2017 Accounting for Tax Reform
GAAP Basis

Presenters

Allan Autry
Principal, CPA
Johnson Lambert LLP

Sarah Stubbs, CPA
Principal
Johnson Lambert LLP

Agenda

- Effect on Current Taxes
- Effect on Deferred Taxes
- Stranded Tax in AOCI
- December 22-31 Significant Transactions
- Financial Statement Presentation
- Footnote Disclosures
- Final Thoughts

Effect on Current Taxes

- 2017 current tax still determined at 34% or 35%
- Include your prior year true-up, if any

Taxable income =	$300,000
Tax rate	34%
2017 tax	$102,000

Current tax incurred	$102,000	
Income taxes payable		$102,000

JOHNSON LAMBERT

Effect on Deferred Taxes

For the purpose of discussion, let’s assume:

	2017	Change	Change at 34%
DTA #1	$400,000	$200,000	68,000
UNR Loss	150,000	50,000	17,000
Net	550,000	250,000	85,000

JOHNSON LAMBERT

Effect on Deferred Taxes

The usual adjusting journal entries:

Deferred tax asset	$68,000	
Change in deferred income tax		$68,000
Deferred tax asset	$17,000	
Unrealized loss through OCI		$17,000

JOHNSON LAMBERT

Effect on Deferred Taxes

Next, let's consider the effect of tax reform

Dec. 31	Net DTA at 34%	187,000
Dec. 31	Net DTA at <u>21%</u>	<u>115,500</u>
Difference (Net DTA at 13%)		71,500

Change in deferred income tax	$71,500	
Deferred tax asset		$71,500

JOHNSON LAMBERT

Stranded Tax in AOCI

- We have now created a mismatch!
  - Entire impact of applying the 21% rate hit the income statement – including the unrealized DTA
- Net unrealized sitting in AOCI at 66%
- But shouldn't it be at 79% under tax reform?

JOHNSON LAMBERT

Stranded Tax in AOCI

- FASB issued an exposure draft on January 18
  - Intent is to patch, not change, existing rules
  - Would allow a reclass of the difference within AOCI
    - Will not appear in statement of OCI
    - Will appear on statement of change in equity
  - Expected to issue after their February 7 meeting
  - Cannot adopt until FASB issues the ASU

- If financials issued before the ASU, expect to apply the reclass in 2018

Dec. 22-31 Significant Transactions

- Why is this time period of concern?
  - December 22 = tax reform enactment date

- Technically, ASC 740-10-35-4 requires the effect of changes in tax laws and rates to be recognized as of the date of enactment
  - Determine DTA(L) and income taxes incurred as just described at 12/22/17
  - Then, period from Dec. 22-31 subject to “familiar” GAAP rules

Dec. 22-31 Significant Transactions

- Realistic view – unless you have a significant transaction, just determine the effect of tax reform as of December 31

- What constitutes a significant transaction?
  - Acquisition of a company
  - Acquisition of significant fixed assets
  - Significant change in investment portfolio
  - Novation agreement/LPT
  - Other significant transactions?

Financial Statement Presentation

- Income statement
  - One line for “Income tax expense (benefit)”
- Comprehensive income statement
  - Unrealized position net of 34% or 35%
- Tax reform effect is not obvious here
- FASB ASU will not change these statements

JOHNSON LAMBERT

Financial Statement Presentation

- Balance sheet
  - Net deferred tax asset or liability at 21%
  - AOCI reported net of 34% or 35% tax rate
- Statement of changes in equity
  - Only affected in 2017 if ASU is issued
  - Add in a line to reclass the stranded (excess) tax from AOCI to RE

- FASB ASU will change these statements

Footnote Disclosures

- Components of income taxes incurred
  - Current income tax incurred
  - Change in deferred income tax
  - Impact of legislative rate change

- Effect of legislative rate change must be disclosed somewhere in the financials

AICPA Example Disclosures

- Illustrative Disclosure – Subsequent Event
  - The Tax Cuts and Jobs Act of 2017 was signed into law on December 22, 2017. The law includes significant changes to the U.S. corporate income tax system, including a Federal corporate rate reduction from 35% to 21%, limitations on the deductibility of interest expense and executive compensation, and the transition of U.S. international taxation from a worldwide tax system to a territorial tax system. We are in the process of analyzing the final legislation and determining an estimate of the financial impact.

JOHNSON LAMBERT

AICPA Example Disclosures

- Illustrative Disclosure – Impact
  - The Tax Cuts and Jobs Act of 2017 was signed into law on December 22, 2017. We have recorded a tax benefit of $XM, primarily due to a re-measurement of deferred tax assets and liabilities offset by the impact of the transition tax on deemed repatriation of deferred foreign income.

AICPA Example Disclosures

- Illustrative Disclosure – No Material Impact
  - The Tax Cuts and Jobs Act of 2017 was signed into law on December 22, 2017. The law includes significant changes to the U.S. corporate income tax system, including a federal corporate rate reduction from 35% to 21%, limitations on the deductibility of interest expense and executive compensation, and the transition of U.S. international taxation from a worldwide tax system to a territorial tax system. We do not expect the legislation to have a financial impact on the partnership because, as a partnership, it is not subject to federal income tax and the tax effect of its activities accrues to the partners.

Example Disclosure for 2018 ASU

Reclassification

The Company adopted Accounting Standard Update 2018-XX which requires entities to reclassify from accumulated other comprehensive income (loss) to retained earnings stranded tax effects resulting from the newly enacted federal income tax rate. The reclassification amounted to ($YY,YYY).

JOHNSON LAMBERT

Final Thoughts

- Loss discounting transition rules
  - Requires revaluation of the 2017 discount
  - Amortize the difference over 8 years
  - IRS has not yet issued discount factors to calculate
  - Should you estimate?

- SEC issued Staff Accounting Bulletin 118
  - Generally, make estimates about the impact of tax reform
  - What if sufficient info is not available to estimate?
  - If you cannot make a reasonable estimate, then make no estimate!

Final Thoughts

- AMT Credits
  - AMT is repealed as of January 1, 2018
  - Credits become refundable as of December 31, 2017
  - Report in 2017 either as DTA or as recoverable

- Valuation Allowance
  - Consider all effects of tax reform when setting
  - 21%, AMT repeal, elimination of deductions, etc
  - Effects future taxable income, ability to realize benefits

Connect with us!

www.johnsonlambert.com – sign up to receive updates, newsletters, webinar invites, and more

@Johnson_Lambert

Facebook.com/JohnsonLambertCPA/

Linkedin.com/company/Johnson-lambert-llp

Disclaimer

- This presentation is provided solely for educational purposes to Johnson Lambert LLP's intended audience.
- The content contained herein should not be relied upon as accounting or tax advice because it does not take into account any specific organization's facts and circumstances.
- The views expressed by the presenters are not necessarily those of Johnson Lambert LLP.
-

Johnson Lambert LLP is a niche-focused CPA and consulting firm, focused on serving distinct industry niches. For over 30 years, we have focused on providing audit, tax, and consulting services to a national and selectively international client base including insurance entities, nonprofit organizations, and ERISA-qualified benefit plans. For more information about Johnson Lambert LLP, please visit www.johnsonlambert.com.