

# Tax Flash

New federal tax developments  
from Grant Thornton's National Tax Office

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## IRS announces intention to require disclosure of uncertain tax positions (FIN 48) on tax returns

The IRS announced on Jan. 26, 2010, (Announcement 2010-9) that it is developing a new tax return schedule to require many business taxpayers to report “uncertain tax positions” on their returns.

The Announcement impacts IRS policy with respect to the disclosure of uncertain tax positions on federal tax returns. Under the Announcement, an uncertain tax position is defined as a position for which a tax “reserve” must be established under FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109* (FIN 48), which has been incorporated into Topic 740 of the Accounting Standards Codification (ASC 740).

The new requirements would apply to business taxpayers who have over \$10 million in assets and are required to identify and quantify uncertain tax positions under ASC 740 “or other accounting standards relating to uncertain tax positions involving United States federal income tax.” All business taxpayers with assets over \$10 million are under the

jurisdiction of the IRS’s Large and Mid-Size Business (LMSB) division.

The proposed schedule would be filed with the Form 1120 or other business tax returns. The IRS described the proposed disclosures as “concise descriptions” of each uncertain tax position along with the maximum amount of a taxpayer’s potential tax exposure attributable to each uncertain tax position if the position was disallowed in its entirety on audit. The proposal would not require taxpayers to disclose their risk assessment or tax reserve amounts.

In addition to those positions for which there are differences between a tax position taken in a return and amounts recognized in the financial statements under ASC 740, the Announcement provides that uncertain positions also include any position related to the determination of any U.S. federal income tax liability for which the taxpayer or a related entity has not recorded a reserve because the taxpayer either expects to litigate the position or has determined that the IRS has a general administrative practice not to examine the issue.

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Specifically, the schedule would require taxpayers to include a concise description of each uncertain tax position so that the IRS can determine the nature of the issue. This would include the following:

- The rationale for the position and a concise general statement of the reasons for determining that the position is an uncertain tax position
- The entire amount of U.S. federal income tax that would be due if the position were disallowed in its entirety on audit (This amount is the maximum tax adjustment for the position reflecting all changes to items of income, gain, loss, deduction or credit if the position is not sustained.)
- The Code sections potentially implicated by the position
- A description of the taxable year or years to which the position relates
- Whether the position involves an item of income, gain, loss, deduction or credit against tax
- Whether the position involves a permanent inclusion or exclusion of any item, the timing of that item or both
- Whether the position involves a determination of the value of any property or right
- Whether the position involves a computation of basis

### Potential implications

The proposal impacts the IRS's long-standing policy of restraint in requesting taxpayer tax accrual workpapers.

The policy was last addressed in 2002, when the IRS announced that it would consider asking for tax accrual workpapers for returns that include certain "listed"

transactions that the IRS identified as abusive. Since then, the IRS has consistently signaled through litigation, regulation and public statements its desire and intention to seek increased transparency in tax reporting. Regulatory and policy change on matters such as increased return preparer standards and reportable transactions evidence the IRS's focus on transparency.

The policy change may impact the extent to which businesses must document positions for financial and tax purposes. It likely will mean increased IRS examination scrutiny of tax positions, including increased demands for position documentation. The IRS's main focus is FIN 48, but the Announcement also targets businesses not subject to FIN 48, "who may be subject to other requirements regarding accounting for uncertain tax positions," such as U.S. GAAP or International Financial Reporting Standards (IFRS) or country-specific generally accepted accounting standards.

The IRS's focus on accounting standards coupled with existing tax position disclosure regimes, such as reportable transaction disclosure requirements and increased tax return preparer standards, suggests that "abusive transactions" are not the driving force behind the policy change. It remains to be seen, but the Announcement suggests businesses may anticipate even greater focus on traditionally intensive examination items such as transfer pricing, research tax credit, issues of capitalization versus expense and generally those technical matters falling under the IRS's issue management focus for Tiered Issues.

The IRS has indicated that focusing on uncertain tax positions will enable it to identify issues of particular interest or significant magnitude more quickly and efficiently. The IRS may view increased disclosure requirements as providing increased incentive for businesses to participate in its various early issue resolution programs, with a focus on increasing currency in the examination cycle.

Besides the new required disclosures, the IRS indicated that it would otherwise retain the existing policy of restraint in requesting tax accrual workpapers. However, without further detail surrounding the IRS's disclosure proposal, it is unclear at this time what that means.

The IRS said in its announcement that it intends to publish the new schedule as quickly as possible. The IRS invited public comments to be submitted on the proposal by March 29, 2010.

**The IRS has not set a definite date for the release or effective date of the schedule.**

The IRS also is currently evaluating options for penalties that could be imposed for taxpayers that fail to make adequate disclosures, but has indicated that that legislation may be required for any such penalties.

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Grant Thornton anticipates that businesses will be concerned about practical and strategic impacts of the policy change on both tax and financial reporting obligations. Evaluation of issues under the Announcement will require strong

recognition and understanding of applicable financial accounting and tax standards.

Regulatory changes, such as increased tax return preparer standards and the implementation of Sarbanes-Oxley in recent years, are reminders that tax and financial regulation and related policies change. Grant Thornton looks forward to assisting businesses address the meaning and impact of the proposed policy on both tax and financial reporting matters.

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