WILLKIE FARR & GALLAGHER LLP

CLIENT ALERT

SEC Provides Reporting Guidance for Recent U.S. Tax Reform

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On December 22, 2017, the day the Tax Cuts and Jobs Act (the "Tax Cuts Act") was signed into law, the SEC staff issued two important interpretations regarding accounting for the tax impact of the Act and related disclosure:

- Staff Accounting Bulletin No. 118 ("SAB 118")[1] provides guidance regarding accounting for the income tax effects of the Tax Cuts Act, including, for example, its impact on deferred tax assets and liabilities.[2]
- New Compliance and Disclosure Interpretation ("CD&I") 110.02[3] clarifies that the re-measurement of a deferred tax asset due to the changes under the Tax Cuts Act is not an impairment requiring filing under Item 2.06 of Form 8-K.

SAB 118

SAB 118 provides three categories depending on the status of a company's assessment of the financial statement impact of the Tax Cuts Act for the reporting period that includes December 22, 2017:

1 Available here.

2 Changes under the Tax Cuts Act that may materially impact an issuer's financial statements include the re-measurement of deferred tax assets due to the significantly reduced corporate income tax rate of 21%, liabilities for taxes due on foreign earnings that are now mandatorily repatriated and reassessments of various valuation allowances.

3 Available here.

- If the company has completed its assessment under Accounting Standards Codification ("ASC") Topic 740, *Income Taxes*, such impact must be reflected in the financial statements that include December 22, 2017.
- If it has not completed its assessment but is able to determine a "reasonable estimate" of the effects, the financial statements should reflect that amount, which should be identified as a "provisional amount" (to the extent the accounting for the tax effects is incomplete). This amount would then be subject to adjustment during a measurement period ending no later than December 22, 2018.
- If, however, it cannot determine a reasonable estimate of the impact, the financial statements should continue to reflect the provisions before the changes made by the Tax Cuts Act. The company would then reassess the impact each subsequent reporting period.

To the extent the financial reporting impact of the Tax Cuts Act required under ASC Topic 740 is incomplete, additional disclosures are required, including:

- qualitative disclosures of the income tax effects of the Tax Cuts 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 Cuts Act have not been completed;
- the reason why the initial accounting is incomplete;
- the additional information needed to be obtained, prepared or analyzed in order to complete the accounting requirements under ASC Topic 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 Cuts Act has been completed.

CD&I 110.02

Many issuers carry on their balance sheet a deferred tax asset that will need to be revalued based on the new, lower corporate tax rate. New CD&I 110.02 clarifies that the re-measurement of this asset is not considered an impairment under ASC Topic 740, and thus does not need to be reported under Item 2.06 of Form 8-K. Issuers may then rely on the instruction to Item 2.06 and disclose the impairment in their next SEC periodic report.

Other Considerations

In preparing their Management's Discussion and Analysis ("MD&A") disclosure in their upcoming annual reports on Form 10-K, companies must evaluate and discuss the impact of the Tax Cuts Act, to the extent material, with respect to the just completed fiscal year as well as its impact on future periods as a "known trend." Companies should also be careful that any disclosures concerning the impact comply with Regulation FD regarding selective disclosure, and make sure to furnish, under Item 2.02 of Form 8-K, any material disclosures of these tax effects for the completed period. Companies should also consider whether they need to make any changes to their internal control over financial reporting in light of this significant tax reform.

If you have any questions regarding this client alert, please contact the following attorney or the attorney with whom you regularly work.

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