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FASB Makes Tentative Decisions About Exposure Draft Related to Reclassifying Certain Tax Effects From AOCI

Background

At its meeting on February 7, 2018, the FASB reached tentative decisions related to its proposed Accounting Standards Update (ASU) *Reclassification of Certain Tax Effects From Accumulated Other Comprehensive Income*. The proposed ASU was issued to address industry concerns related to the application of ASC 740¹ to certain provisions of the new tax reform legislation commonly known as the Tax Cuts and Jobs Act (the "Act").²

Specifically, some constituents in the banking and insurance industries expressed concerns about the requirement in ASC 740 that the effect of a change in tax laws or rates on deferred tax assets and liabilities be included in income from continuing operations in the reporting period that contains the enactment date of the change. That guidance applies even in situations in which the tax effects were initially recognized directly in other comprehensive income at the previous rate, resulting in "stranded" amounts in accumulated other comprehensive income (AOCI) related to the income tax rate differential.

For more information and analyses related to tax reform, visit our [U.S. Tax Reform Insights](#) page on [Deloitte.com](#).

¹ FASB Accounting Standards Codification (ASC) Topic 740, *Income Taxes*.

² H.R. 1/Public Law 115-97 states that it is an "Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018."

In response to the concerns, the FASB issued an exposure draft (ED) of a proposed ASU on January 18, 2018, on which comments were due by February 2, 2018. The ED would require entities to make a one-time reclassification from AOCI to retained earnings for stranded tax effects resulting from the newly enacted corporate tax rate. The amount of the reclassification would be calculated on the basis of the difference between the historical and newly enacted tax rates for deferred tax liabilities and assets related to items within AOCI.

Tentative Decisions Reached

At its February 7, 2018, meeting, the Board reached the following tentative decisions related to the proposed ASU:

- Upon adopting the ASU, an entity will be required to disclose:
 - Its accounting policy related to releasing stranded tax effects (e.g., the portfolio approach or the security-by-security approach).³
 - Whether it has elected to reclassify, to retained earnings in the statement of stockholders' equity, the stranded tax effects in AOCI related to the Act.
 - If it has elected to reclassify to retained earnings the stranded tax effects in AOCI related to the Act, what the reclassification encompasses (whether it only includes the change in the federal corporate tax rate or whether it also includes other changes resulting from the Act that affect AOCI). Other effects might include, for example, the income tax effects of accounting for foreign subsidiaries when a deferred tax liability had previously been recorded for an excess of the amount for financial reporting over the tax basis in the investments.

The ED had required all entities to record the reclassification, to retained earnings, of the stranded tax effects (principally the income tax effects related to the change in the federal corporate tax rate) in AOCI related to the Act.

- The guidance in the proposed ASU will be effective for fiscal years beginning after December 15, 2018, including interim periods therein, and early adoption will be permitted. An entity will apply this guidance to each period in which the effect of the Act (or portion thereof) is recorded and may apply it either (1) retrospectively as of the date of enactment or (2) as of the beginning of the period of adoption. The Board decided to permit early adoption for public business entities for which financial statements have not yet been issued and for all other entities for which financial statements have not yet been made available for issuance. **The ED had also allowed early adoption but had required retrospective application.**



Connecting the Dots

If a registrant elects to apply the guidance **retrospectively** after it files its annual financial statements in its Form 10-K (e.g., the first quarter of 2018 for a calendar-year entity) and subsequently files a new or amended registration statement that incorporates by reference the interim financial statements that reflect the impact of the adoption, the registrant must consider the need to retrospectively revise its annual financial statements that are incorporated by reference in that new or amended registration statement (i.e., the annual financial statements in its Form 10-K). This requirement does not apply to a registrant that chooses to (1) apply the new guidance as of the beginning of the period of adoption or (2) early adopt the new guidance in its annual financial statements that include the period of enactment (e.g., the annual financial statements in its 2017 Form 10-K for a calendar-year entity).

³ For more information on the portfolio approach and security-by-security approach, see Section 7.18 of Deloitte's [A Roadmap to Accounting for Income Taxes](#).

The Board expects to issue a final ASU by February 16, 2018.

For a summary of the Board's [tentative decisions](#) reached at its February 7, 2018, meeting, see the FASB's Web site.

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