FIN 48 Implementation for Private Companies – No More Deferrals

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For fiscal years beginning after December 15, 2008, privately held U.S. companies are required to comply with the Financial Accounting Standards Board's (FASB's) interpretation No. 48 – Accounting for Uncertainty in Income Taxes (FIN 48). FIN 48 calls for the recognition of all income tax positions taken, or expected to be taken, by U.S. companies, effective for fiscal years beginning after December 15, 2006. While public companies have been required to comply with FIN 48 since then, FASB has recognized the difficulty of nonpublic company compliance and therefore, delayed the effective date for privately held companies. Beginning in early 2007, the Private Company Financial Reporting Committee (PCFRDC), a group of financial statement users, preparers, and CPA practitioners, began raising concerns that many nonpublic entities and their tax service providers were not fully aware of FIN 48's implications and had not had the necessary time to understand and apply FIN 48 before its effective date. In addition, many private companies thought it was less relevant to them because they do not engage in tax sheltered types of transactions as frequently as public companies. In December of 2008, FASB extended the deferral of the application of FIN 48 for private companies until years beginning after December 15, 2008, (i.e., until 2009 for calendar-year companies).

Now that the deadline for additional possible deferrals has expired, it is time for private companies to comply, but many lack the expertise to meet the new requirements. Because FIN 48 applies to all income tax positions, it requires additional tracking and documentation of those tax positions, significantly impacting on a corporation's resources.

Prior to their annual audit, calendar-year private companies will need to have completed a FIN 48 analysis of the year-beginning tax positions in order to record the adjustment for the change in accounting method at the end of 2009. For companies that want to report in accordance with U.S. GAAP and issue audited financial statements, an organization's external auditor will need auditable evidence supporting that the company:

- Identified all material income tax positions for all types of income taxes and all open years in all jurisdictions, including multiple states and out-of-U.S. jurisdictions
- Documented those tax positions and subjected them to a recognition test to determine which were more likely than not (greater than 50 percent) to be realized or sustained if examined by a taxing authority
- Computed how much of each tax position would be realized, and
- Computed and tracked the total amount of liability or benefit correctly in the financial statements.

While complex, FIN 48 analysis and documentation can provide a company with a clearer picture of its overall tax exposure and enable it to better monitor and potentially reduce tax exposure. A FIN 48 analysis can uncover areas where the company might be at risk. For example, state income tax nexus is one area of exposure. An analysis may revisit unreported tax positions such as a decision not to file a return in a state where nexus is in doubt. Other areas the IRS is frequently challenging include the R&E tax credit. If a company is booking a benefit from the credit, it also would need to book the liability that might occur if the tax position is challenged.

Other issues include:

- Companies with foreign operations and transfer pricing issues that need to be carefully documented
- Loans provided to private-company owners
- Scrutiny of excess compensation to family members

The time to start is now – not the day before the auditors arrive. For some companies, the FIN 48 analysis can be brief, especially if a company conducts business in only one state and complex business practices are simple. However, any company that does not have experienced tax professionals on staff will likely need to engage outside tax professionals to oversee the process, to help create the analyses, and gain an understanding of the areas of risk.

Do not be fearful of the process. Instead, have straightforward conversations and dialogue about what the tax posture of your company should be and what the acceptable level of risk will be.

This article originally was featured in the *Baker Tilly Tax Strategist* electronic monthly newsletter, featuring hot topics, tax savings ideas, case studies, and other relevant information to help you navigate through the inevitable challenges that arise and capitalize on tax opportunities that come your way. Send an e-mail to tax@bakertilly.com with any questions or to subscribe to the newsletter.