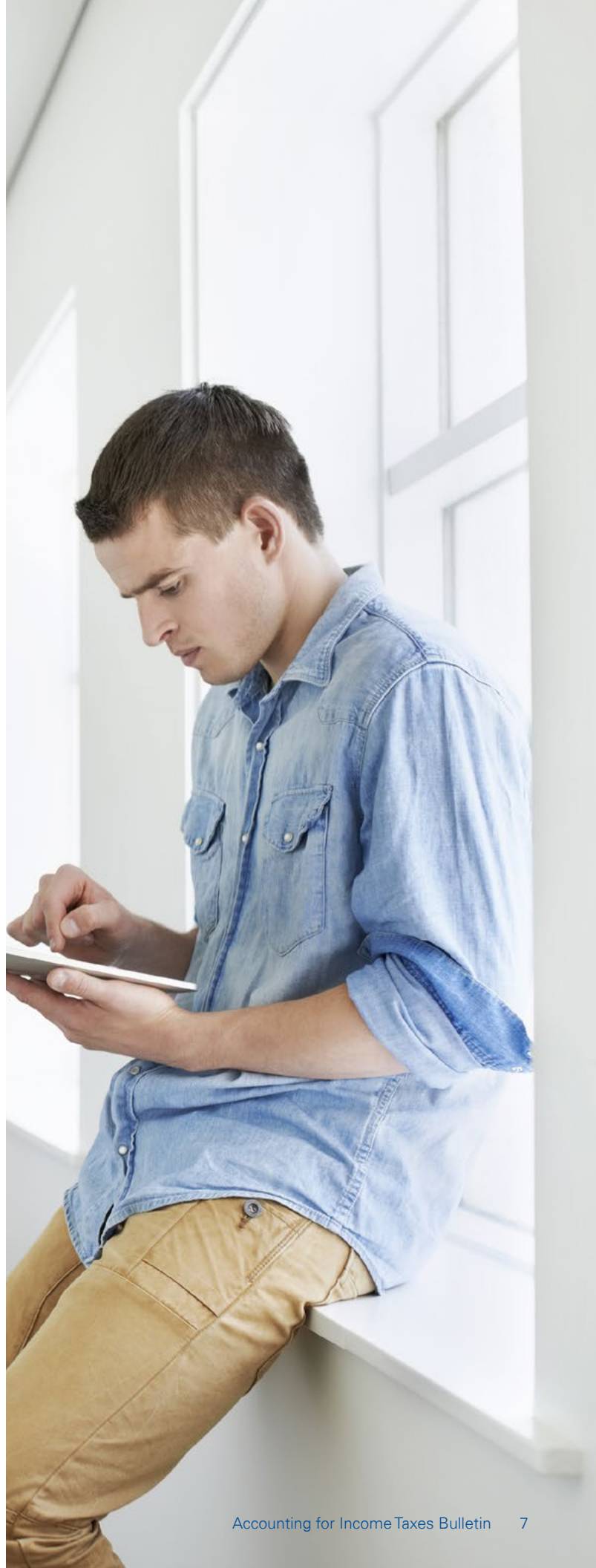
Taxable income and losses flow through pass-through entities to the owners of the entity and are reported with the respective owners' taxable income or loss. Because these entities are not subject to income taxes directly, questions arise as to how a consolidating investor should account for the income tax consequences of its investment in such entities.

Deferred taxes are recognized for the outside basis differences of investments in pass-through subsidiaries, as the differences will generally have a future tax consequence to the parent either when the investment in the subsidiary is sold or when the inside basis differences of the subsidiary reverse and flow through to the parent. The exceptions to the recognition of deferred taxes for outside basis differences generally do not apply to the outside basis difference of the investment in pass-through subsidiaries.

Deferred taxes generally should not be recognized for the portion of the outside basis difference that relates to a pass-through subsidiary's investment in a second-tier corporate subsidiary that meets one of the exceptions to recognizing deferred taxes for outside basis differences. Similarly, an ultimate corporate parent company may not recognize deferred taxes on the portion of its outside basis difference for its investment in a pass-through subsidiary attributable to nondeductible goodwill.

However, KPMG acknowledges diversity in practice where some recognize deferred taxes for the entire basis difference. KPMG would not object to a consistently applied policy either to (a) look through the outside basis difference and exclude all items for which ASC 740 provides an exception to recognition, or (b) record deferred taxes on the entire outside basis difference.

Refer to paragraphs 10.099 and 10.100 of the KPMG Handbook, *Accounting for income taxes*, for additional detail.





## Other items of interest

### **KPMG learning—executive education**

The following **Accounting for Income Taxes Executive Education** courses will be offered:

— December 7 – 10, 2021

This live, virtual seminar is designed to help you understand and apply accounting for income taxes under ASC 740, including the effect of the 2017 tax reform. This interactive course does more than describe technical requirements; the rationale and consequences of the relevant accounting standards will be explained using easy-to-follow examples with detailed journal entries.

Additionally, the following **Advanced Accounting for Income Taxes Executive Education** courses will be offered:

— November 9 – 12, 2021

— November 30 – December 2, 2021

This seminar covers complex aspects of ASC 740 by building upon our intermediate level Accounting for Income Taxes course. For example, the intermediate seminar only covers acquisitions with no tax-deductible goodwill, while this seminar covers tax deductible goodwill, section 338 elections, contingent consideration, transaction costs, and measurement period adjustments. We go beyond describing the technical requirements; we explain the rationale and the consequences of these standards and use examples with journal entries. Complex aspects of ASC 740, including the Tax Cuts and Jobs Act, are covered.

KPMG also offers digital self-studies, which are mobile-friendly and easily accessible at the learner's convenience. The CPE-eligible curriculum covers current and emerging technical accounting topics, including accounting for income taxes, to build skills and confidence in a variety of areas of accounting.

View the catalog of KPMG **virtual seminars** and digital **self-studies**.

### **Look who's talking**

Jenna Summer and Cliff Crockett presented on current developments in accounting for income taxes at a Dallas tax chat event on August 3rd.

Nick Canitano and Mike Pezzetti presented on ASC 740 impacts of tax reform at a Cleveland TEI fall event on September 27th.

Ashby Corum presented on accounting for income taxes at KPMG Norfolk's Accounting and Financial Reporting Update on September 28th.



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