BDO BULLETIN

ONE BIG BEAUTIFUL BILL ACT: IMPLICATIONS FOR ACCOUNTING FOR INCOME TAXES

JULY 2025

SUMMARY

President Donald Trump signed the reconciliation tax bill, commonly known as the “One Big Beautiful Bill Act” (OBBBA) into law July 4, 2025, which is considered the enactment date under U.S. Generally Accepted Accounting Principles (GAAP). The legislative changes included in the OBBBA will affect income tax accounting in accordance with Accounting Standards Codification (ASC) 740, *Income Taxes*. Notable corporate provisions include the restoration of 100% bonus depreciation, the creation of new Section 174A that reinstates expensing for domestic research and experimental (R&E) expenditures, modifications to Section 163(j) interest limitations, updates to the rules for global intangible low-taxed income (GILTI) and foreign-derived intangible income (FDII), amendments to the rules for energy credits, and the expansion of Section 162(m) aggregation requirements. Refer to BDO’s **tax legislative alert** for additional analysis.

Those provisions could have important implications for the calculation of current and deferred taxes, including the assessment of valuation allowances. However, because the bill was signed after the June 30 period-end and its provisions have varying effective dates, only some changes – such as those affecting valuation allowance assessments - might affect the current year's financial statements. For calendar-year filers, there are specific disclosure considerations for their Q2 10-Q filings, as discussed below.

CHANGES IN TAX LAWS

Under ASC 740, the impact of tax law changes on taxes payable or receivable for the current year is reflected in the estimated annual effective tax rate (AETR) in the period that includes the enactment date. Adjustments to prior years’ income taxes resulting from new legislation are recognized as discrete items in income tax expense from continuing operations in the period of enactment.

For deferred taxes, the effects of tax law changes on temporary differences and related deferred taxes existing as of the enactment date are recognized as discrete items in the period of enactment as a component of income tax expense from continuing operations. Companies must make a reasonable effort to estimate temporary differences and related deferred tax amounts, including related valuation allowances, as of the enactment date. For temporary differences arising after the enactment date within the current year, the impact of the tax law change is incorporated into the AETR beginning in the first period that includes the enactment date.

BDO INSIGHTS: ACCOUNTING FOR TAX LAW CHANGES IN AN INTERIM PERIOD

We are aware of an alternative policy that allows companies to use beginning-of-year temporary differences and related deferred tax balances when evaluating the impact of tax law changes during an interim period. Companies should discuss the approach with their auditors and tax advisors.

For companies that have elected to recognize deferred taxes on GILTI, any changes in the tax law that affect GILTI deferred tax accounting must be reflected in the interim period that includes the enactment date, as discussed below. Also, companies may need to assess the impact of the expanded Section 162(m) aggregation rules on the recognition of deferred tax assets (DTAs) related to share-based compensation for covered employees.

BDO INSIGHTS: ACCOUNTING FOR RETROACTIVE CHANGES IN TAX LAWS

If a tax law change is retroactive, the accounting treatment depends on whether the impact relates to prior periods or the current year. For prior-period deferred taxes and taxes payable or receivable, the effect is recognized discretely in the period of enactment. However, if the retroactive change affects current-year taxes payable or receivable – when the effective date is before the enactment date but still within the current year – the impact is recognized through an adjustment to the AETR. The updated AETR is then applied to year-to-date ordinary income, resulting in a catch-up adjustment for taxes payable or receivable in earlier interim periods.

Companies should consider that rule when assessing the financial reporting implications of some provisions enacted in July 2025 that are retroactive to the beginning of 2025. That includes provisions such as R&E expensing, Section 163(j) limitation on interest deductions, and 100% bonus depreciation (for property acquired and placed in service after January 19, 2025).

VALUATION ALLOWANCE CONSIDERATIONS

Adjustments to valuation allowances for DTAs existing as of the enactment date are recorded as discrete items and allocated to income tax expense from continuing operations. Conversely, the expected adjustment to the valuation allowance at year-end for deductible temporary differences originating after the enactment date and related to current-year ordinary income must be incorporated into the estimated AETR.

The corporate provisions - such as the permanent restoration of 100% bonus depreciation, R&E expensing, changes to the GILTI and FDII rules, and the more favorable calculation of the interest limit under Section 163(j) - could have important effects on the determination of valuation allowances for many companies. Specifically, the updates could affect projections of future taxable income, including adjusted taxable income under Section 163(j), potentially triggering a change in judgment about the realizability of DTAs.

If tax law changes are enacted after the period ends but before financial statements are issued, changes to the valuation allowance are not recognized until the period that includes the enactment date. However, disclosure may be required, as discussed below.

BDO INSIGHTS: REASSESS THE REALIZABILITY OF DEFERRED TAX ASSETS

Before, companies might have recorded a full valuation allowance on their Section 163(j) DTA as a result of the interest deduction limitation being based on 30% of adjusted taxable income, which included amortization, depreciation, and depletion (that is, the earnings before income and taxes limitation). The reinstatement of the earnings before income, taxes, depreciation, and amortization limitation under Section 163(j) for tax years beginning after December 31, 2024, might require a reassessment of the realizability of the current-year disallowed interest deduction and Section 163(j) carryforward DTAs from prior years that were previously subject to a full valuation allowance.

INTERNATIONAL PROVISIONS

The OBBBA includes several major changes to international tax provisions. Further, it renames the FDII and GILTI provisions to “foreign-derived deduction-eligible income” (FDDEI) and net controlled foreign corporation tested income (NCTI), respectively. In this Bulletin, we use the terms “FDII” and “GILTI.”

The OBBBA introduces major changes to the FDII regime by increasing the effective tax rate from 13.125% to 14% through a permanent reduction of the Section 250 deduction from 37.5% to 33.34% – a rate still higher than what would have applied without the legislation. It also makes the FDII calculation more favorable by eliminating the reduction for qualified business asset investment (QBAI) and specifying that interest and R&E costs are not allocated to eligible income. Most FDII changes in the OBBBA are effective for tax years beginning after 2025.

The act raises the effective tax rate on GILTI by reducing the Section 250 deduction from 50% to 40%, resulting in a pre-foreign tax credit (FTC) effective rate increase from 10.5% to 12.6%. That is still lower than the rate that would apply without the act. The FTC haircut under GILTI is reduced from 20% to 10%. The OBBBA also repeals the QBAI deemed return, increasing the amount of income subject to GILTI, and narrows expense allocations for FTC purposes. Those changes are effective for tax years beginning after 2025.

The OBBBA raises the base erosion and anti-abuse tax (BEAT) rate from 10% to 10.5% for tax years beginning after 2025, which is lower than the 12.5% rate that would have applied absent the legislation. It also repeals a scheduled 2026 change that would have increased BEAT liability by the sum of all income tax credits.

For tax accounting purposes, FDII and BEAT are treated as period costs, and most companies also account for GILTI as a period cost. Because most of the OBBBA international provisions do not take effect until tax years beginning after December 31, 2025, companies will likely see an immediate accounting impact at enactment only if the law change affects their valuation allowance assessments – for example, if the changes affect future income projections used in the valuation allowance analysis.

However, companies that recognize deferred taxes for GILTI-related basis differences must remeasure those deferred tax balances at enactment if they are expected to reverse after the new law becomes effective. Further, if a company factors BEAT into its assessment of deferred tax asset realizability, it must evaluate how changes to the BEAT calculation affect its valuation allowance and recognize any impacts in the period of enactment.

ENERGY CREDIT PROVISIONS

The OBBBA significantly curtails and modifies a broad range of Inflation Reduction Act (IRA) energy tax incentives, imposes new domestic content and foreign entity restrictions, and phases out or repeals many credits in the coming years. The changes effective in 2025 could affect financial statements if companies had anticipated the impact of IRA credits in their 2025 AETR calculations for interim periods.

ACCOUNTING CONSIDERATIONS FOR UNCERTAINTY IN INCOME TAXES

Companies must assess the act’s impact, particularly in areas where the interpretation of new rules is uncertain. If a tax position expected to be taken on a tax return is not more likely than not to be sustained upon examination based on its technical merits, it must be evaluated under the recognition and measurement requirements of ASC 740 to determine the appropriate amount of tax benefit to recognize.

STATE INCOME TAX CONSIDERATIONS

Companies must assess the state and local tax effects of the OBBBA; the impact will depend on whether and how states conform to the federal tax code. State tax implications may be significant for bonus depreciation, R&E expensing, FDII, GILTI, and interest deductibility. Companies must review state conformity rules to determine the appropriate state tax effect and related tax accounting and may need to adjust state current and deferred tax balances in addition to federal balances.

FINANCIAL STATEMENT DISCLOSURES

Companies need to consider disclosing the expected effects of new tax laws in the notes to the financial statements, management's discussion and analysis, and risk factors.

If a law is enacted after the interim balance sheet date but before financial statements are issued, the tax law change would be considered a Type II nonrecognized subsequent event under ASC 855, *Subsequent Events*. In that case, companies must disclose the nature of the event and either estimate its effect (if material) or state that an estimate cannot be made. If a law is enacted during an interim period, major variations in the relationship between income tax expense and pretax income must be explained.

For annual financial statement reporting, ASC 740-10-50-9(g) requires companies to disclose the tax effects of adjustments to deferred tax liabilities or assets resulting from enacted changes in tax laws or rates in their annual financial statements. Public business entities in the U.S. need to separately disclose the effect of tax law changes in the annual effective tax rate reconciliation.

NEXT STEPS

Companies must assess the impact of the tax legislation on their income tax provision calculations, including current and deferred tax balances, the AETR, valuation allowances, and related financial statement disclosures. The analysis will likely require extensive modeling and planning because the provisions are highly interconnected. While this Bulletin highlights selected areas of income tax accounting that might be affected by the OBBBA, it is important to consider how the changes apply to specific facts and circumstances.

For further guidance, please consult BDO's resources or reach out to **BDO's Accounting for Income Taxes** group.

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