

Interpretation of the Emerging Accounting Issues Working Group

INT 00-22: Application of SSAP No. 10 to Admissibility of Deferred Tax Assets

ISSUE NULLIFIED BY SSAP NO. 101

INT 00-22 Date Discussed

June 12, 2000; September 11, 2000

INT 00-22 References

SSAP No. 10—Income Taxes (SSAP No. 10)

INT 00-22 Issue

1. SSAP No. 10, paragraph 10.a., provides that a reporting entity may admit deferred tax assets (DTAs) in an amount equal to federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse by the end of the subsequent calendar year. The NAIC staff have received several inquiries as to the practical application of this admissibility guidance.

2. The primary question that arises is whether or not the reporting entity is required to project a tax net operating loss (NOL) for future periods before admitting any DTAs in accordance with paragraph 10.a. Interpreted literally, it appears the reporting entity is required to estimate a tax NOL for the subsequent tax year. However, the following practical application concerns arise when estimating a tax NOL:

- a. An entity may not be able to estimate their tax NOL or tax obligation for the subsequent tax year. While taxable entities currently estimate their tax on a quarterly basis to ensure proper quarterly tax payments are made to the Internal Revenue Service, the entity may not be able to reasonably estimate the annual tax.
- b. An entity will be able to admit the same amount of DTA for loss carrybacks pursuant to paragraph 10.b.i. of SSAP No. 10, provided the entity is not limited to the ten percent of statutory capital and surplus described in paragraph 10.b.ii.
- c. It is uncertain whether or not the benefit of estimating a tax NOL for the subsequent tax year will exceed the costs involved (i.e., subjectivity in estimates) in performing the estimation.

INT 00-22 Discussion

3. The working group reached a consensus that paragraph 10.a. of SSAP No. 10 does not require a reporting entity to project a tax NOL for future periods. Rather, the reporting entity may admit DTAs equal to the amount of taxes paid in prior years (the tax years before the NOL year) that can be recovered through loss carrybacks for existing temporary differences that reverse by the end of the subsequent calendar year, regardless of whether or not the reporting entity anticipates a tax NOL in the following tax year. Generally, the reporting entity must carry back the entire amount of the NOL to the applicable tax years before the NOL year (the carryback period), and then carry forward any remaining NOL (the carryforward period). The reporting

entity can, however, choose not to carry back an NOL and carry it forward only. The NOL year is the year in which the NOL occurred. The reporting entity cannot deduct any part of the NOL remaining after the carryforward period. This interpretation is illustrated as follows:

Assumptions:

- (1) ABC Company paid Year 2001 taxes in the amount of \$300,000. The entire \$300,000 may be carried back pursuant to the two year carryback period provided by the current IRS provisions. Year 2001 was the first year in which the company paid income taxes. The company does not expect to generate a tax NOL in 2002.
- (2) ABC Company has \$10,000,000 of gross DTAs at 12/31/01, \$2,000,000 of which is expected to reverse by 12/31/02. The \$2,000,000 is significantly less than 10% of the company's adjusted capital and surplus.
- (3) ABC Company has \$8,000,000 of gross deferred tax liabilities (DTLs) at 12/31/01.

ABC Company will admit the following DTAs at 12/31/01 pursuant to SSAP No. 10:

Paragraph 10.a.	\$ 300,000	(Taxes paid in prior year which are eligible for NOL carryback.)
Paragraph 10.b.	1,700,000	(\$2,000,000 worth of DTAs reversing in 2002 less \$300,000 from paragraph 10.a.)
Paragraph 10.c.	<u>8,000,000</u>	(Amount of DTAs offset against existing DTLs.)
Total	\$10,000,000	

INT 00-22 Status

4. No further discussion is planned.