



FAF Releases Post-Implementation Review Report on FIN 48

The Financial Accounting Foundation (FAF) reported in its first formal post-implementation review report that FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48) (codified in Accounting Standards Codification Topic 740, *Income Taxes*) generally meets its goal of increasing the relevance and comparability in reporting information about tax uncertainties.¹

Background on FAF and Process

The FAF, which oversees the FASB and Governmental Accounting Standards Board (GASB), established the post-implementation review process to review the development and implementation of selected FASB and GASB accounting standards. The primary objectives of a post-implementation review are to (1) determine whether a standard is accomplishing its stated purpose, (2) evaluate the implementation of a standard and continuing compliance costs and related benefits, and (3) provide recommendations to improve the standard-setting process (as opposed to recommending standard-setting actions). The first objective is divided further to determine whether:

- The standard resolved the issues underlying its need;
- Decision-useful information is being reported to, and being used by, financial statement users;
- The standard is operational;
- Significant unexpected changes to financial reporting and operating practices have occurred; and
- Significant economic consequences have occurred that the Board had not considered before issuing the standard.

The procedures include reviewing FASB historical files, conducting stakeholder surveys and questionnaires, reviewing academic publications, reviewing footnote disclosures and other public information for selected public companies, and interviewing stakeholders.

The post-implementation review process is independent of the standard-setting processes of the FASB and GASB and was created to provide real-world feedback and analysis of standards. The FAF review staff reports to the trustees and FAF president, not to the FASB. Input from investors and other financial statement users, preparers, accounting practitioners, academics, and financial regulators was obtained by the staff in arriving at its final assessments in the FIN 48 review.

¹ Post-Implementation Review Report On FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, available at www.accountingfoundation.org.

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Results of FIN 48 Post-Implementation Review

Observations from the FAF's FIN 48 post-implementation review team highlighted that:

- More information about income tax uncertainties is reported using FIN 48's provisions than using prior accounting guidance. Investors are using that information in different ways, including to predict income tax cash flows and to assess how aggressive managements are in their income tax strategies.
- Uncertain income tax positions are recognized and measured more consistently using FIN 48's guidance than using prior accounting guidance. However, the post-implementation review team reported that consistently applying FIN 48's guidance may not increase the comparability of information about income tax uncertainties across companies because managements' judgments may differ and due to tax code complexity.
- Reported information about income tax uncertainties is more relevant since FIN 48 was issued. However, the post-implementation review team reported that such information may not be predictive of future cash flows because FIN 48 employs a benefit-recognition approach (recognizes benefits only when they are more likely than not to be sustained based on the technical merits and measures those benefits recognized as the greatest amount more than 50% likely to be realized).
- On balance, the benefits of FIN 48's improved consistency and reporting of income tax uncertainty information outweigh its costs.

The report also provided a summary of stakeholder comments on FIN 48's effectiveness, which were made in response to the following questions:

- **Does FIN 48 Provide Decision-Useful Information?** Investors and other financial statement users believe FIN 48 generally provides useful information and public companies have increased the amount of information provided about income tax uncertainties. Preparers said, however, that they are concerned that the judgments involved in accounting for income tax uncertainties result in information that is not comparable, and may not represent amounts expected to be paid.
- **Does FIN 48 Work in Practice?** While preparers generally understand FIN 48's provisions and are able to apply them, they said that difficulties arise in making judgments about outcomes applied to complex, and often vague, tax codes and practices.
- **Did FIN 48 Result in Unexpected Changes in Practice?** As expected, preparers and practitioners said that they changed some operating practices to implement FIN 48. The most common changes were employing additional tax specialists, engaging tax advisors, and changing the level of coordination between tax and other functions. Relatively few preparers said that they changed their tax strategies for FIN 48 reasons.

- **Did FIN 48 Result in Significant Implementation Costs?** Most preparers said that they did not incur significant FIN 48 implementation and continuing compliance costs. However, some preparers, particularly those from smaller organizations, said they incurred significant costs such as additional audit fees, fees of external legal and accounting experts, and costs of documenting existing tax positions.
- **Did FIN 48 Result in Any Significant Economic Consequences?** Preparers said that they did not experience any significant capital market effects or effects on entity valuations attributable to FIN 48's implementation and disclosures. Users said that they did not perceive any significant capital market effects, or effects on entities' valuations attributable to FIN 48.

Next Steps

The post-implementation review report also provides the FASB with recommendations to continue its efforts to improve user input in the agenda and early deliberation phases to evaluate alternatives addressing user needs of applicable standards. The report also recommends that the FASB include in each standard (1) a thorough discussion about the need for new financial reporting guidance; (2) the benchmark characteristics of useful financial information considered; and (3) a thorough discussion about the benefits and beneficiaries of the new guidance, the associated costs to affected principal stakeholders, and how benefits and costs are evaluated and assessed. The report also encourages the FASB to consistently follow its established policies and procedures related to re-exposing all or part of a proposed standard.

Based on the results of the report, the FASB will prepare and submit a written response to the FAF findings.

Although judgments around complex issues may result in different conclusions in some instances, as noted by the post-implementation review team, we believe that the principles and recognition and measurement thresholds established in FIN 48 provide a consistent framework for evaluating uncertain tax positions, which substantially increases the likelihood of consistent reporting of similar transactions.

The FAF plans to perform more post-implementation reviews of accounting standards in the future. The topics of those reviews have not yet been publicly identified.

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