

In brief

The latest news in financial reporting



No. US2017-11
March 29, 2017

At a glance

When the UK completes its exit from the EU, existing tax reliefs and exemptions will likely cease to apply to transactions between UK entities and entities in other EU Member States. Entities that may be subject to potentially material effects upon UK withdrawal should provide transparent disclosure now.

Brexit—Income tax accounting implications

What happened?

On March 29, 2017, the UK Government gave formal notice of its intention to leave the EU. This notice triggers the process of negotiating the UK's exit, which will occur in two years, unless the deadline is extended or a withdrawal agreement is negotiated sooner.

Various tax reliefs and exemptions that apply to transactions between EU Member States under existing tax laws will likely cease to apply to transactions between the UK and EU Member States when the UK ultimately withdraws from the EU. It is unclear at this stage if or when any new tax treaties between the UK and the EU or individual EU Member States will replace those reliefs and exemptions.

Why is this important?

US GAAP requires entities to recognize the effect of a change in tax law or rate on deferred taxes at the date of enactment. The unprecedented nature of the UK's withdrawal from the EU raises a question about whether written notification of withdrawal constitutes a recognition event under the provisions of ASC 740, *Income taxes*.

Written notification of withdrawal begins the negotiations regarding the terms of withdrawal between the UK and the EU. It does not change the application of existing tax laws, and does not establish a clear framework for what the ultimate outcome of the negotiations and legislative process will be. It is the commencement, not the culmination, of a complex, multi-territory, multifaceted legislative process.

As a result, we believe entities should not account for the impacts of withdrawal in their income tax provisions until enacted changes in tax laws or treaties between the UK and the EU or individual EU Member States occur, but no later than the UK's withdrawal from the EU.

In the interim, entities that have intra-European dealings (such as dividend distributions and prior restructurings) that may be subject to potentially material deferred income tax effects upon the UK's withdrawal from the EU should provide clear and transparent disclosure of the status of the UK's withdrawal efforts and the potential tax effects of an eventual withdrawal. Such disclosure should include a description of the UK withdrawal event, the nature of the entity's activities that could be affected, and the potential income tax accounting impact.

It is our understanding that the SEC staff would not object to this approach.

What's next?

Entities that may be materially affected by the UK's withdrawal from the EU should continue to monitor the status of tax law changes and tax treaty negotiations at the UK, EU, and individual EU Member State levels.

Questions?

PwC clients who have questions about this *In brief* should contact their engagement team. Engagement teams who have questions should contact the National Professional Services Group.

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