May 30, 2023

Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: Financial Accounting Standards Board's (the "*Board*") Proposed Accounting Standards Update, *Improvement to Income Tax Disclosures* (File Reference No. 2023-ED100) (the "*Proposal*")

Dear Technical Director:

The National Foreign Trade Counsel (the "***NFTC***") appreciates the opportunity to comment on the Proposal. We are an association focused on international tax and trade policy issues and the promotion of an open, rules-based global economy. Our membership is not limited to accountants, tax attorneys, or other tax professionals. Rather, we represent a diverse group of U.S.-based businesses—the very businesses that will ultimately bear the costs and other burdens of the purported improvements set forth in the Proposal. We, and our constituency, are deeply concerned. For the reasons set forth below, the NFTC strongly recommends that the Proposal not be adopted.

The impact of the additional disclosures required by the Proposal is significant. Companies would be required to divulge, through a tabular reconciliation and using both percentages and currency amounts, the following specific categories of information by jurisdiction (*i.e.*, federal, state, and foreign countries): state and local income tax, net of federal (national) income tax effect, foreign tax effects, the enactment of new tax laws, the effect of cross-border tax laws, tax credits, valuation allowances, nontaxable or non-deductible items, and changes in unrecognized tax benefits. For each of the aforementioned categories, the disclosures must further disaggregate and/or describe significant differences between the statutory tax rate and the effective tax rate based on their nature and/or jurisdiction.

The information required by the Proposal is either already included in existing required disclosures in less granular detail; outdated; prepared differently by companies under the advisory of different auditor perspectives (potentially leading to further confusion for investors); or otherwise irrelevant. Simply put—this information is not decision-useful for investors. In fact, the disclosure of this information is likely to expose U.S. multinational entities ("***U.S. MNEs***") to enhanced scrutiny by foreign governments, regulators, and taxing authorities (collectively, "***Foreign Authorities***") and may place U.S. MNEs at a competitive disadvantage as compared with their non-U.S. peers.

I. *The Securities and Exchange Commission (the "**SEC**") was founded for the purpose of protecting investors and derives its Congressional grant of authority therefrom.*[1] *This is directly relevant to the Proposal, which is justified on the basis of enhanced disclosures and transparency and the*

[1] Congress passed the Securities Act of 1933 (the "***Securities Act***") and the Securities Exchange Act of 1934 (the "***Exchange Act***," and together with the Securities Act, the "***Acts***"), thus creating the SEC.

provision of decision-useful information to investors. As such, it is essential to consider the scope of the SEC's authority.

The SEC's purpose is threefold: (i) protect the ordinary investor, (ii) maintain fair, orderly, and efficient markets, and (iii) facilitate capital formation.[23] The SEC must "protect the public with the least possible interference to honest business"[4] and has a duty to balance the benefits of regulatory action with the costs and burdens imposed on businesses.[5]

The Acts afford the SEC significant authority. Section 7(a) of the Securities Act authorizes the SEC to promulgate rules and regulations that are "**necessary or appropriate in the public interest or for the protection of investors**,"[6] and when determining whether an action is necessary or appropriate in the public interest, Congress directed the SEC to consider "**whether the action will promote efficiency, competition, and capital formation**."[7] Section 12(b) of the Exchange Act authorizes the SEC to promulgate rules or regulations requiring disclosure of information that it believes is "**necessary or appropriate for the proper protection of investors and to insure fair dealing in the security.**"[8] Federal securities laws give the SEC ***content of financial statements*** to be filed under those laws.[9,10]

II. *Contrary to FASB's stated justification for the proposed changes, the extensive additional disclosures required by the Proposal will not provide decision-useful information for investors.*

FASB concludes that the broad information that companies would be required to release under the Proposal is useful for investors to (i) understand an entity's exposure to potential changes in jurisdictional tax legislation and the ensuing risks and opportunities, (ii) assess income tax information that affects cash flow forecasts and capital allocation decisions, and (iii) identify potential opportunities to increase future cash broad authority to determine the ***content*** of registration statements filed under the Securities Act, and the responsibility to prescribe ***the methods to be followed in the preparation of accounts and the form and*** flows.[11] The disclosure requirements, however, will not have the effect of achieving the Proposal's stated purpose. For example:

> Valuation Allowances: Valuation allowances impact an entity's effective tax rate but generally have no, or immaterial, bearing on its cash-tax exposure, cash flows, or capital allocations. The Proposal would require companies to separately disclose material Valuation Allowance changes by jurisdiction. Because companies already disclose their bottom-line effective tax rate, there is no basis to believe that a detailed analysis of valuation allowance changes by jurisdiction–as required by the Proposal–would provide any decision-useful information for investors.

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[2] *See, e.g.*, H.R. Rep. No. 85, 73d Cong., 1st Sess. (1933) (legislative history of Securities Act); H.R. Rep. No. 1383, 73d Cong., 2d Sess. (1934) ("As a complex society so diffuses . . . the financial interests of the ordinary citizen that he . . . cannot personally watch the managers of all his interests . . . it becomes a condition of the very stability of that society that its rules of law . . . protect that ordinary citizen's dependent position.").

[3] *See* What We Do, U.S. SECURITIES AND EXCHANGE COMMISSION, https://www.sec.gov/about/what-we-do (last modified April 6, 2023).

[4] *See, e.g.*, H.R. Rep. No. 85, 73d Cong., 1st Sess. (1933) (legislative history of Securities Act).

[5] See 15 U.S.C. § 77b.

[6] *See* 15 U.S.C. § 77g (emphasis added).

[7] *See* 15 U.S.C. § 77b (emphasis added).

[8] *See* 15 U.S.C. § 78l (emphasis added).

[9] *See* 15 U.S.C. § 77s, § 78m (emphasis added).

[10] *See* Sarbanes-Oxley Act of 2002.

[11] *See* ASU 740 (Proposed Accounting Standards Update—Income Taxes (Topic 740)—Improvements to Income Tax Disclosures) (March 15, 2023), available at Proposed Accounting Standards Update—Income Taxes (Topic 740): Improvements to Income Tax Disclosures (fasb.org).

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Effect of Cross-Border Tax Laws: Much of the information that relates to this category is already disclosed to some extent by U.S. MNEs in their financial statements, albeit in less granular detail. The Proposal requires companies to further disaggregate the projected effective tax rate impact of individual cross-border tax laws if material, which includes –Global Intangible Low-Taxed Income (GILTI), the Base Erosion Anti-Abuse Tax (BEAT), Foreign Derived Intangible Income (FDII), etc. The additional detail required by the Proposal will provide limited, if any, incremental knowledge or benefit to investors, especially given the complexity and inter-relationships between different tax provisions such as GILTI and BEAT.

Foreign Tax Effects: The Proposal requires the disaggregation of material Foreign Tax Effects by jurisdiction. In connection with the OECD/G20 Base Erosion and Profit Shifting Project, most major jurisdictions will implement the Pillar Two rules, including a Qualified Domestic Minimum Top-Up Tax by 2024, which will result in a global minimum tax of 15% based upon financial accounting net income or loss. Pillar Two is discussed further below. We also strongly oppose the requirement to separately disclose material changes in unrecognized tax benefits for each taxing jurisdiction, which would provide taxing authorities a roadmap to a taxpayer's tax reserve positions. See Part III below for further discussion. Finally, by default, separating these line items by country results in a situation where there are no materiality thresholds on U.S. Federal tax impacts. Items such as valuation allowance, unrecognized tax benefits, and non-deductible items would have to be disclosed without regard to the effective tax rate impact.

Disaggregation: The Proposal requires the disaggregation of certain data by nature and jurisdiction for both rate reconciliation (as noted above) and income taxes paid.[12] It also requires all entities to disclose income taxes paid both on an interim and annual basis, broken out by federal, state, and foreign taxes, and by individual jurisdiction where such jurisdiction is equal to or greater than 5% of total income taxes paid for the year.[13] This level of granularity is unprecedented and confusing, and the required data is unnecessarily complex and costly to compile. The disaggregation of countries in the effect of foreign rates/cross-border categories do not represent meaningful data to the reader. The current proposal does not account for the relationship between the various line items or how changes in those line items would impact the overall rate. This would also make it impossible for comparison between multiple entities. Separate disclosures by country would not fully represent the tax paid on that income since some of the tax liability is due to cross-border tax laws such as GILTI, which by law is not calculated on a separate company basis. Investors will still not be able to precisely predict the impact of how a change in local tax laws would impact the overall ETR. Tax Items such as a withholding tax, disclosed separately in a foreign jurisdiction, may/may not be creditable against U.S. taxes, and could also impact the ETR without being clear to the reader. Additionally, non-deductible expenses could result in changes to expense allocations for U.S. tax purposes. The result is that investors will have no way of knowing how a change in one item will impact the ETR and could lead to incorrect assumptions.

Far from achieving the Proposal's stated justifications of helping investors, the required disclosures are likely to have the opposite effect. Adding excessive and irrelevant disclosures can be counterproductive, making it more difficult for investors to discern the material data points that are necessary for informed investment decisions.[14] This also seems to be in direct contradiction to FASB's own initiative, "Reducing Unnecessary Complexity in Financial Accounting."[15] Moreover, since the current

[12] *Id.*

[13] Although the 5% threshold also applies to reconciling items by nature, for purposes of this comment, we address only jurisdictional disaggregation.

[14] *See* Securities and Exchange Commission, Concept Release on Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064, 81 Fed. Reg. 23,916, 23,918 (Apr. 22, 2016).

[15] *See* Reducing Unnecessary Complexity in Financial Reporting, Financial Accounting Standards Board, https://www.fasb.org/page/PageContent?pageId=/reducing-unnecessary-complexity/index.html&isStaticPage=true; *see also*

accounting standards do not require specific jurisdiction-by-jurisdiction tax disclosures, significant time and money may be required for companies to update their processes to accurately collect such information. Given the volume of data and level of detail required by the Proposal, the cost of compliance (including ongoing audit fees) for companies may be significant.

III. *The Proposal mandates the public disclosure of confidential taxpayer information, the scope of which is unprecedented. The release of this information may well confer a commercial benefit on Foreign Authorities as well as non-U.S. multinational entities ("**non-U.S. MNEs**") at the expense of U.S. MNEs.*

While the Proposal and its far-reaching disclosures apply to U.S. MNEs, non-U.S. MNEs are subject to the far more limited parameters set forth in the International Accounting Standards Board's ("***IASB***") current formulation of the Proposed Amendments to IAS 12 (the *"**Proposed Pillar Two Accounting Rules**")*.[16]

The Proposed Pillar Two Accounting Rules, acknowledging concerns regarding commercial sensitivity, simply require that non-U.S. MNEs disclose the jurisdictions in which their effective tax rate for the current period falls below 15%.[17] The IASB previously considered additional disclosures that would have also required companies to identify their aggregate tax liability for such jurisdictions, a much more limited disclosure than is currently contemplated by the Proposal. Many respondents disagreed with the IASB's incremental proposed disclosure requirement. The IASB's staff summary of the feedback received notes that the "*proposed disclosures would not result in useful information and would require entities to incur significant costs to prepare that information*." [18] As a result, the IASB concluded that "*requiring entities to disclose detailed information reflecting the specific requirements of the Pillar Two model rules (Pillar Two-based information) would either not be feasible or be likely to result in undue cost or effort*."[19]

By contrast, the Proposal requires U.S. MNEs to divulge, through a tabular reconciliation, using both percentages and currency amounts, broken out by jurisdiction, the following information: (i) state and local income tax, net of federal (national) income tax effect, (ii) foreign tax effects, (iii) enactment of new tax laws, (iv) effect of cross-border tax laws, (v) tax credits, (vi) valuation allowances, (vii) nontaxable or non-deductible items, and (viii) changes in unrecognized tax benefits. In addition, for each of the foregoing categories, U.S. MNEs must further disaggregate/describe significant differences between the statutory tax rate and the effective tax rate based on their nature and/or jurisdiction.[20] The operation of Pillar Two may also distort cash taxes paid under the Proposal, as the Income Inclusion Rule and UTPR liabilities may result in cash tax paid to a country where the tax liability did not originate.

We are especially concerned by the requirement to disaggregate material changes in unrecognized tax benefits on a jurisdictional basis, which would pose a financial risk to companies without providing decision-useful information to investors. This disclosure would further expose what a taxpayer has set aside as a tax contingency in its financial statements and would become a floor, rather than a ceiling, in audit settlement discussions with tax authorities across the globe (especially in more aggressive jurisdictions), potentially leading to deleterious financial outcomes since the reserve thresholds related to income tax positions are generally lower when compared to other types of reserves. Moreover, this proposed requirement would put U.S. multinational entities at a disadvantage in audit settlement discussions relative to their non-U.S. peers that prepare and submit financial statements under

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Simplifying Accounting Standards, Financial Accounting Standards Board, https://www.fasb.org/page/PageContent?pageId=/reducing-unnecessary-complexity/simplifying-standards.html

[16] *See* International Accounting Standards Board, Exposure Draft ED/2023/1 International Tax Reform–Pillar two Model Rules, Proposed Amendments to IAS 12, available at IASB-ED-2023-1 – International Tax Reform—Pillar Two (ifrs.org).

[17] *Id.*

[18] *See* International Accounting Standards Board, Staff Paper (Agenda Reference 12B) on International Tax Reform–Pillar two Model Rules, available at AP12B: Disclosures.

[19] *Id.*

[20] *See supra* note 10.

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other accounting standards, including IFRS, which do not require the jurisdictional disaggregation of unrecognized tax benefits.

The Proposal would thus prove helpful to Foreign Authorities when reviewing the results of U.S. multinational taxpayers. Historically, confidential taxpayer information has not been disclosed to Foreign Authorities unless there is a tax information exchange agreement (a "***Tax Information Exchange Agreement***") in place. The U.S. will only enter into a Tax Information Exchange Agreement if the Treasury Department and Internal Revenue Service (the "***IRS***") are satisfied that the applicable Foreign Authority will properly safeguard the confidential taxpayer information and limit its use to tax purposes.

The Proposal would discard these much-needed safeguards and mandate the public release of this information on a separate jurisdictional basis. This would allow Foreign Authorities to more easily review and audit U.S. MNEs' tax positions while not subjecting non-U.S. MNEs to the same level of scrutiny. Moreover, such data could easily be used by Foreign Authorities for non-tax purposes. Indeed, providing Foreign Authorities with such a granular view into the tax planning strategies and unrecognized tax benefits of U.S. MNEs on a jurisdictional basis affords them a commercial advantage that could be used to, for example, implement regulations or provide government support to certain entities or industries in a way that would benefit non-U.S. MNEs and Foreign Authorities at the expense of U.S. MNEs. This may include providing support to foreign government state-owned enterprises.

In addition, these disclosures may well be helpful to foreign competitors of U.S. MNEs, providing them with nuanced insight into the tax planning strategies of their U.S. counterparts. Requiring U.S. MNEs to provide commercially sensitive information without the imposition of any reciprocal burden on non-U.S. MNEs places U.S. MNEs at a material competitive disadvantage.

As discussed, NFTC strongly urges that the Proposal not be adopted. If aspects of the Proposal should move forward, we would suggest the following:

Disclose material unrecognized tax benefit change on a consolidated basis: Preparers should disclose the effective tax rate impact of material unrecognized tax benefit changes (see below for threshold) in all jurisdictions on a global consolidated basis with the appropriate qualitative disclosures that align with current accounting guidance. A global consolidated disclosure will clearly inform investors of the effective tax rate impact resulting from material changes in unrecognized tax benefits without raising the above noted concerns arising from jurisdictional disaggregation. The instructions should also clarify that this category includes interest, penalties, and indirect tax impacts.

Eliminate the proposed interim reporting provision: The proposed requirement to disclose a qualitative description of any reconciling items that results in significant changes in the *estimated annual effective tax rate* from the effective tax rate of the prior annual reporting period on an interim basis should be removed because the two rates are not comparable. In addition, the *estimated annual effective tax rate* is a technical accounting term and may not be familiar to the users of the financial statements. Finally, companies are already required to disclose the reasons for significant variations in the interim tax rate under existing accounting guidance.

Providing thresholds before requiring disclosure: In general, we believe that requiring disclosure of specific categories without applying a numeric threshold is burdensome for companies and not useful to the users of the financial statements. Without consideration of a materiality threshold, companies will be required to track and disclose immaterial amounts. We agree having specified categories are helpful to promote comparability, but they should only be required to be disclosed if above the numeric threshold. To accomplish this, the Board should consider a standard threshold determined by applying a percentage of profit before tax (e.g., 1.5% of profit before tax) to promote consistency across multinational companies which may reconcile to varying rate starting points depending on their country of domicile, some of which may have lower statutory tax rates.

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Introduce a percentage of profits before tax threshold: We agree that for public entities, this is consistent with current disclosure rules under SEC Regulation S-X 210.4-08(h)(2), as both preparers and readers of the financial statements should be familiar with this approach. However, rigid application of this threshold could require companies with lower profit levels or those starting with lower tax rates to expend significant time and resources to disclose immaterial amounts. As a result, we believe that applying a standard threshold determined by applying a percentage of profit before tax is more appropriate (e.g., 1.5% of profit before tax) and would promote consistency across multinational companies which may otherwise reconcile to varying rate starting points, depending on their country of domicile.

Provide a Transition Rule: Transition on a retrospective basis is operable and would likely be useful for readers of financial statements, but as previously mentioned, will likely require significant investment in time and expenses as information supporting prior year disclosures may not have been prepared in the same manner that would easily allow for the increased disaggregation required under the proposed amendments.

Delay Implementation Date: We recommend the proposed amendments to interim and annual reporting apply no earlier than for financial years starting after December 31, 2024 (i.e., the 2025 tax year), to allow preparers time to implement changes and present the retrospective periods. The Proposal, as currently written and being required on a retrospective basis, will require significant, additional effort to maintain compliance with the new rules. For companies that operate in multiple jurisdictions (foreign or domestic), the additional effort will be exponential. Changes will likely be required in how companies gather and analyze information, including changes to information technology systems or other tools used. Furthermore, as the changes will require retrospective disclosure of comparative periods going back two years, companies may not currently have systems or processes in place to capture and disaggregate the prior period data as required, resulting in manual, labor intensive efforts. Additionally, the resulting disclosure changes may necessitate updates in the design of related internal controls, while also requiring coordination with external financial auditors. As a result, once final rules are published, sufficient lead time will be needed for companies to develop a thorough plan of implementation. Guidance on whether partial (or full) early adoption is permissible is requested; while we do not anticipate many companies to proceed with early adoption, it should be permitted.

Additionally, should the Proposal move forward, clarity is needed in the following:

Discretion to present on a net or gross basis: We recommend the Board issue language allowing companies to exercise judgment on whether to present reconciling items on the net or gross basis within a jurisdiction depending on the nature of offsetting effects and their interdependency. To promote transparency, companies would then provide a qualitative comment on the presentation method adopted.

While it is important for the proposed amendments to retain a level of flexibility in interpretation and application based on a company's unique operations and circumstances, we believe some additional (general) guidance or examples on acceptable interpretations would be helpful. For example:

- **True-ups to prior year provisions (based on tax return filings):** We believe the aggregate income tax impacts related to prior year-true-ups should be considered its own item by "nature," subject to disaggregation and separate disclosure if the threshold is met, instead of having to look through to the underlying driver of each item generating the true-up and then aggregating with other line items in the rate reconciliation (e.g., tax credits, etc.). The cost of having to determine the underlying composition of every prior year true-up, especially for multinational companies, would not outweigh the potential benefit to the investors, which would likely be minimal. Instead, we believe it would be more meaningful to investors and readers of the financial statements if significant impacts resulting from prior year true-ups are disclosed separately only if the threshold to separately disclose is met.

- **Jurisdictional characterization of withholding taxes:** As the Proposal focuses on disaggregating disclosures by jurisdiction, we believe it would be helpful to have the jurisdictional characterization of withholding taxes clarified – i.e., should the expense be recorded in the country that imposes and receives the tax, or should the expense be recorded in the country that suffers the cost of the tax? We believe withholding taxes should be disclosed in the country that suffers the cost of the tax.

- **Enactment of new tax laws:** Clarify that it only considers remeasurement of deferred taxes and prior year adjustments to current taxes to the extent retroactive changes in tax law are enacted.

- **Tax credits:** As it relates to foreign tax credits, there is an inconsistent application since the effect of cross-border tax laws (for instance, GILTI) is gross of foreign tax credits. It would be more appropriate to include the effect of items like foreign tax credits along with the underlying item that is generating the credit. This treatment would be consistent with state and local income taxes, which are presented net of the federal effect.

For the reasons set forth herein, we strongly encourage FASB to reconsider adopting the Proposal. We are happy to provide additional details regarding our comments and welcome the opportunity to provide additional constructive feedback as the Board deliberates on the Proposal.

Sincerely,

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