TEI-SJSU
High Tech Tax Institute

Hot Topics in Accounting for Income Taxes

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Agenda

- ASU 2023-09 Improvements to Income Tax Disclosures
- California SB 122 and Valuation Allowance
- Current Internal Control Environment

ASU 2023-09 Improvements to Income Tax Disclosures

Retrospect on adoption by public business entities

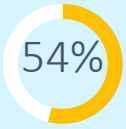
Initial Insights from the Adoption of ASU 2023-09

Key trends

The entities assessed included Form 10-K and Form 20-F filings from January 1, 2026 to March 17, 2026, specifically focusing on companies with year-ends after December 15, 2025 and revenue over $25.0 billion resulting in a sample size of 147 companies.



Adopted prospectively



Of non-U.S. domiciled companies used a rate other than the rate of the country of domicile



Did not disclose disaggregated total income tax expense (benefit)



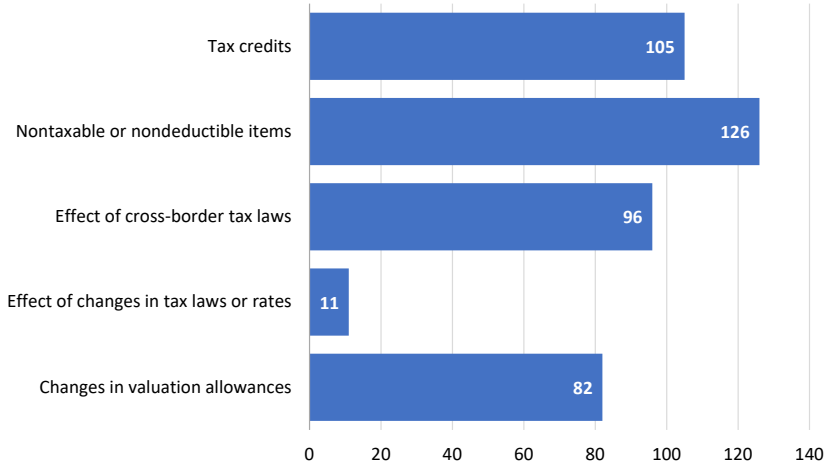
Did not specify the states that make up the majority of the state and local income tax category



Domestic Federal Specific Categories

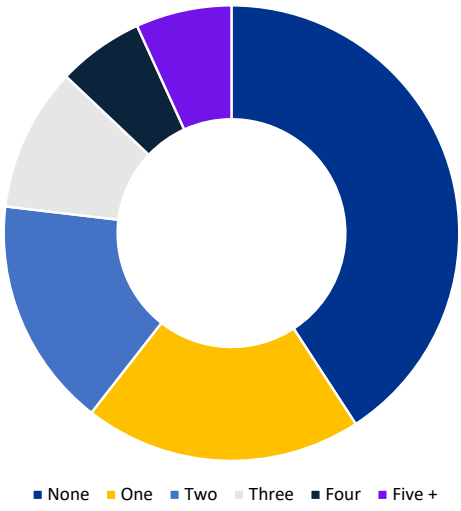
Disaggregation of domestic federal categories

- Within the tax credits category, research tax credits and foreign tax credits were the most often disaggregated.
- Within the nontaxable or nondeductible items category, the effects of share-based payment awards was by far the most often disaggregated.
- Within the effect of cross-border tax laws category, global intangible-low taxed income and foreign-derived intangible income represented the most often disaggregated.



Foreign Tax Effects Category

Disaggregation of jurisdictions within the foreign tax effects category



60
Instances of no foreign jurisdictions disclosed

16
Times Brazil and the United Kingdom were disclosed

50
Number of unique foreign jurisdictions disclosed

State and Local Income Taxes

State and local jurisdictions that make up the majority of the effect of state and local income tax category

Average of 3 state and local jurisdictions

California was the most frequently disclosed state and local jurisdiction, followed by Illinois, Pennsylvania, Florida, New York City, New York, and New York State.



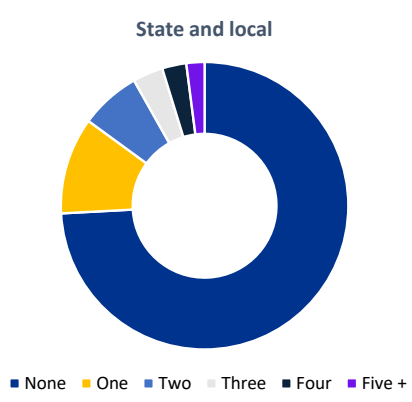
26
Instances of the qualitative disclosure omitted

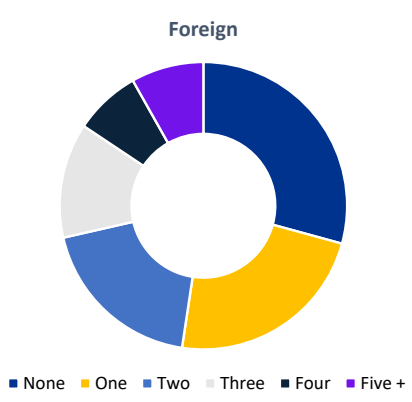
73
Number of times California was disclosed

46
Number of unique state and local jurisdictions disclosed

Income Taxes Paid

Disaggregation of jurisdictions within income taxes paid disclosures





127
Disclosures included in the income taxes notes

29
Instances of the United Kingdom disclosed

2
Average number of foreign jurisdictions disclosed

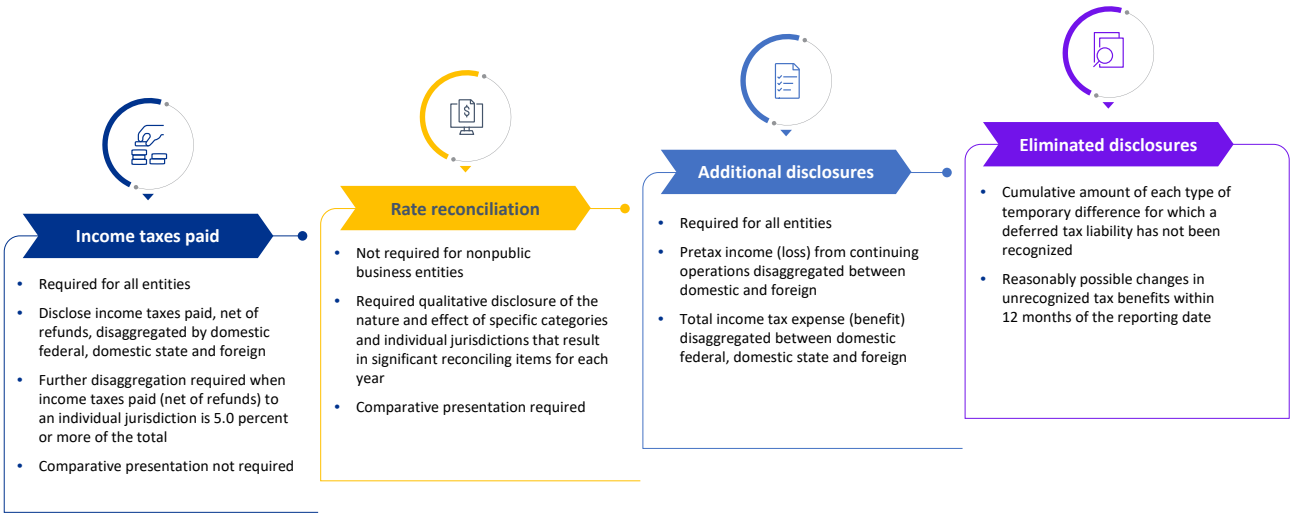
Commonly Asked Questions on Adopting ASU 2023-09



1. Consideration of materiality for the required disclosures, primarily related to entities with near break-even pretax income (loss)
2. Classification of reconciling items in the effective tax rate reconciliation, including prior year adjustments reflected in the current year
3. Evaluation of policy elections, including presentation of credits related to the effects of cross-border tax laws and presentation of unrecognized tax benefits
4. Consideration of combined rates for foreign jurisdictions, such as Canada, Germany and Switzerland, among others

Adoption by nonpublic business entities (non-PBEs)

Overview for Non-PBEs



The amendments are effective for entities other than public business entities for annual periods beginning after December 15, 2025.

Non-PBE Qualitative Disclosures

Differences between the statutory income tax rate and effective tax rate

Statutory income tax rate

We believe that non-PBEs should consider using the domestic federal statutory income tax rate in the country of domicile and disclosing the statutory income tax rate used to determine significant reconciling items.

Effects of significant reconciling items

We believe qualitative discussion about the effect of a specific category or individual jurisdiction may simply indicate whether that item increases or decreases the effective tax rate.

Significant domestic and foreign reconciling items

If significant reconciling items are domestic, determine the specific domestic categories a significant reconciling item relates to and disclose the nature of those items. If foreign, determine and disclose the country.

Tabular rate reconciliation disclosure by non-PBEs

We believe non-PBEs that choose to disclose a tabular rate reconciliation follow all of the rate reconciliation guidance for PBEs to prevent the disclosures from being misleading.

Specific categories

Non-PBEs use the rate reconciliation categories used by PBEs in the tabular reconciliation.

Example: Qualitative disclosures by non-PBEs

Entity's effective tax rate for the fiscal year ending December 31, Year 3 was 17%, which differs from the statutory income tax rate of 21%. This difference is primarily due to the decreasing effect of research tax credits, excess tax benefits on share-based payments and foreign tax effects due to lower tax rates in foreign countries, particularly operations in Ireland. These effects were partially offset by the increasing effect of state and local taxes, net of federal effect, and cross-border taxes in the US for global intangible low-taxed income.

California SB 122 and Valuation Allowance

California SB 122 – Updates and Considerations

Credits, NOLs, and More

- Continued Limitation on Credit Utilization:
  - SB 122 continues to place limitations on the utilization of certain California credits, such as the California research and development credit, jobs tax credit, “California Competes” credit, and motion picture production credit.
    - This temporary limitation and credit refundability continue through taxable years beginning before January 1, 2030.
    - A permanent credit limitation beginning in the 2030 tax year.
    - This permanent limitation generally allows credit utilization up to the greater of $5 million or 70% of the taxpayer’s California tax liability.

- Net Operating Loss (“NOL”) Carryover Deduction
  - California suspended the NOL carryover deduction for most taxpayers for taxable years beginning on or after January 1, 2024, and before January 1, 2027.
  - Beginning with taxable year January 1, 2027, taxpayers are permitted to resume the NOL carryover deduction.

Assessing the Realizability of Deferred Tax Assets (DTAs) Due to California R&D Credit Limitation

Three approaches can be considered:

- Tax law ordering approach
- With-and-without approach
- Replacement approach

Assumptions:

- Entity A is U.S.-based technology company with significant ongoing R&D activities
- Entity A consistently generates substantial California R&D credits each year
- California R&D credit has been carried forward
- Entity A generates consistent taxable income but offset against R&D credits

Tax Law Ordering Approach

Line item	$
PBT	1,000
Sec. 59(e) Amortization	(200)
Taxable income	800
Apportionment	10.0%
Tax rate	8.84%
Tax liability	7
R&D credit utilization	(7)
Tax liability after credits	**0**

Note: Apportionment and tax rate illustrative (e.g., California 8.84% corporate rate). Figures in $ millions unless noted.

- Following the tax return ordering, Sec. 59(e) is utilized before R&D credits
- Therefore, no valuation allowance is needed for non-credit DTA (i.e. 59(e) DTA)
- Given credit generation exceeds utilization, the credit DTA requires a valuation allowance
- No impact from SB 122

With / Without Approach – Before SB 122

Line item	With	Without	Difference
PBT	1,000	1,000	0
Sec. 59(e) Amortization	(200)	0	(200)
Taxable income	800	1,000	(200)
Apportionment	10.0%	10.0%	0.0%
Tax rate	8.84%	8.84%	0.00%
Tax liability	7	9	(2)
R&D credit utilization	(7)	(9)	2
Tax liability after credits	**0**	**0**	**0**

- Following the with / without approach, there is no difference in the overall tax liability prior to SB 122
- Therefore, there is no economic value from the utilization of the non-credit DTA
- Full valuation allowance against both noncredit and credit DTAs in CA.

With / Without Approach – After SB 122 (Assume Post 2029)

Line item	With	Without	Difference
PBT	1,000	1,000	
Sec. 59(e) Amortization	(200)	0	
Taxable income	800	1,000	
Apportionment	10.0%	10.0%	
Tax rate	8.84%	8.84%	
Tax liability	7	9	(2)
R&D credit utilization	(5)	(6)	1
Tax liability after credits	**2**	**3**	**(1)**

Note: The (1.768) difference in tax liability is the marginal tax effect of the Sec. 59(e) amortization deduction.

- Post SB 122, the non-credit DTA saves the Company $1 cash tax
- Therefore, now there is economic value from the utilization of the non-credit DTA
- Release $1 of valuation allowance ("VA") resulting in a partial VA in CA post SB 122

Replacement Approach

Line item	$
PBT	1,000
Sec. 59(e) Amortization	(200)
Taxable income	800
Apportionment	10.0%
Tax rate	8.84%
Tax liability	7
R&D credit utilization	(7)
Tax liability after credits	**0**

Conclusion: As long as credit generation (7.072) exceeds the DTA utilized (1.768), the full valuation allowance is retained.

- If the generation of credits exceeds the utilization of non-credit DTA (i.e. $200 x 10% x 8.84% = 2), the utilization of the non-credit DTA is simply replaced by a credit DTA
- Therefore, retain a full valuation allowance post SB 122

SEC Comment Letters

SEC Comment Letter Trends: Non-GAAP Measures

Non-GAAP Measures – Themes

- Reflected net of tax vs. presenting income taxes separately
- Non-GAAP measures exclude income taxes
- Further explanation of income tax adjustments needed

SEC Compliance and Disclosure Interpretation on Non-GAAP Financial Measures, Question 102.11

A registrant should provide income tax effects on its non-GAAP measures depending on the nature of the measures. If a measure is a liquidity measure that includes income taxes, it might be acceptable to adjust GAAP taxes to show taxes paid in cash. If a measure is a performance measure, the registrant should include current and deferred income tax expense commensurate with the non-GAAP measure of profitability. In addition, adjustments to arrive at a non-GAAP measure should not be presented "net of tax." Rather, income taxes should be shown as a separate adjustment and clearly explained.

Comment Letter Examples

> "Clearly describe to us in detail what the adjustments represent and your reasons for excluding the changes in your tax valuation allowances from the measure. Tell us why management believes the adjustments are meaningful and appropriate. Explain to us how you determined that your evaluation of the positive and negative evidence to support realizability would be different on a non-GAAP basis such that excluding the changes in the GAAP tax valuation allowance would be appropriate. Tell us why the adjustments are consistent with Questions 100.01 and 102.11 of the Non-GAAP Financial Measures Compliance & Disclosure Interpretations.

> "Revise your adjusted net income and related per share amounts to include separate income tax adjustments related to your non-GAAP adjustments to reflect current and deferred income expense commensurate with the level of non-GAAP profitability presented by your measure. Otherwise, tell us why the non-GAAP adjustments you reflect would have no impact on your taxes if the related expenses were not incurred. See Question 102.11 of the Compliance and Disclosure Interpretations (CDIs) for Non-GAAP Financial Measures.

SEC Comment Letter Trends: Income Tax Disclosures

Effective Tax Rate Reconciliation

- Expand disclosure of ETR composition and quantify components exceeding 5% of the statutory amount (pre-ASU disclosures)
- Explain fluctuations between the current and prior year

Valuation Allowances

- Further explanation of rationale for release of a valuation allowance
- Additional disclosure on timing of release of a valuation allowance

Comment Letter VA Example

> "We note the release of your income tax valuation allowance related to UK deferred tax assets resulted in you recording an income tax benefit of $153.1 million in the fiscal year ended June 28, 2025. Please explain to us, and expand your disclosures in future filings to more fully address, the specific positive and negative evidence you considered in determining it was more-likely-than-not UK deferred tax assets are realizable, how that evidence was weighed, and how that evidence led you to determine it was appropriate to reverse a portion of your income tax valuation allowance in the current fiscal year. Refer to Item 303(b)(3) of Regulation S-K and ASC 740-10-30-16 through 30-25.

SEC Comment Letter Trends: Income Tax Disclosures

Withholding taxes

- The Staff may request additional information on the specific plans to support the indefinite reversal criteria are met.

Comment Letter Investment in Subsidiary Example

> We note that Company A declared dividends of $X and $X to Company B in October and November 202X, respectively, and these dividends were subject to a 5% withholding tax in accordance with the applicable tax treaty. We also note the Group did not provide for deferred income taxes and withholding taxes on the undistributed earnings of foreign subsidiaries during the two years ended December 31, 202X. ASC 740-30-25-17 requires a parent entity to have evidence of specific plans to support the assertion that the indefinite reversal criteria are met. Tell us the specifically documented plans for reinvestment during the two-year period to support your assertion that the remittance of the earnings will be postponed indefinitely. Explain what occurred, when it became apparent that some or all of the undistributed earnings of your subsidiary would be remitted in the foreseeable future and why the related income taxes were not accrued as a current period expense in an earlier period. See ASC 740-30-25-17 and 25-19.

SEC Semiannual Reporting

Semiannual Reporting – Proposal

The SEC's proposed optional semiannual reporting framework would offer public companies an alternative to quarterly reporting with the SEC.

> **Our proposal focuses on flexibility—ensuring companies and their investors can select reporting cadences that best reflect their business models."**
>
> **SEC Commissioner, Mark T. Uyeda**

- **Quarterly reporting would remain the default, and a company would need to affirmatively elect semiannual reporting annually** through a check box
- A semiannual filer would file a new **Form 10-S** covering the first half of the fiscal year instead of filing Form 10-Q for each of the first three quarters
- Form 10-S would require the **same information** as Form 10-Q, with financial statements covering a six-month period, auditor review, and Inline XBRL tagging
- The proposal **would not change Form 8-K requirements** and triggering events, including related to furnishing any earnings releases
- Comment period ended July 6, 2026

Semiannual Reporting – Comment Period Feedback

Supporters of reducing reporting frequency

- Flexibility in reporting frequency preferable to a one-size-fits-all approach
- Quarterly earnings releases or other financial information would likely still be released

Opponents of the proposal

- Reduced transparency
- Less timely investor information
- Greater risk that fraud and other errors go undetected
- Skepticism that the anticipated cost would be significant