

Baker Tilly Comments on Proposed Schedule UTP

In April 2010, the IRS released a draft of [Schedule UTP](#), a new form requiring reporting of uncertain tax positions effective for 2010. If adopted, this schedule will be a significant expansion of previous reporting requirements and could prove burdensome and costly to many businesses. With this in mind, Baker Tilly submitted formal comments and recommendations to the IRS to recommend against the imposition of this schedule on small and mid-sized businesses. A copy of that letter is reproduced immediately below.

If you have any questions or concerns regarding the comments, or this potential new schedule, please contact your Baker Tilly advisor or send an e-mail to tax@bakertilly.com.

In addition, you can find more information on the proposed new schedule in our Tax Alert dated April 28, 2010, "[IRS Releases Draft Schedule to Report Uncertain Tax Positions.](#)"

May 27, 2010

Internal Revenue Service
C:PA:LPD:PR (Announcement 2010-9)
Room 5203
P.O. Box 7604
Ben Franklin Station, N.W.
Washington, D.C. 20044

Dear Sir or Madam:

Baker Tilly, on behalf of our clients, offers the following comments concerning the schedule for reporting uncertain tax positions proposed in Announcement 2010-9 and Announcement 2010-30. We have noted that numerous professional firms and associations have raised substantial concerns regarding this schedule, and we concur that this proposal requires careful reconsideration before being implemented. Our fundamental concerns are that the asset threshold is too low to effectively target the transactions the Service wishes to identify and the proposed instructions are overly vague and need additional clarification in certain areas. Also, if the Service later extends the application of the Schedule UTP to entities that do not issue audited GAAP-basis financial statements, the schedule as proposed will result in an undue burden on many taxpayers who do not currently conduct the required analyses, but then would be required to do so.

Undue Burden on Taxpayers – Should the Service later impose the reporting requirements of Announcement 2010-30 on entities that do not issue audited GAAP-basis financial statements, it would effectively impose FIN 48 reporting requirements on businesses not otherwise subject to FIN 48. FIN 48 applies to publicly-traded companies, and starting this year, to private companies that issue GAAP-basis financial statements. Consequently, private companies have limited experience with complying with this requirement. In addition, not all private companies have the need or the accounting resources to prepare GAAP-basis financial statements. Many such companies either do not issue financial statements or issue income tax basis financial statements, neither of which require FIN 48 disclosure or completion of the underlying analysis. Therefore, a business that does not issue GAAP-basis financial statements and does not fall under FIN 48 for GAAP purposes would essentially be thrust into FIN 48 by the IRS.

Proposed Schedule UTP would impose an unnecessary and heavy compliance burden on these companies, many of which are already experiencing financial difficulties in the current economic environment. FIN 48 analyses are expensive and time-consuming. These companies, mostly small and mid-size businesses, would incur substantial fees for an accounting firm or other knowledgeable advisor to perform a FIN 48 analysis. For the average smaller-sized client this would represent a material increase in fees. We respectfully request that the proposed schedule be limited to taxpayers subject to FIN 48 for financial statement purposes.

Timing Concerns – Public companies have been subject to FIN 48 for a few years. However, private companies are subject to FIN 48 for the first time this year. Many are still struggling with the requirements of FIN 48 and their application, and as noted above, many private companies have no experience with FIN 48 since they do not issue GAAP-basis financial statements. Accordingly we respectfully request that you consider limiting application of the proposed schedule to public companies that have already waded through the complexities of FIN 48 and delaying the application to private companies for three years until those companies have the same opportunity to become familiar with the rules.

Please also note that not all tax advisors represent public companies. Although almost all tax professionals have been aware of the application of FIN 48 to public companies for several years, many of those tax professionals advise privately held companies and have not studied the rules of FIN 48 for application to their clients. Therefore, the specific applications of FIN 48 are new to those advisors this year, too.

Proposed Instructions – The instructions as proposed are difficult to apply. For example, they state, “Schedule UTP also requires the reporting of tax positions taken by the corporation in a tax return for which a reserve has not been recorded by the corporation or a related party based on an expectation to litigate or an IRS administrative practice.” Neither of these additional reporting requirements are defined. Either they refer to definitions under FIN 48, or they are wholly without definition or guidance. We would respectfully remind the Service that most tax return preparers are unfamiliar with the specific application of FIN 48 rules, as auditors are normally engaged to prepare a FIN 48 analysis. If these instructions implicitly refer to a FIN 48 concept, then they should explicitly state that and cite the language in FIN 48.

Threshold Considerations – As currently proposed, the schedule would apply to taxpayers with assets of \$10 million or more. Companies with such a small asset base do not reflect the typical profile of taxpayers engaging in aggressive tax transactions that the IRS is apparently trying to identify. Such structures generally involve entities with considerably greater assets than the threshold now proposed. This low threshold does not adequately encompass businesses based on true size. We recommend considering either a higher threshold (i.e., \$100 million in assets) or a threshold based on business activity such as gross receipts (i.e., \$100 million in annual gross receipts).

Maximum Tax Adjustment – The Service has stated that one of the objectives of the proposed schedule is to improve the efficiency of the examination process by reducing the amount of time agents spend identifying issues. We are concerned, however, that requiring disclosure of a Maximum Tax Adjustment will have the opposite effect. Agents could be distracted by large numbers on the proposed schedule and waste time looking at outcomes that have a very low probability of occurrence. FIN 48 allows taxpayers to adjust for these “outliers” by incorporating risk analysis into the measurement of their reserve. FIN 48 recognizes that disclosure of extremely low-probability outcomes is not helpful to the users of the financial statements, nor will it be helpful to the Service in our opinion. If the purpose of the proposed schedule is to help the Service identify and audit the right issues, then the description of the issue should suffice. We recommend that the Maximum Tax Adjustment be removed from the proposed schedule.

Example: A taxpayer takes a position on their return that meets the more likely than not standard under FIN 48. The position produces a \$10 million tax benefit in the current year. Since the position meets the more likely than not standard under FIN 48, the deduction is allowed for financial statement purposes, but a probability assessment is done and a liability reserve recorded in the financial statements. Based on the probability of losing if the position is litigated, the taxpayer determines that the chance of losing is 5 percent or \$500,000. Accordingly, the net deduction for financial statement purposes is \$9.5 million. However, under the maximum adjustment contemplated by the Schedule, a taxpayer would be required to disclose \$10 million as the maximum tax adjustment. This amount is recorded even though the position only has a 5-percent risk of loss.

While the Service has indicated that it will not use the maximum tax exposure for audit purposes, it is human nature to focus on large numbers. Therefore, we recommend disclosure be limited to discussion of issues that do not meet a more likely than not standard, and that no monetary estimate of tax exposure be required to be disclosed on Schedule UTP.



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Materiality Standard – We recommend that the IRS provide a materiality threshold so taxpayers are not burdened with disclosing immaterial tax issues. A FIN 48 analysis requires all items be considered, but only material items are disclosed in the financial statements, because it falls below the auditor’s materiality assessment. We recommend that the IRS adopt the auditor’s materiality level or provide a safe-harbor threshold so that taxpayers are not burdened with preparing immaterial disclosures. This will also reduce the Service’s time in assessing disclosures.

In summary, we respectfully request that the proposed Schedule UTP apply only to entities subject to FIN 48 for financial statement purposes, that its implementation be delayed for non-public companies, and that the final schedule incorporates the changes discussed above.

Very truly yours,

Baker Tilly Virchow Krause, LLP
Vienna, VA