Accounting for Income Taxes – Tax Reform and Other Current Developments

2019 U.S. Cross-Border Tax Conference
May 14 – 16, 2019

tax.kpmg.us
Notices

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The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser.
Agenda

01 Continuing accounting for income taxes considerations of tax reform

02 Proposed ASU: Disclosure framework – Changes to the disclosure requirements for income taxes

03 Forthcoming proposed ASU on simplifications to accounting for income taxes

04 SEC comments on cross-border income taxes matters
## Today’s Presenters

<table>
<thead>
<tr>
<th>Name</th>
<th>Title</th>
<th>Firm/Company Name</th>
<th>Email</th>
</tr>
</thead>
<tbody>
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<td>Partner</td>
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</tbody>
</table>
Continuing accounting for income taxes considerations of tax reform
Excessive executive compensation

- Changes covered employees to principal executive officer, principal financial officer and three other highest compensated officers
- Removes exceptions for commissions and performance based compensation
- Employees that are covered persons remain covered persons for all future years

— Current tax impact
  - Increase in nondeductible compensation may increase taxable income and the effective tax rate

— Deferred tax impact
  - §162(m) limitations should be considered in measuring deferred tax assets on share-based compensation
    — Two most common methods used in practice to determine which compensation amounts are deductible are pro rata or stock compensation last
  - Consider impact to other compensation related deferred taxes
Net operating losses

- Limits utilization to 80 percent of taxable income for losses arising in tax years beginning after December 31, 2017
- Repeals ability to carryback net operating losses, except for certain farming losses, for losses in years ending after December 31, 2017
- Permits indefinite carryforward of losses in years ending after December 31, 2017
- Special rules for property and casualty insurance companies

— Net operating loss carryforwards arising in tax years ending after December 31, 2017 may be supported with reversing taxable temporary differences differently than older losses

— Valuation allowance judgment
  - Scheduling may be required for net operating loss limitation in determining the amount of deferred tax assets supported by reversing deferred tax liabilities
  - Support of indefinite life deferred tax assets with indefinite life deferred tax liabilities
  - We believe tax-planning strategies are required to be considered for carryforwards with an indefinite life
Interest expense limitation

- **Current tax impact**
  - May result in an increase in taxable income and the effective tax rate

- **Valuation allowance judgment**
  - Consider amount and character limitations for utilization of disallowed interest carryforward, including ordering rules
  - Support of indefinite life deferred tax assets with indefinite life deferred tax liabilities

• Disallows interest expense in excess of 30 percent of adjusted taxable income (generally without regard to activity not associated with a trade or business, interest income or expense, and net operating losses, amongst other adjustments)
• For taxable years beginning after December 31, 2017 and before January 1, 2022, adjusted taxable income also excludes deductions for depreciation, amortization, or depletion
• Disallowed interest may be carried forward indefinitely
Valuation allowance analysis example

Facts
— ABC is a U.S. taxpayer with a $1,500 80 percent limited NOL carryforward and an $800 taxable temporary difference as of January 1, 2018
— ABC expects EBITDA of $1,000, depreciation of $400, and interest expense of $800 in 2018 and expects the same for future years
— ABC expects to maintain (through reversal and origination) an $800 taxable temporary difference at the end of each year
— ABC expects to indefinitely incur annual interest expense in excess of the annual limitation

Question
— How much valuation allowance does ABC need at December 31, 2018?
Valuation allowance analysis example

ABC first analyzes whether the reversal of taxable temporary differences is adequate to realize its deferred tax assets

<table>
<thead>
<tr>
<th>Income statement:</th>
<th>2018</th>
<th>2019 and beyond</th>
</tr>
</thead>
<tbody>
<tr>
<td>EBITA</td>
<td>$1,000</td>
<td>$800</td>
</tr>
<tr>
<td>Depreciation</td>
<td>(400)</td>
<td>-</td>
</tr>
<tr>
<td>Interest</td>
<td>(800)</td>
<td>-</td>
</tr>
<tr>
<td>Pretax income (loss)</td>
<td>$(200)</td>
<td>$800</td>
</tr>
<tr>
<td>Interest incurred</td>
<td>800</td>
<td>-</td>
</tr>
<tr>
<td>Allowed interest</td>
<td>(300)</td>
<td>(240)</td>
</tr>
<tr>
<td>Taxable income before NOLs</td>
<td>$300</td>
<td>$560</td>
</tr>
<tr>
<td>NOLs</td>
<td>(240)</td>
<td>(448)</td>
</tr>
<tr>
<td>Taxable income</td>
<td>$60</td>
<td>$112</td>
</tr>
</tbody>
</table>
Valuation allowance analysis example

Based upon the analysis of taxable temporary differences, the ending temporary differences and carryforwards is as follows:

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019 and beyond</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ending temporary differences and carryforwards:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>NOL</td>
<td>$1,260</td>
<td>$812</td>
</tr>
<tr>
<td>Disallowed interest</td>
<td>500</td>
<td>260</td>
</tr>
<tr>
<td>Total carryforward</td>
<td>$1,760</td>
<td>$1,072</td>
</tr>
<tr>
<td>Taxable temporary difference</td>
<td>(800)</td>
<td>-</td>
</tr>
<tr>
<td>Net</td>
<td>$960</td>
<td>$1,072</td>
</tr>
</tbody>
</table>

—As a result, ABC concludes that of its $1,760 in total carryforwards at December 31, 2018, $688 will be realized through reversal of its existing taxable temporary differences
Valuation allowance analysis example

— ABC then analyzes whether it expects future taxable income (exclusive of reversing temporary differences and carryforwards) will support the realizability of its remaining deferred tax assets

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>EBITA</td>
<td>$1,000</td>
<td>$1,000</td>
<td>$1,000</td>
<td>$1,000</td>
<td>$1,000</td>
<td>$1,000</td>
<td>$1,000</td>
<td>$1,000</td>
</tr>
<tr>
<td>Depreciation</td>
<td>(400)</td>
<td>(400)</td>
<td>(400)</td>
<td>(400)</td>
<td>(400)</td>
<td>(400)</td>
<td>(400)</td>
<td>(400)</td>
</tr>
<tr>
<td>Interest</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
</tr>
<tr>
<td>Pretax income (loss)</td>
<td>$(200)</td>
<td>$(200)</td>
<td>$(200)</td>
<td>$(200)</td>
<td>$(200)</td>
<td>$(200)</td>
<td>$(200)</td>
<td>$(200)</td>
</tr>
<tr>
<td>Interest incurred</td>
<td>800</td>
<td>800</td>
<td>800</td>
<td>800</td>
<td>800</td>
<td>800</td>
<td>800</td>
<td>800</td>
</tr>
<tr>
<td>Allowed interest</td>
<td>(300)</td>
<td>(300)</td>
<td>(300)</td>
<td>(300)</td>
<td>(180)</td>
<td>(180)</td>
<td>(180)</td>
<td>(180)</td>
</tr>
<tr>
<td>Taxable income before NOLs</td>
<td>$300</td>
<td>$300</td>
<td>$300</td>
<td>$300</td>
<td>$420</td>
<td>$420</td>
<td>$420</td>
<td>$420</td>
</tr>
<tr>
<td>NOLs</td>
<td>(240)</td>
<td>(240)</td>
<td>(240)</td>
<td>(240)</td>
<td>(336)</td>
<td>(204)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Taxable income</td>
<td>$60</td>
<td>$60</td>
<td>$60</td>
<td>$60</td>
<td>$84</td>
<td>$216</td>
<td>$420</td>
<td>$420</td>
</tr>
</tbody>
</table>
Valuation allowance analysis example

— ABC then analyzes whether it expects future taxable income (exclusive of reversing temporary differences and carryforwards) will support the realizability of its remaining deferred tax assets

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2019</th>
<th>2020</th>
<th>2021</th>
<th>2022</th>
<th>2023</th>
<th>2024</th>
<th>2025</th>
</tr>
</thead>
<tbody>
<tr>
<td>NOL</td>
<td>$1,260</td>
<td>$1,020</td>
<td>$780</td>
<td>$540</td>
<td>$204</td>
<td>$-</td>
<td>$-</td>
<td>$-</td>
</tr>
<tr>
<td>Disallowed interest</td>
<td>500</td>
<td>1,000</td>
<td>1,500</td>
<td>2,000</td>
<td>2,620</td>
<td>3,240</td>
<td>3,860</td>
<td>4,480</td>
</tr>
<tr>
<td><strong>Total carryforwards</strong></td>
<td><strong>$1,760</strong></td>
<td><strong>$2,020</strong></td>
<td><strong>$2,280</strong></td>
<td><strong>$2,540</strong></td>
<td><strong>$2,824</strong></td>
<td><strong>$3,240</strong></td>
<td><strong>$3,860</strong></td>
<td><strong>$4,480</strong></td>
</tr>
<tr>
<td>Taxable temporary difference</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
<td>(800)</td>
</tr>
<tr>
<td><strong>Net</strong></td>
<td>$960</td>
<td>$1,220</td>
<td>$1,480</td>
<td>$1,740</td>
<td>$2,024</td>
<td>$2,440</td>
<td>$3,060</td>
<td>$3,680</td>
</tr>
</tbody>
</table>

— At December 31, 2018, ABC concludes that it is more likely than not that it will realize the benefit from the remaining $1,260 of NOL carryforwards

— At December 31, 2018, ABC concludes that it is not more likely than not that it will realize any incremental benefit from the remaining $260 in disallowed interest carryforwards
Base erosion and anti-abuse tax

• Imposes a base erosion minimum tax amount based on the taxpayer’s modified taxable income (taxable income excluding base erosion payments) for the year, over an amount equal to the pre-credit regular income tax liability reduced by certain tax credits
• The tax rate is 5% (2018), 10% (2019-2025) and 12.5% (after 2025) except for banks and registered securities dealers that have rates of 6% (2018), 11% (2019-2025) and 13.5% (after 2025)

— Deferred tax impact

- Measure deferred taxes based upon the regular tax rate
- Amounts payable in excess of the regular tax liability will be treated as a periodic cost in the period incurred
- Companies would not need to consider whether they expect to pay BEAT when assessing the realizability of deferred tax assets under the regular tax system
- We believe companies may elect to consider whether they expect to pay BEAT when assessing the realizability of deferred tax assets as an accounting policy election that should be consistently applied
Global intangible low-taxed income

- Include a U.S. shareholder’s pro rata share of its CFC global intangible low-taxed income (GILTI) in taxable income
- Allows deduction for a deemed return on tangible assets
- Allows deduction equal to 50 percent (2018-2025) or 37.5 percent (after 2025) of GILTI but capped at taxable income (the Section 250 deduction)
- Provides an 80 percent foreign tax credit and separately baskets the foreign taxes with no carryforward or carryback

Deferred tax impact
- Consider and explicitly disclose policy on whether U.S. federal deferred taxes are recognized for GILTI inclusions
- If deferred taxes are recognized, we believe the net deemed tangible income return for GILTI may be akin to a special deduction; however, we would also accept consideration in the rate used to measure deferred taxes
- If deferred taxes are recognized, we believe that if a company believes it will have a section 250(a) deduction, the deduction should be considered in the rate used to measure deferred taxes
Global intangible low-taxed income

Valuation allowance
— An entity accounting for GILTI as a period cost should consider its expected GILTI when assessing the need for a valuation allowance by electing one of the following policies and applying it in a consistent manner
  - With and without approach: Deferred tax assets not supported by taxable temporary differences consider the potential displacement of one benefit by another (for instance, the foregone Section 250 deduction or foreign tax credits that would be utilized if a net operating loss carryforward did not exist)
  - Tax law ordering approach: Consider how benefits would be reflected in the tax return in order to determine which would be recognized (generally, net operating losses will be benefited prior to the Section 250 deduction or foreign tax credits, resulting in recognition of the full net operating loss deferred tax asset)

Entities may not have the same policy election if recognizing GILTI deferred taxes
— When GILTI deferreds are measured at less than 21 percent, we believe an entity should use the with and without approach
— When GILTI deferreds are measured at 21 percent, we believe an entity should use the tax law ordering approach
Global intangible low-taxed income

CFCs with different tax and financial reporting year-ends

— We believe that if a CFC has different year-ends for financial reporting purposes and U.S. federal tax purposes and the U.S. parent expects a portion of the CFCs financial reporting year related income to result in a GILTI inclusion, the U.S. parent should accrue an estimate of the related tax in the year associated with the financial reporting income.

— One approach is to treat the period from the beginning of the CFC’s U.S. federal tax year to the end of the CFC’s financial reporting year as a short period tax year:
  - U.S. parent would estimate the effect of foreign tax credits when estimating the expected GILTI tax for the hypothetical short period.
  - Under this approach, an entity would only evaluate the ability to use foreign tax credits based on the attributes arising from the CFCs hypothetical short period.

— Other acceptable approaches may be available.
Investments in subsidiaries

We believe a company considers its expected manner of recovery in determining to what extent, if any, a taxable temporary difference exists with respect to a subsidiary.

— Temporary differences may exist with respect to the following items:
  - Section 986(c) currency gains (losses) on previously taxed earnings and profits (PTEP)
  - Section 965(b) PTEP
  - Hybrid deduction accounts
  - Foreign taxes attributable to a distribution of PTEP
  - Certain other recoveries in excess of basis
  - Withholding taxes
  - State taxes

Tax reform does not eliminate the need for an entity (including a U.S. parent) to consider its assertion about the indefinite reinvestment of undistributed earnings when a taxable temporary difference exists.
Investments in subsidiaries

— Continue to evaluate the ability to assert indefinite reinvestment to avoid recognizing deferred tax consequences associated with taxes that would become due once an actual distribution is made

— Consider tax law ordering of future taxation in considering eligibility to assert

— Consider different intentions on the part of the operations of the business due to the potential accessibility of cash with limited tax cost

— We believe a company that does not assert indefinite reinvestment measures the deferred tax consequences based on the expected manner of recovery
Intraperiod tax allocation

Section 986(c) currency gains (losses) and changes in state taxes
— Changes in exchange rates resulting in an increase or decrease to the outside basis difference of an investment
— Generally adjusted through other comprehensive income when changes in exchange rates result in a translation adjustment that is recognized in other comprehensive income, subject to the intraperiod tax allocation guidance

Withholding taxes
— We believe a parent company should recognize in earnings changes to the withholding tax liability attributable to changes in exchange rates
— Elect a policy to present transaction gains (losses) in pretax income (loss) or income tax expense (benefit)
Intraperiod tax allocation example

Facts
— U.S. Parent is a calendar year-end company and a 100% shareholder of CFC1
— CFC1 is a foreign subsidiary of U.S. Parent and also has a calendar year-end
— The functional currency of U.S. Parent is U.S. dollar (USD) while the functional currency of CFC1 is FC for U.S. GAAP, U.S. income tax and local reporting purposes
— The consolidated financial statements are presented in the group’s reporting currency of USD
— Throughout 2017, the foreign exchange rate is 1.20 USD: 1 FC
— CFC1 is not subject to local income taxes; however, there is a 10% withholding tax on distributions from statutory retained earnings of CFC1 to the U.S.
— The withholding is remitted by CFC1 in FC to the taxing authority when distributions are made, but is attributed to U.S. Parent as an income tax of the U.S. Parent
— A 5% state income tax is due on distributions of earnings and profits (E&P) from CFC1 to the United States, payable in USD by U.S. Parent
— There are no book to tax basis differences in the calculation of statutory retained earnings and E&P
Intraperiod tax allocation example

During 2017, CFC1’s statutory retained earnings and E&P are as follows:

<table>
<thead>
<tr>
<th>January 1, 2017 unremitted earnings</th>
<th>Foreign currency (FC)</th>
<th>Exchange rate (FC to USD)</th>
<th>USD</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>-</td>
<td>1.2</td>
<td>-</td>
</tr>
<tr>
<td>2017 earnings</td>
<td>1,000</td>
<td>1.2</td>
<td>1,200</td>
</tr>
<tr>
<td>December 31, 2017 unremitted earnings</td>
<td>1,000</td>
<td>1.2</td>
<td>1,200</td>
</tr>
</tbody>
</table>

— U.S. Parent historically asserted indefinite reinvestment on its outside basis differences related to CFC1 but changes its assertion in Q4 2017

— After being subject to the transition tax (deemed repatriation), the 1,000 FC of E&P is considered PTEP for U.S. federal income tax purposes and U.S. Parent receives $1,200 of tax basis in the PTEP

— U.S. Parent expects to recover its investment in CFC1 through periodic distributions of earnings over its life, followed by a liquidation at an indefinite point in the future

— It is apparent that the PTEP will be distributed in early 2019 and no valuation allowance would be required for any related U.S. federal deferred tax assets
Intraperiod tax allocation example

U.S. Parent calculates its deferred tax liability for withholding and state income taxes as follows:

<table>
<thead>
<tr>
<th></th>
<th>Withholding taxes</th>
<th>State income taxes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Statutory retained earnings or E&amp;P</td>
<td>FC 1,000</td>
<td>FC 1,000</td>
</tr>
<tr>
<td>December 31, 2017 spot rate</td>
<td>1.2</td>
<td>1.2</td>
</tr>
<tr>
<td>USD equivalent</td>
<td>$1,200</td>
<td>$1,200</td>
</tr>
<tr>
<td>Tax rate</td>
<td>10%</td>
<td>5%</td>
</tr>
<tr>
<td>Deferred tax liability</td>
<td>$120</td>
<td>$60</td>
</tr>
</tbody>
</table>

—As the entire deferred tax liability is attributable to 2017 earnings, the related deferred tax expense is allocated to income tax expense attributable to continuing operations
Intraperiod tax allocation example

— During 2018, CFC1 generates an additional 600 FC of earnings increasing statutory retained earnings and E&P for state income tax purposes to 1,600 FC

— For U.S. federal income tax purposes the 600 FC of earnings are eligible for a 100% dividends received deduction

— The average exchange rate for 2018 is 1.10 USD: 1 FC and the December 31, 2018 exchange rate is 1.00 USD: 1 FC

— CFC1’s statutory retained earnings activity and state E&P activity during 2018 is summarized as follows, along with a rollforward of the related deferred tax liability recognized by U.S. Parent

<table>
<thead>
<tr>
<th>December 31, 2017 unremitted earnings</th>
<th>Foreign currency (FC)</th>
<th>Exchange rate (FC to USD)</th>
<th>USD</th>
<th>Withholding deferred tax liability</th>
<th>State deferred tax liability</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018 earnings</td>
<td>FC 1,000</td>
<td>1.2</td>
<td>$1,200</td>
<td>$120</td>
<td>$60</td>
</tr>
<tr>
<td>FX movement</td>
<td>600</td>
<td>1.1</td>
<td>660</td>
<td>66</td>
<td>33</td>
</tr>
<tr>
<td>December 31, 2018 unremitted earnings</td>
<td>FC 1,600</td>
<td>1.0</td>
<td>$1,600</td>
<td>$160</td>
<td>$80</td>
</tr>
</tbody>
</table>

— U.S. Parent recognizes a U.S. federal deferred tax asset of $16 for the currency loss related to PTEP (($1,200 tax basis in PTEP - $1,000 USD equivalent PTEP) x 8%)
Intraperiod tax allocation example

— The $26 benefit arising from the remeasurement of the FC denominated withholding deferred tax liability is a transaction gain in accordance with ASC 830
  - U.S. Parent can elect a policy to present such transaction gains or losses in pretax income (loss) or in income tax expense (benefit) as long as the policy is consistently applied, but must disclose the amounts as part of total transaction gains (losses) in the notes to financial statements

— If U.S. Parent were expected to take a FTC for the withholding taxes and could recognize the related deferred tax asset without a valuation allowance, we believe the benefit for the U.S. federal effect of the withholding deferred tax liability would be recognized in income tax expense (benefit) from continuing operations

— The $13 deferred tax benefit from the remeasurement on the state deferred tax liability, along with any federal effect of the state deferred tax liability, and the $16 deferred tax benefit from the remeasurement of the U.S. federal deferred tax asset for PTEP would be allocated under the step-by-step approach, generally resulting in the amounts being allocated to the cumulative translation adjustment account within other comprehensive income
US federal effect of foreign branch deferred taxes

— U.S. tax law generally allows taxpayers to take a FTC for taxes paid, deemed paid or accrued to a foreign tax jurisdiction

— As the income (loss) of a U.S. taxpayer’s foreign branch is included in a taxpayer’s U.S. return as earned, a foreign branch’s inside basis differences generally result in deferred tax consequences in both the foreign and U.S. tax jurisdictions

— In such circumstances, the U.S. taxpayer includes the availability of unborn or anticipatory FTCs that will be generated when foreign income taxes are incurred (or forgone FTCs if a deferred tax asset exists)
US federal effect of foreign branch deferred taxes

— We believe entities generally should measure the U.S. federal effect using the lesser of the foreign tax rate or the U.S. rate
  - The U.S. deferred tax asset for an anticipated FTC or deferred tax liability for a forgone FTC is limited to the amount of FTCs that the U.S. parent would be able to utilize if the foreign branch reported taxable income sufficient to realize its deferred tax assets or settle its deferred tax liabilities
  - When more than one foreign branch exists, a weighted average foreign tax rate should be considered based upon the rates expected to apply in each foreign jurisdiction
— Companies may also measure the U.S. federal effect as the adjustment to the amount of FTCs that would be generated if the foreign branch realized its deferred tax assets and liabilities
  - The approach would not limit the deferred tax asset (liability) to the amount of FTCs expected to be utilized; instead, the U.S. deferred taxes would equal the amount of FTCs expected to be generated
— Under either approach, the U.S. parent must evaluate whether it is more likely than not that all or a portion of its deferred tax assets will not be realized
Recognizing forgone FTCs for a foreign branch example

Facts
— Company A, a U.S. entity, operates Branch B in a foreign jurisdiction
— Branch B has a 30% statutory tax rate and Company A has a 21% U.S. statutory tax rate
— During 20X1, Company A’s U.S. operations generated pretax book and taxable income of $250, and Branch B incurred pretax book and a taxable loss of $100
— Branch B’s 20X1 taxable loss resulted in a $100 net operating loss carryforward in the foreign jurisdiction and a $30 deferred tax asset, with no related valuation allowance
— During 20X2 Company A’s US operations and Branch B’s operations are expected to generate income of $250 and $400, respectively
— Branch B has the following amounts in 20X1 and expected in 20X2 in the foreign jurisdiction

<table>
<thead>
<tr>
<th></th>
<th>20X1</th>
<th>20X2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current tax expense (benefit)</td>
<td>-</td>
<td>90</td>
</tr>
<tr>
<td>Deferred tax expense (benefit)</td>
<td>(30)</td>
<td>30</td>
</tr>
<tr>
<td>Total income tax expense (benefit)</td>
<td>$(30)</td>
<td>$120</td>
</tr>
</tbody>
</table>
Recognizing forgone FTCs for a foreign branch example

— Company A would recognize the following current tax expense (benefit) in 20X1 and expected in 20X2, including the amount of FTCs that Company A expects to generate in 20X2 if the foreign deferred tax asset did not exist and the branch had incurred $120 of current tax expense (benefit)

<table>
<thead>
<tr>
<th></th>
<th>20X1 Actual</th>
<th>20X2 Forecast</th>
</tr>
</thead>
<tbody>
<tr>
<td>Branch pretax income (loss)</td>
<td>$(100)</td>
<td>$400</td>
</tr>
<tr>
<td>Company A pretax income (loss)</td>
<td>250</td>
<td>250</td>
</tr>
<tr>
<td>Taxable income (loss)</td>
<td>$150</td>
<td>$650</td>
</tr>
<tr>
<td>Current tax expense (benefit) before credits</td>
<td>$32</td>
<td>$137</td>
</tr>
<tr>
<td>FTC generated</td>
<td>-</td>
<td>(90)</td>
</tr>
<tr>
<td>FTC utilized</td>
<td>-</td>
<td>(63)</td>
</tr>
<tr>
<td>Current tax expense (benefit)</td>
<td>$32</td>
<td>$74</td>
</tr>
</tbody>
</table>

— Assume a valuation allowance would be required for the $27 of FTC carryforwards expected to exist at the end of 20X2
Recognizing forgone FTCs for a foreign branch example

— Lesser of approach

- Recognize a deferred tax liability of $21 because it is the lesser of $21 ($100 foreign net operating loss times the U.S. tax rate of 21%) and $30 ($100 foreign net operating loss times the foreign tax rate of 30%)

— Dollar for dollar approach

- Recognize a deferred tax liability of $30 (equal to the $30 foreign deferred tax asset)
Other tax reform considerations

— AMT credit carryforwards
  - Continue to assess the balance sheet classification to the extent AMT credit carryforwards are presented as income taxes receivable

— Deemed repatriation
  - Assess the balance sheet classification of remaining income taxes payable if electing to pay over the eight year period

— Foreign derived intangible income
  - We believe the foreign derived intangible income (FDII) deduction is akin to a special deduction because the amount is contingent on the future deemed tangible income return
Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income (OCI)

— Permits a reclassification from accumulated OCI to retained earnings for stranded tax effects resulting from the application of U.S. federal tax reform
  - The requirement to reflect the impact of the change in tax laws or rates directly to income tax expense (benefit) from continuing operations remains unchanged
  - Includes effects of the change in the U.S. federal income tax rate on the gross deferred tax amounts and related valuation allowances at the date of enactment (excludes the effect of the change on gross valuation allowances that were originally charged to continuing operations)
  - Companies also have the option to reclassify other income tax effects of the law
— Requires disclosure for all entities (including those that do not elect to reclassify) of the accounting policy for releasing income tax effects from accumulated OCI
— If an entity elects to reclassify, disclose a statement that an election was made to reclassify the income tax effects from accumulated OCI to retained earnings and a description of other income tax effects of the law change that are reclassified, if any
— If an entity elects to not reclassify, a statement to that effect is required to be disclosed
— Effective for all entities for years beginning after December 15, 2018 and interim periods within those years with early application permitted for any interim periods for which financial statements have not been issued or made available for issuance
— Retrospective or modified retrospective application

ASU 2018-02
Consideration of treasury guidance

— Entities should analyze the benefit of tax positions that it expects to report on a current or future tax return, taking into consideration the recognition and measurement guidance of ASC 740

— The analysis should be based on existing tax law, including existing interpretive guidance, as of the reporting date, even if a company anticipates a future change in tax law

— When evaluating whether to recognize a tax position, consider the following:
  - Changes in tax law must be accounted for in the period of enactment and cannot be anticipated
  - Administrative practices of the taxing authority, such as not challenging its own proposed regulations
  - There is a presumption that beneficial tax positions based on currently enacted tax law will be claimed, even if not reported on an originally filed tax return
Proposed ASU: Disclosure framework – Changes to the disclosure requirements for income taxes
Proposed ASU: Income taxes disclosures

The Board issued the amendments in the proposed update as part of its disclosure framework project

— The objective and primary focus of the project is to improve the effectiveness of disclosures required by U.S. GAAP in the notes to the financial statements by facilitating clear communication of information that is most important to financial statement users

— Separate projects on inventory, income taxes, fair value measurements and defined benefit pensions and other postretirement plans

The amendments in the proposed update would modify the current disclosure requirements for income taxes

— Replace the term public entity currently in ASC 740 with the term public business entity as defined in the Master Glossary of the Accounting Standards Codification
Proposed ASU: Income taxes disclosures

Additional Disclosure Requirements for All Entities

— The following additional disclosures would be required by ASC 740:

- Income (loss) from continuing operations before income tax expense (benefit) disaggregated between domestic and foreign*

- Income tax expense (benefit) from continuing operations disaggregated between federal or national, state and foreign*

- Income taxes paid disaggregated between federal or national, state and foreign

- Clarifies that the disclosure of income taxes paid is required for interim periods

* Disclosures currently required by SEC regulations
Proposed ASU: Income taxes disclosures

**Additional Disclosure Requirements for Public Business Entities**

— The following additional disclosures would be required by ASC 740:
  - An explanation of the year-to-year changes in rate reconciling items
  - The amount and explanation of the valuation allowance recognized and released during the reporting period
  - The amount of valuation allowance associated with deferred tax assets for federal or national, state and foreign carryforwards
  - The line items in the statement of financial position in which the unrecognized tax benefits are presented and the related amounts of such unrecognized tax benefits
  - The total amount of unrecognized tax benefits that offsets the deferred tax assets for carryforwards
Proposed ASU: Income taxes disclosures

Modification of Existing Disclosure Requirements for All Entities

— Current disclosures requirements would be modified by ASC 740 as follows:

- Eliminate the requirement for all entities to disclose the nature and estimate of the range of the reasonably possible change in the unrecognized benefits balance in the next 12 months or make a statement that an estimate of the range cannot be made

- Eliminate the requirement to disclose the amount of the taxable temporary difference associated with investments that are indefinitely reinvested

- Require entities other than public business entities to disclose the total amounts of federal or national, state, and foreign tax credit carryforwards, and the total amounts of other carryforwards (not tax effected), separately for those carryforwards that do not expire and those that do expire, along with the expiration dates (or a range of expiration dates)
Proposed ASU: Income taxes disclosures

Modification of Existing Disclosure Requirements for Public Business Entities

— Current disclosures requirements would be modified by ASC 740 as follows:

- Separate disclosure for any reconciling item that amounts to more than five percent of the amount computed by multiplying the income before tax by the applicable statutory federal income tax rate

- Amounts of deferred tax assets for federal or national, state and foreign carryforwards (tax effected) before the valuation allowance and further disaggregate such amounts by time period of expiration for each of the first five years after the reporting date and a total for any remaining years, and a total for indefinite carryforwards

* Disclosures currently required by SEC regulations
Proposed ASU: Income taxes disclosures

**Effective Date and Transition**

— An entity would apply the proposed changes prospectively
— Early application is under consideration and may or may not be permitted
— The effective date of the amendments will be determined after stakeholder feedback on the proposed amendments is considered
— Comments are due by May 31, 2019
Proposed ASU: Income taxes disclosures

**Reporting and Disclosure**

— If and when a final ASU is issued, disclosure is required of the impact that recently issued accounting standards will have on the financial statements of the Registrant when adopted in a future period (SAB 74)

| Brief description of the new standard, the date adoption is required and the date the registrant plans to adopt (if earlier application is permitted) | Discussion that adoption of the standard is applied on a prospective basis | Disclosure of the potential impact of other significant matters that the Registrant believes might result from the adoption of the standard |
Forthcoming proposed ASU on simplifications to accounting for income taxes
Proposed simplifications to accounting for income taxes

The FASB Board tentatively decided to remove the following exceptions:

— Exception to the incremental approach for intraperiod tax allocation when there is a loss from continuing operations and income outside of continuing operations

— Exception to the requirement to recognize a deferred tax liability for equity method investments when a foreign subsidiary becomes an equity method investment (modified retrospective application)

— Exception to the ability not to recognize a deferred tax liability for a foreign subsidiary when a foreign equity method investment becomes a subsidiary (modified retrospective application)

— Exception to the general methodology for calculating income taxes in an interim period when a year-to-date loss exceeds the anticipated loss for the year
Proposed simplifications to accounting for income taxes

The FASB Board also decided the following:

— An entity should recognize a franchise tax that is partially based on income in accordance with ASC 740 and account for any incremental amount as a non-income based tax (retrospective application)

— An entity should evaluate when a step-up in the tax basis of goodwill should be considered part of the initial recognition of book goodwill and when it should be considered a separate transaction

— An entity should be permitted to forgo the allocation of consolidated current and deferred tax expense to legal entities that are not subject to tax in separate company financial statements (retrospective application)

— An entity should reflect the effect of an enacted change in tax laws or rates in the annual effective tax rate computation in the interim period that includes the enactment date
SEC comments on cross-border income tax matters
Areas of common questions

— Valuation allowance
  - Reasons for the lack of a valuation allowance when a cumulative loss exists, including the analysis of evidence and the extent to which the evidence is objectively verifiable
  - Additional detail as to why a valuation allowance exists when the entity does not have a three year cumulative loss
  - Additional detail as to why a valuation allowance was partially released due to tax law change

— Effective tax rate
  - Reasons on why an entity is reconciling to a rate different from the statutory rate of the parent company’s country of domicile
  - Additional detail on why adjustments of prior years reflected within the rate reconciliation are considered changes in estimates as opposed to corrections of errors
  - Detail as to whether material items within the rate reconciliation are recurring or non-recurring
  - Further insight on the rate reconciling items included within the effect of foreign operations line of the rate reconciliation

SEC comments on income taxes
SEC comments on income taxes

Areas of common questions

— Investments in subsidiaries
  - Reasons for the ability to assert indefinite reinvestment when a history of domestic losses and distributions exists
  - Additional detail as to why a deferred tax liability exists when an entity asserts it is indefinitely reinvested and why it is not practicable to determine the unrecognized deferred tax liability
  - Detail as to whether a change in judgment was reflected in the appropriate period and if the measurement of the liability was accurate

— Unrecognized tax benefits
  - Reasons as to why an unrecognized tax benefit exists even though the tax position is more likely than not of being realized
  - Additional detail as to why no current year layer of unrecognized tax benefits exists when the issue is continuously reflected in the same manner on the return
  - Reasons why the required disclosures related to unrecognized tax benefits are omitted
SEC comments on income taxes

Areas of common questions

— Omitted disclosures
  - Domestic and foreign components of income (loss) from continuing operations
  - Amounts and expiration dates of net operating loss carryforwards
  - Unrecognized deferred tax liability on indefinitely reinvested earnings, or a statement that it is not practicable to determine
  - Per share effects of tax holiday

— Tax Reform
  - Reasons why no liability for transition tax was recognized as a result of tax reform
Questions
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