

FASB Emerging Issues Task Force

Issue No. 06-3

Title: How Sales Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross Versus Net Presentation)

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References:

FASB Statement No. 19, *Financial Accounting and Reporting by Oil and Gas Producing Companies* (FAS 19)

FASB Statement No. 109, *Accounting for Income Taxes* (FAS 109)

FASB Concepts Statement No. 6, *Elements of Financial Statements* (CON 6)

EITF Issue No. 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent" (Issue 99-19)

EITF Issue No. 00-10, "Accounting for Shipping and Handling Fees and Costs" (Issue 00-10)

EITF Issue No. 01-14, "Income Statement Characterization of Reimbursements Received for 'Out-of-Pocket' Expenses Incurred" (Issue 01-14)

International Accounting Standard 18, *Revenue* (IAS 18)

*** The alternative views presented in this Issue Summary are for purposes of discussion by the EITF. No individual views are to be presumed to be acceptable or unacceptable applications of Generally Accepted Accounting Principles until the Task Force makes such a determination, exposes it for public comment, and it is ratified by the Board.**

Background

1. Taxes are assessed by various governmental authorities on all kinds of transactions. These taxes range from sales taxes that are applied to a broad class of transactions involving a wide range of goods and services to excise taxes that are applied only to specific types of transactions or items. The characteristics of how these different types of taxes are calculated, remitted to the governmental authority, and administered are numerous and therefore very difficult to summarize into simple discernible models. In many industries, general practice has developed on the presentation of these various taxes in the financial statements.

2. In March 2002, the Chief Accountant of the SEC offered the SEC staff's view on the treatment of franchise taxes in the cable industry (see paragraph 15 below). At that time, the chief accountant stated in the minutes to the SEC Regulations Committee that "the SEC staff believes that such fees should be shown gross versus net of revenue in the income statement." Since that time, the SEC staff has received inquiries on how to present various types of taxes in the income statement. At the 2005 AICPA National Conference on Current SEC and PCAOB Developments, an SEC staff member noted that a specific kind of inquiry that the staff had repeatedly received was the impact of changes in the party responsible for paying state and local sales taxes on income statement presentation. Specifically, the inquiries were directed at determining the impact on income statement presentation of vendors rather than on customers bearing the incidence of sales taxes. That staff member noted that the staff had historically addressed the income statement presentation of pass through taxes by reference to Issue 99-19 and Issue 01-14 and noted that consideration of such guidance continues to be appropriate.

3. The Issue originally considered by the EITF Agenda Committee for addition to the EITF agenda, was concerned with providing clarifying guidance on how to present sales taxes in the income statement.

4. The following examples of the various taxes paid on goods and services is intended to provide a general background on how sales taxes and other types of taxes are calculated and administered along with some background information on specific industries that have, aside from income taxes, a significant number of other taxes assessed on their transactions. It is not

intended to be an exhaustive list of all taxes that are assessed by various governmental authorities. Rather, it is designed to provide the Task Force with a general understanding of the breadth and complexity of the types of taxes that may be within the scope of the issue.

Sales Tax

5. Sales taxes are assessed by a governmental authority on the purchase of goods and services. These taxes are assessed on each individual transaction as they occur and are calculated by multiplying the retail sales price of each transaction by a statutorily determined percentage. The amount of sales taxes assessed is typically displayed separately on the invoice or sales receipt provided to the customer. Depending on the jurisdiction, certain classes of products and services (for example food items) are exempt from sales tax. Current practice is that the vast majority of entities report sales taxes on a net basis in the income statement. Forty-five states, the District of Columbia, and another 7,400 local jurisdictions assess sales taxes on the purchase of goods and services that occur within their jurisdictions. The responsibility for the collection of sales taxes is generally divided into two types of jurisdictions; customer levy jurisdictions and seller privilege jurisdictions.

6. Customer-Levy Jurisdiction—The customer is generally responsible for paying sales tax in a customer levy jurisdiction. Typically, the sales tax is explicitly required by statute to be separately displayed on the customer's invoice to enable the customer to determine how much sales tax is being paid for the transaction. The taxes are collected by the seller at the point of sale and remitted to the governmental authority within a prescribed time period. If a governmental authority conducts an audit of the sales tax records of the seller and uncovers a deficiency in the amount of sales tax collected, the governmental authority is legally entitled to recover this deficiency from the customer based on the legal statute in that customer-levy jurisdiction. As a practical matter, the governmental authority will typically recover the deficiency from the seller, unless the sale is related to a large-dollar item (for example, an automobile).

7. Seller-Privilege Jurisdiction—The seller of the goods and services is responsible for paying sales tax in a seller-privilege jurisdiction. In some jurisdictions the seller is required to

separately display the sales tax on the invoice to inform the customer of the amount of sales tax that is being assessed on the purchase of the goods or services. However, the statutes in some states do not clearly define who has responsibility for collecting the tax or even what the intent of the tax is. Consider the difficulties in evaluating the tax statutes for the state of Alabama. Section 40-23-2 of the Alabama Tax Code levies a privilege tax against the person on account of the business activities in which that person is involved and in an amount to be determined by the application of rates against gross sales or gross receipts as the case may be. Section 40-23-26 states that all taxes paid shall conclusively be presumed to be a direct tax on the retail consumer, precollected for the purpose of convenience and facility only. Finally, Section 40-23-67 requires the seller to collect the tax and states that it is unlawful for the seller to state that the tax will be assumed or absorbed by the seller or that it will not be added to the selling price of the goods or services purchased. This same section goes on to state that the tax that is required to be collected by the seller shall constitute a debt owed by the seller to the state of Alabama. This example provides an illustration of the confusion that can occur when trying to understand which party is the primary obligor.

8. Issues concerning who is responsible for the tax and what the intended purpose of the tax is are not just limited to state jurisdictions. Each local jurisdiction can have its own set of statutes, and those statutes may not be consistent with the statutes of their own state jurisdictions.

Use Tax

9. Use taxes are assessed at the state and local levels for the sale of goods and services that are initiated out of state. Use taxes are assessed on the end-customer. However, in some circumstances the use tax is required to be collected by the seller. Use tax statutes were enacted in the 1930's because the U.S. Supreme Court ruled that it was illegal for a state to require an end-customer to pay "sales tax" on a sale that occurred outside that state's jurisdiction. Frequently, use taxes that are collected by the seller are displayed on an invoice as a sales tax in order to avoid confusion to the end-customer. Use tax rates are generally applied at the same tax rate as the applicable sales taxes and are typically displayed on a net presentation basis in the seller's income statement.

Excise Tax

10. Excise taxes are taxes that are assessed on specific types of transactions involving certain products and services. At the federal level, these taxes are assessed by the Department of the Treasury through either the Internal Revenue Service (IRS) or the Alcohol and Tobacco Tax and Trade Bureau (TTB) depending on the type of transaction. The TTB is responsible for excise taxes on the sale of alcohol, firearms and ammunitions, and tobacco, and the IRS is responsible for all other excise taxes. Additionally, state and local jurisdictions will assess excise taxes on transactions involving a number of different types of products and services including alcohol and tobacco.

11. Consistent with sales and use taxes, state and local excise tax statutes are not always consistent with the federal excise tax statutes. Excise taxes are assessed in a number of different manners including those based on the volume of a commodity produced or purchased (for example, the number of barrels of alcohol), the number of transactions (for example, the number of airline passengers), or the selling price of the product (for example, the sales prices of the components of a tractor semi-trailer, including the tractor bodies and semi-trailer chassis). General practice in the U.S. is that preparers and users believe that an excise tax is a tax on the producer or provider of the goods or services and not on the end-customer.

12. SEC Rule S-X 05-3 requires that if excise taxes are greater than 1 percent of revenues and are presented gross in the income statement, the amount of excise taxes paid should be disclosed on the face of income statement.

Value Added Tax

13. A value added tax is a tax assessed on the sale of goods and services. In some countries a value added tax is referred to as a goods and services tax. A value added tax is an important funding source for many countries in Europe, Africa, and Asia. A value added tax is typically applied to a broad range of products. A value added tax represents a tax on the sale of the products or services to the end-customer. Paragraph 18 of IAS 18 requires that value added taxes should be presented on a net basis in the income statement.

Examples of Taxes in Certain Industries

14. Oil and Gas Industry—The oil and gas industry is required to pay numerous excise taxes (see above) on its products, sales taxes (see above) on sales in company-owned retail stores, and severance or production taxes. Severance taxes are federal taxes assessed when a raw material is removed from the ground. FAS 19, paragraph 24(e), states that severance taxes are required to be included in production costs. Entities in the oil and gas industry generally present all taxes on a gross basis, including sales taxes, regardless of who is obligated to pay the tax. The FASB staff believes that there is diversity in practice in the oil and gas industry as to the level of disclosure that is included in the footnotes to the financial statements on how taxes are presented and the amount of taxes include in revenue.

15. Gaming & Entertainment Industry—The entities in this industry are assessed a significant number of taxes including sales taxes on goods and services sold in their hotels and shops, taxes on their hotel rooms, and taxes on entertainment offered in their hotels. Additionally, there are principally three types of taxes that are specific to the gaming industry; a federal tax per gambling unit (for example a flat tax on each slot machine), a tax on the casino's net cash winnings (referred to as the "Gross Wagering Tax"), and a tax paid on each person entering the casino (typically for riverboat casinos). The largest of these taxes is the Gross Wagering Tax. The gambling-specific taxes are generally presented on a gross basis in the income statement.

16. Cable Industry—There are principally two taxes that are presented on a customer's invoice for cable services; a sales tax and a franchise tax. The sales tax is calculated based on the price of the services provided to a customer and presented net in the cable company's income statement. The franchise tax is a tax assessed by a local municipality that the cable operator is allowed, but not required, to pass directly on to its customers. The franchise tax generally is passed on to the customers but, in some situations, it is not passed on because of competition from satellite cable providers or other media suppliers. The cable industry presents the franchise tax on a gross basis in the income statement (see paragraph 2 above).

17. Airline industry—The airline industry is subject to a number of different taxes at different points in the delivery of the service to the end-customer and specific taxes on the sale of the

airline ticket to the end-customer. For example, the airline is subject to an excise tax on every gallon of jet fuel used. The taxes that are assessed on the delivery of the service to the end customer are presented on a gross basis. An airline is assessed a number of taxes on the sale of the airline ticket to the end-customer including the Air Transportation Taxes (AT tax), Federal Security Surcharge (flat fee per passenger), and Airport Passenger Facility Charge (flat fee per passenger). The AT tax includes, but is not limited to, the Federal Ticket Tax (7.5 percent of the ticket price), and the Federal Flight Segment Tax (flat fee per segment). All of the taxes assessed on the sale of the ticket to the end-customer are federally imposed taxes. The airlines are required to remit the taxes when the taxes are collected, but do not recognize revenue until the ticket is used by the end-customer. There can be a several month lag between the time the taxes are remitted and the revenue is recognized by the airline. The AT tax is a trust fund taxes which means that the seller is holding the money in trust for the government until the taxes are remitted. The taxes assessed on the sale of a ticket to an end-customer are presented on a net basis.

Scope

18. This Issue is not intended to readdress the accounting models in Issue 99-19, Issue 00-10, and 01-14 but, rather, the applicability of these models to the presentation of various taxes in the income statement.

Accounting Issues and Alternatives

19. Although the EITF Agenda Committee was originally requested to consider adding an issue on the presentation of sales taxes in the income statement to the EITF agenda, the FASB staff believes the EITF should consider whether or not the Issue should address other types of taxes not subject to FAS 109 as well.

Issue 1: Whether the scope of this Issue should include (a) all nondiscretionary amounts assessed by governmental authorities, (b) all nondiscretionary amounts assessed by governmental authorities in connection with a transaction with a customer, or (c) only sales, use, and value added taxes.

View A: The scope of this Issue should include taxes that are externally imposed on a revenue producing transaction between a seller and a customer or on the activities of the seller (the production process) that are ultimately used in a revenue producing transaction with a customer.

20. Proponents of View A believe that the scope of this Issue (and, accordingly, any consensus reached) should be applied broadly. These proponents believe that the consensus reached in this Issue should be applied broadly regardless of whether the tax is on a revenue producing transaction or on the production process. These proponents believe that there is no conceptual reason to restrict the scope because all taxes should be subject to the same presentation requirements. These proponents believe that if the scope is restricted to a specific class of taxes, then preparers will either request that additional guidance should be provided or analogize to the guidance in this Issue regardless.

21. Some proponents of View A also believe that defining taxes very broadly allows for the scope of the issue to convergence with international standard setters. Paragraph 8 of IAS 18 requires taxes to be reported in the following manner:

Revenue includes only the gross inflows of economic benefits received and receivable by the entity on its own account. Amounts collected on behalf of third parties such as sales taxes, goods and services taxes and value added taxes are not economic benefits which flow to the entity and do not result in increases in equity. Therefore, they are excluded from revenue.

22. Opponents of View A believe that there is actual diversity in current practice in the application of the scope of IAS 18. They believe that this diversity exists because entities have difficulty determining what taxes are in the scope of IAS 18, such as excise taxes. For example, some excise taxes are reported net because they are viewed to be within the scope of IAS 18 while other excise taxes that have similar characteristic are reported gross because they are determined to be outside the scope of IAS 18. The diversity exists because some preparers have concluded that since paragraph 8 of IAS 18 does not explicitly mention excise taxes, then a company can/should present excise taxes gross. This diversity in applying IAS 18 supports their claim that defining the scope of the issue broadly does not work in practice and it is impractical

to develop relevant characteristics that will be understood by preparers, users, and regulators alike.

View B: The scope of this Issue should include taxes that are externally imposed on a revenue producing transaction between a seller and a customer.

23. Proponents of View B believe that this Issue (and, accordingly, any consensus reached) should be applied to taxes on revenue producing transactions between a seller and a customer and not taxes that are applied to the production process. These proponents believe that taxes applied during the production process should be considered a component of the cost of the inventory or the cost of providing the service. Proponents of View B believe that from the customer's perspective, when a tax is assessed by a seller on a transaction between the seller and customer, the seller is always acting as an agent for the governmental authority.

24. Proponents of View B also believe that the standards setters have previously concluded that taxes on the production process should be included as a component of the cost of inventory. For example, severance taxes in the oil and gas industry are included in the cost of the inventory in accordance with FAS 19.

25. Opponents of View B believe that supporting View B presupposes a conclusion that taxes assessed during the production process should be presented gross. Opponents of View B believe that drawing a distinction in the accounting basis on when the tax is assessed fails to reflect the economic substance on the transaction between the governmental authority and the seller or customer. These opponents believe that a governmental authority's election to assess the tax on the production of the product or service and not on the sale is frequently a matter of convenience for the governmental authority or a desire of the governmental authority to have the taxes remitted on a timelier basis.

View C: The scope of this Issue should include only sales, use, and value added taxes. The common characteristics of these types of taxes are that they are imposed at one rate on the retail sale of a broad range of classes of items, but not necessarily every item. The fact that sales taxes

do not apply to some or all food, clothing, medical supplies, and motor vehicles should be disregarded for the purpose of making a determination of the scope of this Issue.

26. Proponents of View C believe that this Issue (and, accordingly, any consensus reached) should be applied narrowly to sales, use, and value added taxes (collectively, "sales taxes"). This Issue was first presented to the Task Force in the context of sales taxes and the Task Force should limit its discussions to those fact patterns. Proponents of View C believe that expanding the Issue to include all taxes would significantly change/expand the scope of the project and potentially require a different accounting model for each type of tax. Proponents of View C also believe that expanding the scope to all taxes would potentially change the definition of revenue and therefore should be dealt with within the context of the Board's revenue recognition project.

27. Proponents of View C acknowledge that this Issue was first raised in the context of the franchise tax in the cable industry; however, this Issue is a significant issue for all entities in the context of reporting sales taxes. Proponents of View C believe that this Issue should be limited to sales taxes because of the difficulties encountered in assessing all of the other unique characteristics of other types of taxes.

28. Opponents of View C believe greater diversity in practice will result if the Task Force limits the scope of this Issue because taxes with similar economic characteristics will be presented differently. For example, an excise tax on air transportation is considered to be a tax on the end-customer similar to a sales tax. It is applied to the sales price of the ticket, is the responsibility of the customer, and is a non-discretionary tax. However, if the scope is limited to sales taxes, opponents of View C believe that this excise tax and related sales taxes could be presented differently in the financial statements. Additionally, opponents of View C believe that preparers and auditors will have difficulty determining whether they should analogize to either Issue 99-19 or the consensus reached in this Issue in determining how to present other types of taxes in the financial statements that are not specifically addressed in this Issue.

Issue 2: How taxes assessed by a governmental authority, within the scope as determined by Issue 1, should be presented in the income statement (that is, gross versus net presentation).

View A: Taxes by a governmental authority should be presented on a net basis.

29. Proponents of View A believe that taxes assessed by a governmental authority should be recorded on a net basis. Proponents of View A believe that the taxes imposed by governmental authorities are non-discretionary costs that are usually passed through by the seller to the end-customer and reduce the amount of revenue otherwise available to cover the company's expenses. Those holding this view believe that financial statements are not enhanced (that is, neither relevance nor comparability is improved across financial statements) by a practice of accounting for taxes on a jurisdiction-by-jurisdiction basis, resulting in mixed accounting presentation for economically similar transactions.

30. Proponents of View A believe that this represents an opportunity to converge with existing international accounting standards. Paragraph 8 of IAS 18 requires that all taxes collected on behalf of a third party be presented net because these taxes "are not economic benefits which flow to the entity and do not result in increases in equity." Because IAS has a different model for presenting taxes, comparability between U.S GAAP preparers and IAS preparers is currently limited.

31. Proponents of View A also believe that including a portion of the taxes on a gross basis in revenue is inconsistent with the definition of revenue in CON 6, paragraphs 78 and 79. Paragraph 78 states the following:

Revenues are inflows or other enhancements of assets of an entity or settlements of its liabilities (or a combination of both) from delivering or producing goods, rendering services, or other activities that constitute the entity's ongoing major or central operations.

These proponents believe that those activities do not constitute an entity's major or central operations. Rather, the transactions are the governmental authority's way of funding its operations, influencing an entity's or an individual's behavior, or providing services to the end-customer.

32. Opponents of View A believe that for taxes other than "sales taxes," View A would represent a substantial change in practice that would not improve financial reporting in such a manner that would justify the costs. A number of industries report taxes on a gross basis, such as excise taxes, and they believe that an entity would have to make a number of system changes in order to comply with View A. These opponents believe that presenting taxes net would not reflect the economic substance of the transactions because many of these taxes are not passed through to the customer but, rather, are a cost of producing the product or service.

View B: The taxes assessed by a governmental authority should be presented in the income statement based on an evaluation of the criteria in Issue 99-19 for determining whether the seller is acting as a principal or an agent.

33. Proponents of View B believe that preparers should use the criteria in Issue 99-19 for determining how to present taxes in the income statement. These proponents believe that Issue 99-19, Issue 00-10, and Issue 01-14 are the principle authoritative literature on gross versus net presentation. They believe that the evaluation of the gross versus net indicators in the tax fact pattern will focus on the primary obligor criterion as the other criteria are not specifically relevant to determining how to present taxes in the income statement. Tax collections would be recorded as revenue on a gross basis with the corresponding sales tax payment being recognized as an expense in those jurisdictions where the governmental authority is levying the tax on the seller (that is, the seller is the primary obligor). In those jurisdictions where the seller is acting as the collection agent of the governmental authority (that is, the customer is the primary obligor), the tax collections would be recorded net in revenue.

34. Some opponents of View B believe that preparers should not analogize to Issue 99-19, which provides guidance on how to present revenue in a transaction between a seller and an end-

customer. They believe that the arrangements in Issue 99-19 are arm's length transactions between a seller and a customer. These opponents believe that taxes assessed by a governmental authority are based on a legal requirement imposed on the seller and/or the customer and therefore should not be subject to the same criteria as the transactions within the scope of Issue 99-19. They believe that the criteria in Issue 99-19 are not always appropriate in this circumstance because they frequently do not reflect the economic substance of the transaction, and any reliance on the legal structure could result in a conclusion that is not appropriate.

35. Some opponents of View B believe that requiring presentation of taxes based on who the primary obligor is possesses some significant operational issues, principally relative to sales and use taxes. As discussed above, there is diversity in how states and local municipalities administer the sales tax and use tax statutes. Some jurisdictions are seller-privilege jurisdictions while others are customer-levy jurisdictions. Additionally, as noted in paragraph 7 (the Alabama example), it is not always clear to sellers how to determine who is the primary obligor in those arrangements.

36. Some opponents of View B believe that requiring companies to treat taxes on a gross basis in those jurisdictions where the statutes consider the seller to be the primary obligor also requires companies to evaluate and monitor tax laws for every jurisdiction in which they operate. There are estimated to be as many as 14,000 different tax jurisdictions globally. While not only burdensome for the individual companies, such a requirement would result in there being a significant risk that individual companies would not all reach consistent legal interpretations in identifying the primary obligor or in determining whether a particular tax in a particular jurisdiction is within the scope of this Issue.

37. Some opponents of View B also note that the key financial metrics used by many retail companies for decades are all based on sales excluding the impact of sales and use taxes. Expense ratios as a percentage of revenues, same store "comp" sales, and sales per square foot each represents measures that organizations use throughout their operational and financial groups to measure results and profitability. These measures are communicated to the public and other applicable constituents to provide an understanding of how the business is performing. A change

in the treatment of accounting for sales and use taxes, especially if not consistently applied industry-wide because of jurisdiction by jurisdiction conclusions on primary obligor determinations, could significantly distort these measures and affect comparability.

38. The FASB staff solicited feedback from various preparers on the cost benefit of View B. The preparers expressed concern with the cost of applying View B in Issue 2, even if the scope was limited to only sales taxes. The preparers who were queried on View B noted that it would be an extremely difficult task to analyze the tax attributes of each tax jurisdiction to determine who the primary obligor was. In the U.S. alone there are over 7,400 state and local jurisdictions. For an entity that has significant international operations, the number of jurisdictions could be as many as 14,000.

View C: The taxes assessed by a governmental authority should be presented in the income statement based on an evaluation of specific criteria for determining gross versus net presentation.

39. The FASB staff believes that View C is only applicable if the Task Force selects View A in Issue 1.

40. These proponents believe that taxes should be presented in the income statement after considering specific criteria for determining gross versus net presentation. Proponents of View C agree with proponents of View B that taxes with the same economic characteristics should have the same presentation requirements; however, they disagree with proponents of View B that the criteria in Issue 99-19 are the appropriate criteria to use in evaluating gross versus net presentation. Proponents of View C believe that sellers should focus on the economic substance of the tax in determining how to present the taxes within the financial statements.

41. Proponents of View C believe that the following criteria should be considered in determining whether a seller should report taxes on a gross or a net basis:

What is the nature of the tax?

42. A seller should evaluate the nature of the tax in order to determine if the tax should be reported on a gross or net basis. If the tax is assessed on the production process that would indicate that the nature of the tax is a tax on the seller and should be presented on a gross basis. Conversely, if the tax was assessed on a revenue producing transaction, that would indicate the tax was a tax on the end-customer and it should be reported net. However, if this tax represented a tax on all gross receipts (including, for example, investment income), this would indicate that it should be presented on a gross basis.

Is the seller subject to financial exposure or obligation as a result of the tax?

43. If the seller is responsible for the tax regardless of whether a transaction is completed with the end-customer, then this would be an indication that the seller is subject to financial exposure or obligation as a result of the tax and that the seller should record the tax on a gross basis. If the seller is able to get a refund of any taxes remitted to a governmental authority in the event that the transaction with the end-customer ultimately is written off as a bad debt, this is one indication that the seller is merely acting as an agent and should record the tax on a net basis. Another indication of whether the seller is subject to financial exposure or obligation as a result of the tax is by considering what effect a change in the tax rate or other terms of the statute would have on the pricing and/or margin of the product or service. For example, if Connecticut raises the general sales tax, a seller in Connecticut would not have to modify its pricing to pass along the tax to the customer or recover its margin on the product. This would be an indicator that the seller should report its tax on a net basis. However, if Connecticut were to raise the excise tax on alcohol, a seller would have to raise its prices in order to recover the increased tax and maintain its margin on the product or service, which would be an indicator that the seller should report it on a gross basis.

From the customer's perspective, is the tax a tax on the transaction or a tax on the seller?

44. The seller should evaluate how the customer views the tax and whether the customer believes that the tax is a tax on the seller or a tax on their transaction. If the invoice or receipt separately states the amount of tax that is being paid, then this is an indication that the customer would believe this is a tax on the transaction and should be presented on a net basis. However, if

the customer is not aware of the tax or the amount of the tax is never presented to the customer, then this should be considered a tax on the seller and presented on a gross basis. For example, when a customer purchases a bottle of wine, the invoice frequently includes any sales taxes, but does not include any excise taxes. This is an indication that the sales tax is a tax on the transaction and should be presented net, while the excise tax is a tax on the seller and should be presented gross.

45. Proponents of View C believe that none of the indicators should be considered to be presumptive or determinative; however, the relative strengths of each indicator should be considered.

46. Opponents of View C do not support View C for the same reason that opponents of View B do not support View B. Opponents of View C also believe that these criteria will allow an entity to structure the arrangements with the end-customer to achieve a presentation basis that is most favorable to the seller. These opponents believe that this will add to the complexity of the accounting literature and that this Issue is not viewed as a significant accounting and reporting issue in the financial community by preparers and users of the financial statements. They believe it will have the same operational and cost benefit concerns as discussed in paragraphs 36 and 38 of View B.

View D: A company may adopt a policy of presenting taxes assessed by a governmental authority on either a gross basis or a net basis. If taxes are significant, a company should disclose its policy of presenting taxes in the accounting policy section of the notes to the financial statements. In addition, if taxes are significant and are not presented net, a company shall disclose the amounts of such taxes that are recognized on a gross basis.

47. Proponents of View D believe that industry practice for presenting taxes either net or gross has been well established and View D would allow for these practices to continue unchanged. These proponents believe that the cost of implementing accounting guidance in any other manner than what is proposed by View D would clearly outweigh the benefits. Proponents of View D believe that making a determination of the legal obligor can be difficult because the statutes in

each jurisdiction can be interpreted differently. Proponents of View D also believe that this would be consistent with Issue 2 of Issue 00-10 because it would allow for a company to make an accounting policy election and disclose the effect of that election if it was material.

48. The FASB staff solicited feedback from several analysts, who are members of the FASB's Investor Task Force (ITF), regarding the presentation of taxes in a company's financial statements. These analysts believe that no change in the current industry practice is justified from a cost benefit basis. They note that any change would result in significant costs to shareholders with little incremental benefit. They believe, however, that any additional disclosures would not require a significant amount of effort by the entity and would help ensure comparability among industries.

Transition

49. The staff believes that upon application of the consensus, comparative financial statements for prior periods should be reclassified to comply with the classification guidelines of this Issue. If it is impracticable to reclassify prior-period financial statements, disclosure should be made of both the reasons why reclassification was not made and the effect of the reclassification on the current period. This transition guidance is consistent with the transition guidance previously required in Issue 99-19, Issue 00-10, and Issue 01-14.

Effective Date

50. The FASB staff's recommendation is that the consensus in this Issue should be effective for periods beginning after December 15, 2006, with early application of this guidance permitted.