

**MEMO# 20680**

December 13, 2006

# **ICI Requests Delay in Accounting Pronouncement Regarding Uncertain Tax Positions**

©2006 Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice. [20680] December 13, 2006 TO: BOARD OF GOVERNORS No. 30-06 INVESTMENT COMPANY DIRECTORS No. 29-06 PRIMARY CONTACTS - MEMBER COMPLEX No. 21-06 ACCOUNTING/TREASURERS MEMBERS No. 27-06 TAX MEMBERS No. 45-06 SEC RULES COMMITTEE No. 53-06 RE: ICI REQUESTS DELAY IN ACCOUNTING PRONOUNCEMENT REGARDING UNCERTAIN TAX POSITIONS Attached is an important letter from Institute President Paul Stevens to Chairman Christopher Cox of the Securities and Exchange Commission (the "SEC") and Chairman Robert Herz of the Financial Accounting Standards Board (the "FASB") regarding an accounting pronouncement governing uncertain tax positions. The letter requests that the FASB or the SEC delay application of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes ("FIN 48"),<sup>1</sup> to investment companies until supplemental written guidance is provided. FIN 48, which applies to all companies that follow generally accepted accounting principles, mandates a two-part test for recognition of a tax benefit in a company's financial statements. First, the company must determine whether it is more likely than not (i.e., a likelihood of more than 50 percent) that its tax position will be sustained upon examination, including resolution of any related appeals or litigation, based on the technical merits of the position. If a tax position satisfies this threshold, the company must then determine the amount of benefit that may be recognized in the financial statements by considering all the potential outcomes and measuring the probability that each will occur. FIN 48 is effective for fiscal years beginning after December 15, 2006. <sup>1</sup> See Institute Memorandum (20183) to Accounting/Treasurers Members No. 14-06, Tax Members No. 24-06, and Advisor Distributor Tax Issues Task Force No. 8-06, dated July 14, 2006. <sup>2</sup> The Institute has been in discussions with the FASB and the SEC for over a year to ensure that FIN 48 applies appropriately to funds.<sup>2</sup> FIN 48 uniquely affects mutual funds because the two-part test must be applied each day when a fund's net asset value is calculated. As a result, fund share prices could be inaccurate if FIN 48 requires a fund to recognize tax liabilities that the fund will not be required to pay. This may occur when: • Tax is not paid based on IRS administrative practices; • Tax is paid by another party; or • No tax liability will be incurred for reasonable positions taken in fiscal years prior to the effective date of FIN 48. To resolve these issues, the Institute's letter proposes that mutual funds be allowed to disclose potential tax liabilities under FIN 48 in footnotes to their financial statements. Thus, such liabilities would not be recognized in the daily NAV calculations or on the balance sheet. Alternatively, the FASB or the Commission should issue guidance that: • Expands the

factors that may be considered by mutual funds in determining whether a tax benefit may be recognized; • Provides relief for situations in which a mistake is made, giving rise to a potential tax liability, but for which another party is expected with reasonable certainty to pay the tax; and • Does not apply FIN 48 to positions taken on tax returns prior to the effective date of the interpretation, unless it is probable that the fund will pay the tax. In addition, the letter requests that the application of FIN 48 to investment companies be delayed until such written guidance is provided. For additional information, please contact the undersigned (202/326-5815 or [ekrentzman@ici.org](mailto:ekrentzman@ici.org)), Keith Lawson (202/326-5832 or [lawson@ici.org](mailto:lawson@ici.org)), Greg Smith (202/326-5851 or [smith@ici.org](mailto:smith@ici.org)), or Karen Lau Gibian (202/371-5432 or [kgibian@ici.org](mailto:kgibian@ici.org)). Elizabeth Krentzman General Counsel Attachment (in .pdf format) Note: Not all recipients receive the attachment. To obtain a copy of the attachment, please visit our members website (<http://members.ici.org>) and search for memo 20680, or call the ICI Library at (202) 326-8304 and request the attachment for memo 20680. 2 See Institute Memorandum (19148) to Accounting/Treasurers Members No. 17-05 and Tax Members No. 24-05, dated September 12, 2005; see also Institute Memorandum (20061) to Accounting/Treasurers Members No. 11-06 and Tax Members No. 17-06, dated May 23, 2006.

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