



New Developments Summary

Modifications to uncertain tax position guidance

FASB provides implementation guidance and eliminates certain disclosures for nonpublic entities

Summary

In September 2009, the FASB issued Accounting Standards Update (ASU) 2009-06, *Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities*, which modifies the guidance on uncertain tax positions in *FASB Accounting Standards Codification™* (ASC or Codification) 740, *Income Taxes* (formerly FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes*), as follows:

- Provides implementation guidance that is applicable for all entities
- Amends the disclosure requirements for nonpublic entities by eliminating the requirements for certain disclosures

This bulletin discusses those amendments, including a revised definition of “tax position” in the Codification, as well as examples that illustrate whether entities should attribute income tax to the entity or to its owners and the applicability of uncertain tax position guidance to consolidated or combined financial statements.

The amendments are effective for interim and annual periods ending after September 15, 2009 for entities that previously adopted the uncertain tax position guidance in ASC 740. For all other entities, the amendments are effective for annual financial statements for fiscal years beginning after December 15, 2008.

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A. Introduction

In September 2009, the FASB issued Accounting Standards Update (ASU) 2009-06, *Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities*, to amend the existing guidance in *FASB Accounting Standards Codification*[™] (ASC or Codification) 740, *Income Taxes*, which was formerly included in FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes* (Interpretation 48).

ASU 2009-06 provides implementation guidance, primarily through the use of examples, in accounting for uncertain tax positions for pass-through entities and tax-exempt not-for-profit entities, and it eliminates certain disclosure requirements relating to uncertain tax positions for nonpublic entities.

In particular, the ASU

- Expands the definition of a “tax position” in the Codification Glossary and includes illustrative examples that help clarify the revisions
- Includes examples to help entities determine whether to attribute income tax to the entity or to its owners
- Provides an example that demonstrates how a reporting entity must account for the tax positions of all entities within a related group, regardless of the tax status of the reporting entity

B. Background

The FASB had broadly addressed the accounting for uncertainty in income taxes in June 2006 through the issuance of Interpretation 48, which was initially effective for fiscal years beginning after December 15, 2006. In February 2008, the FASB deferred the effective date of that guidance to fiscal years beginning after December 15, 2007 to provide certain nonpublic entities additional implementation time.

In December 2008, the FASB once again deferred the effective date for nonpublic entities to fiscal years beginning after December 15, 2008. The second deferral allowed the FASB time to develop certain guidance included in ASU 2009-06 that addresses the application of ASC 740 for pass-through entities and tax-exempt not-for-profit entities.

C. Definition of a tax position

ASU 2009-06 revises the definition of a “tax position” in the ASC Glossary to clarify that an entity’s status, including its status as a pass-through entity or as a tax-exempt not-for-profit entity, is considered a tax position. The amendments also clarify that the guidance on accounting for uncertain tax positions applies to all entities, including tax-exempt not-for-profit entities, pass-through entities, and entities that are taxed similarly as pass-through entities, such as real estate investment trusts and registered investment companies.

ASU 2009-06 also provides several examples to assist in clarifying the modified definition of a tax position. The examples included in ASC 740-10-55-223 through 55-225 specifically address the following scenarios:

- The decision relating to whether or not an entity files or does not file an income tax return in a jurisdiction is a tax position subject to the guidance on uncertain tax positions in ASC 740

- An S corporation, which previously converted from a C corporation that disposed of assets subject to the built-in gains tax may consider the following tax positions, among others:
 - If other assets previously disposed of were subject to the built-in gains tax
 - If income related to the built-in gains tax is correct
 - If the tax basis associated with the assets is correct
 - The tax status of the S corporation
 - A tax-exempt not-for-profit entity with transactions that might be subject to unrelated business income tax must consider tax positions including, but not limited to, the following:
 - Characterization of activities as related or unrelated to its exempt purpose
 - Allocation of revenue and expenses between tax-exempt activities vs. unrelated business income activities
 - If it qualifies as a tax-exempt entity, regardless of whether it is subject to income tax on unrelated business income
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D. Attribution of income taxes to the entity or its owners

Constituents have raised questions about determining whether an entity or its owners are responsible for certain income taxes associated with a pass-through entity, which reflects the varying methods that jurisdictions use in assessing and collecting income taxes. For instance, some jurisdictions tax the entity directly while others tax the owners directly, but allow (1) the entity to remit the income tax on behalf of the owners and (2) the owner to claim the income tax refund under certain conditions. This distinction will help to determine if a tax payment is an income tax expense of the entity, subject to the provisions of ASC 740 or if the payment is a transaction with the owners, which falls outside the scope of ASC 740.

ASU 2009-06 provides guidance, primarily in the form of examples, as illustrated in ASC 740-10-55-226 through 55-228, to help entities in determining whether to attribute income tax to the entity or its owners. The illustrations indicate that an entity should make this determination based on the laws and regulations of the taxing jurisdiction rather than on who pays the income tax. Further, the examples imply that any agreements between an entity and its owners to settle who will pay income taxes to the tax authorities are deemed irrelevant for purposes of determining whether income tax is attributable to the entity or its owners. The examples also show that if the entity pays income taxes attributable to the entity's owners, the transaction should be accounted for as a transaction with owners rather than as a component of income taxes.

Given the variation in local tax laws, determining whether an income tax for a particular jurisdiction is attributable to the entity or to its owners may require the use of a tax specialist. As a result, nonpublic entities should consider if their particular facts and circumstances warrant the use of a tax specialist as they prepare to implement the uncertain tax position guidance of ASC 740.

E. Application to consolidated or combined financial statements

Questions were also raised by constituents on how to apply the uncertain tax position guidance in ASC 740 to consolidated or combined financial statements, including situations in which a pass-through entity is either the parent or a member of the consolidated or combined financial statements.

ASU 2009-06 includes an example that demonstrates how a reporting entity must account for the tax positions of all entities within a related group of entities, regardless of the tax status of the reporting entity (parent company), even if it is a pass-through entity. For instance, if a partnership consolidates a C corporation, the partnership should include the corporation's assets, liabilities, income, and expenses in the consolidated financial statements as if it were a single economic entity, while also accounting for the tax positions related the C corporation.

F. Disclosure relief for nonpublic entities

ASU 2009-06 amends the nonpublic entity disclosure requirements for uncertain tax positions in ASC 740, by eliminating the tabular reconciliation disclosure of unrecognized tax benefits and the requirement to disclose the total amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate. The FASB eliminated these disclosures because they were not considered to be useful to users of nonpublic company financial statements.

The table below shows a comparison of the amended disclosure requirements for nonpublic entities versus public entities.

| Uncertain tax position disclosure | Nonpublic entity | Public entity |
|---|------------------|---------------|
| <p>A tabular reconciliation of the beginning and ending balances of unrecognized tax benefits, including the following reconciling items:</p> <ul style="list-style-type: none"> ▪ Gross amount of increases in unrecognized tax benefits resulting from <ul style="list-style-type: none"> – Current-period tax positions – Prior-period tax positions ▪ Gross amount of decreases in unrecognized tax benefits resulting from <ul style="list-style-type: none"> – Current-period tax positions – Prior-period tax positions ▪ Decreases in unrecognized tax benefits resulting from <ul style="list-style-type: none"> – Settlements with taxing authorities – Lapses in applicable statute of limitations | Not required | Required |

| Uncertain tax position disclosure | Nonpublic entity | Public entity |
|---|-------------------------|----------------------|
| Information concerning tax positions for which a material change in the unrecognized tax benefit liability is reasonably possible in the next 12 months | Required | Required |
| The total amount of unrecognized tax benefits which, if recognized, would impact the effective tax rate | Not required | Required |
| The total amount of interest and penalties recognized in the income statement and in the balance sheet | Required | Required |
| Open tax years by major jurisdiction | Required | Required |

G. Effective date

For entities that previously adopted the uncertain tax position guidance in ASC 740, the guidance in ASU 2009-06 is effective for interim and annual periods ending after September 15, 2009 (interim periods ending September 30, 2009 for public companies with a calendar year-end). For nonpublic entities that elected to defer the application of the uncertain tax position guidance in ASC 740 in accordance with ASC 740-10-65-1(e) (formerly FASB Staff Position FIN 48-3, "Effective Date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises"), the guidance in ASU 2009-06 is effective upon adoption of the uncertain tax position guidance in ASC 740. ASC 740-10-65-1 requires entities that elected deferral to adopt the uncertain tax position guidance for annual financial statements for fiscal years beginning after December 15, 2008. ASU 2009-06 does not change the effective dates for the application of the uncertain tax position guidance in ASC 740.

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