

## **SEC Issues Staff Guidance on Accounting and Reporting Impacts of the Recently-Enacted Tax Cuts and Jobs Act**

Recently, the U.S. Securities and Exchange Commission ("SEC") announced that the staff of the Office of the Chief Accountant issued Staff Accounting Bulletin No. 118 ("SAB 118"), which provides guidance for publicly traded companies, auditors, and others to help ensure timely public disclosures of the accounting impacts of the Tax Cuts and Jobs Act (the "Tax Act") signed into law on December 22, 2017. The SEC also announced that the Division of Corporation Finance issued Compliance and Disclosure Interpretation 110.02 ("C&DI 110.02"), which expresses views of the staff regarding the applicability of Item 2.06 of Form 8-K with respect to reporting the impact of a change in tax rate or tax laws pursuant to the Tax Act.

### **SAB 118**

While Financial Accounting Standards Board Accounting Standards Codification Topic 740, *Income Taxes* ("ASC 740") addresses the recognition of deferred tax liabilities and deferred tax assets for future tax consequences in certain circumstances and accounting for income taxes for certain changes in tax law or tax rates, ASC 740 does not address circumstances that may arise for some public companies in accounting for the income tax effects of the Tax Act. The SEC staff issued SAB 118 "to address situations where the accounting under ASC Topic 740 is incomplete for certain income tax effects of the Tax Act upon issuance of an entity's financial statements for the reporting period in which the Tax Act was enacted." In particular, SAB 118 sets forth the staff's views on the application of ASC 740 in the annual or quarterly reporting period that includes December 22, 2017, which is the date the Tax Act was signed into law.

SAB 118 establishes a three-part procedure for companies to follow when accounting and reporting the income tax effects of the Tax Act in financial statements that include a reporting period in which the Tax Act was enacted:

1. Reflect the income tax effects of the Tax Act in which the accounting under ASC 740 is complete on a non-provisional basis;
2. Report provisional amounts for those specific income tax effects of the Tax Act for which the accounting under ASC 740 is incomplete but a reasonable estimate can be determined; and
3. Continue to apply ASC 740 based on the provisions of the tax laws that were in effect immediately prior to the enactment of the Tax Act for any specific income tax effects of the Tax Act for which a reasonable estimate cannot be determined.

When a company is unable to determine a reasonable estimate for any income tax effects, it must report provisional amounts in the first reporting period in which a reasonable estimate can be determined. SAB 118 provides a number of examples of how its guidance should be applied.

SAB 118 uses the concept of a "measurement period" that begins in the reporting period that includes the Tax Act's December 22, 2017 enactment date and ends when an entity has

obtained, prepared and analyzed the information that is needed in order to complete the accounting requirements under ASC 740. SAB 118 recognizes that during the measurement period, an entity may need to make changes in subsequent reporting periods based on facts and circumstances that existed when the Tax Act was enacted and that, if known, would have affected the income tax effects initially reported as provisional amounts. However, income tax effects of events unrelated to the Tax Act should not be reported as measurement period adjustments. Any provisional amounts or adjustments to provisional amounts included in a registrant's financial statements during the measurement period should be included in income from continuing operations as an adjustment to tax expense or benefit in the reporting period the amounts are determined. The staff stated that under no circumstances should the measurement period extend beyond one year from the enactment date.

SAB 118 specifies that financial statement disclosures should provide information about the material financial reporting impacts of the Tax Act for which the accounting under ASC 740 is incomplete, including:

- Qualitative disclosures of the income tax effects of the Tax Act for which the accounting is incomplete;
- Disclosures of items reported as provisional amounts;
- Disclosures of existing current or deferred tax amounts for which the income tax effects of the Tax Act have not been completed;
- The reason why the initial accounting is incomplete;
- The additional information that is needed to be obtained, prepared, or analyzed in order to complete the accounting requirements under ASC 740;
- The nature and amount of any measurement period adjustments recognized during the reporting period;
- The effect of measurement period adjustments on the effective tax rate; and
- When the accounting for the income tax effects of the Tax Act has been completed.

### **C&DI 110.02**

*Item 2.06 of Form 8-K requires the filing of a current report on Form 8-K "[i]f the registrant's board of directors, a committee of the board of directors or the officer or officers of the registrant authorized to take such action if board action is not required, concludes that a material charge for impairment to one or more of its assets, including, without limitation, impairments of securities or goodwill, is required under generally accepted accounting principles applicable to the registrant."*

C&DI 110.02 clarifies that the re-measurement of a deferred tax asset to incorporate the effects of the Tax Act does not in-and-of-itself trigger an obligation to file under Item 2.06 of Form 8-K because such re-measurement does not constitute an impairment under ASC 740. However, the enactment of new tax rates or tax laws could have implications for a registrant's financial statements, including whether it is more likely than not that the DTA will be realized. C&DI 110.02 clarifies that if a company employing the "measurement period" approach of SAB 118 (as discussed above) concludes that an impairment has occurred due to changes resulting from

the enactment of the Tax Act, the registrant may rely on the Instruction to Item 2.06 and disclose the impairment, or a provisional amount with respect to that possible impairment, in its next periodic report.

### **Practical Considerations**

For reporting periods within their measurement period, companies should consult with their accountants and other advisors to determine the extent to which they either a) know specific income tax effects of the Tax Act; b) are able to make reasonable estimates of specific income tax effects of the Tax Act; or c) are not able to know or make reasonable estimates for specific income tax effects of the Tax Act. Based on this information, companies should prepare their financial statements in accordance with SAB 118, including the narrative explanations necessary to provide information about the material financial reporting impacts of the Tax Act.

While developing language to explain the extent to which their reports contain provisional estimates and the extent to which there was not sufficient information upon which to make reasonable estimates, companies may want to expressly raise the possibility that adjustments may be needed in subsequent financial statements once further information becomes available.

Companies should also consider their approach for disclosing information about the accounting impact of the Tax Act before the filing of their financial statements with the SEC. For example, some companies may find it appropriate to include a discussion of the accounting issues under the Tax Act in their earnings releases in order to enhance the understanding of the results being presented.

Finally, companies considering disclosing information in addition to that required by ASC 740 and SAB 118 should consider whether such information is a non-GAAP financial measure triggering the requirements of Item 10(e) of Regulation S-K and/or Regulation G, as applicable.

Full details of SAB 118 can be found at: [www.sec.gov/interps/account/staff-accounting-bulletin-118.htm](http://www.sec.gov/interps/account/staff-accounting-bulletin-118.htm).

Full details of C&DI 110.02 are available at: [www.sec.gov/divisions/corpfin/guidance/8-kinterp.htm#110.02](http://www.sec.gov/divisions/corpfin/guidance/8-kinterp.htm#110.02)

### **For More Information**

Clients should contact their engagement team to discuss these new releases, while friends of the firm and others can contact any member of the PKF Texas SEC Group or visit the website at [www.PKFTexas.com/SECDesk](http://www.PKFTexas.com/SECDesk).