



# Accounting Brief Financial Reporting Implications of Tariffs

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## Summary

Historically, many imported goods have been subjected to tariffs, which serve to provide government income, encourage buying local by making imports more expensive, and assist in trade negotiations or retaliation against unfair practices. The recent wave of new tariffs and the increase of existing tariffs, combined with the possibility of additional reciprocal tariffs, have increased the potential impact on businesses across various industries.

Some affected entities may need to find new suppliers or adjust their supply chains to mitigate tariff impacts, while entities that cannot pass on the increased costs to consumers may find themselves at a competitive disadvantage. The evolving tariff landscape is making it difficult for some entities to plan long-term strategies. Uncertainty around tariffs has caused some to delay investment decisions as entities are unsure of future costs and market conditions.

As organizations navigate through this changing environment, it is important for members of finance, legal, compliance, operations, accounting and tax to work together to identify and assess the risks tariffs may present to the entity’s operations, financial condition and cash flows. This publication highlights some of the financial reporting implications associated with the intricacies of evolving tariffs.

## 1. Implications of evolving tariff policies

Imposition of tariffs on imported products is a long-standing governmental policy of most countries. However, recent shifts in tariff policy, including reciprocal tariffs, may potentially impact entities across industries. Potential responses to this shift include supply chain modifications, changes in pricing strategy, revised asset use and altered investment decisions. Each of these, along with their potential impact on profitability, create several financial reporting considerations.

It is important that personnel across all disciplines of potentially impacted entities work together to identify and assess the risks tariffs may present to the entity's operations, financial condition and cash flows. This publication highlights some of the financial reporting implications associated with the intricacies of evolving tariffs.

## 2. Disclosure considerations

Entities that have not yet issued their 2024 year-end financial statements should assess how to address the potential impact of tariff policy changes in required financial statement disclosures, particularly Accounting Standards Codification (ASC) 275, *Risks and Uncertainties*, and ASC 855, *Subsequent Events*. Note that while the disclosure requirements of ASC 275 and ASC 855 should be assessed separately, the considerations in their application overlap.

ASC 275 requires discussion of estimates when, based on known information available before the financial statements are issued or are available to be issued, it is reasonably possible that an estimate will change in the near term and the effect of the change will be material. While the tariff policies of economies such as the U.S., Mexico, Canada and China continue to evolve, importers of goods from countries impacted by increased tariffs should evaluate whether this situation meets the threshold for increased disclosure of risks and uncertainties. For example, importers of steel or aluminum should assess the sensitivity of accounting estimates for which raw material prices are inputs. If the entity concludes that disclosure is necessary, it should disclose the expected impact due to the change in circumstances that existed at the date of the financial statements. The disclosure should indicate the nature of the uncertainty and include an indication that it is at least reasonably possible that a change in the estimate will occur in the near term.

ASC 275 also requires disclosure of certain concentrations. Entities must disclose concentrations when they exist at the date of the financial statements, make the entity vulnerable to the risk of a near-term severe impact and are at least reasonably possible to occur in the near term. For example, if an entity imports all of its raw materials from a country subject to new or escalated tariffs, the impact of those tariffs on the entity's operations could be severe and warrant disclosure.

Even if all the conditions are not currently met, entities should monitor how tariff policies evolve and continually assess if the criteria for disclosure of concentrations under ASC 275 are met at a future date. For instance, retaliatory tariffs could impact the future sales of entities that export products subject to such tariffs, creating inventory valuation and liquidity concerns that may need to be disclosed in future accounting periods.

ASC 855 defines subsequent events as events or transactions that occur after the balance sheet date but before financial statements are issued or are available to be issued. There are two types of subsequent events:

- Events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements (i.e., recognized subsequent events).
- Events that provide evidence about conditions that did not exist at the date of the balance sheet but arose subsequent to that date (i.e., nonrecognized subsequent events).

For entities with calendar year-ends, the recently announced changes in tariff policies do not result in financial statement recognition as of or for the period ended December 31, 2024 (i.e., the tariff policy changes represent nonrecognized subsequent events).

However, some nonrecognized subsequent events may be of such a nature that they must be disclosed to keep the financial statements from being misleading. ASC 855 does not provide an explicit threshold for determining which subsequent events require disclosure. Accordingly, the decision regarding when to disclose a subsequent event is based on specific facts and circumstances, including materiality, and requires judgment. For those events determined to be of such significance that disclosure is required, an entity should disclose:

- The nature of the event
- An estimate of the financial effect or a statement that such an estimate cannot be made

Entities should carefully monitor the evolving tariffs landscape to assess the impact on their operations, liquidity and financial reporting requirements. Recent developments treated as nonrecognized subsequent events as of December 31, 2024, may require recognition in interim financial statements issued during 2025 or, at a minimum, require disclosure in subsequent reporting periods to keep the financial statements from being misleading.

## 2.1 SEC reporting considerations

Under Item 105 of Regulation S-K, United States Securities and Exchange Commission (SEC) registrants are required to discuss the material factors that make an investment in the registrant risky or speculative. They must concisely explain how each risk affects the registrant (or the securities being offered) and present entity-specific discussion of the nature of the risks that they face, rather than providing boilerplate disclosures.

Many registrants included a discussion of potential impacts of tariffs as risk factors in their most recent annual reports on Form 10-K. Such risks included increased material cost, declining profitability, operational disruption and potential retaliatory actions. As tariff policies and their impact become clearer, registrants should continually review their Item 105 disclosures and update these disclosures in future SEC filings.

To date, far fewer registrants have addressed the potential impact of tariff policy changes as part of their management discussion and analysis (MD&A) disclosures under Item 303 of Regulation S-X. However, as tariff policies and their related effects become known, it is likely that they will impact some registrants' liquidity and capital needs, results of operations, and critical accounting estimates. As with Item 105 disclosures, registrants should continually monitor the impact of trade policy decisions, assess their impact on their operations and adjust their MD&A discussions in future filings to reflect any changed circumstances in these areas due to tariff policy implementation.

## 3. Accounting considerations

As new tariff policies are implemented, entities with significant import or export activity subject to those tariffs are likely to see impacts to their cost structure and revenue streams, which may impact the inputs to models used to develop various accounting estimates under accounting principles generally accepted in the U.S. The following sections address some potential accounting implications of the changing tariff policies. The list is not meant to be comprehensive.

### 3.1 Revenue Recognition

Entities use estimates extensively when applying ASC 606, *Revenue From Contracts With Customers*. Updated assumptions due to changes in tariff policy may impact estimates used when entities recognize revenue at a point in time under ASC 606, such as with estimates of variable consideration and standalone selling price (SSP). For instance, entities may increase the standalone selling prices of products that are also sold in a bundle, resulting in the need to reassess SSP when applying the ASC 606 model.

Entities recognizing revenue over time under ASC 606 will potentially see greater impacts on their revenue recognition. For example, assume that an entity uses imported materials subject to tariff increases in its production process. Increased tariffs on these materials could result in an increase in total contract costs, which is an input into the cost-to-cost method for recognizing revenue over time. The increase in total contract costs would impact estimated costs at completion, the completion percentage of the contract and the overall profitability of the contract. Moreover, if the cost of imported products used in the production process increases significantly, it could lead to estimated contract costs surpassing contract revenue. This may require the entity to recognize a loss for an onerous contract under ASC 606.

Entities may be able to recover the cost of tariffs through increasing the sales price of a product in a contract. Price increases based on existing contractual clauses related to tariffs would be accounted for as variable consideration. Those obtained by changing contractual terms would be accounted for as contract modifications. Lastly, any increase in consideration received due to tariff surcharges would not meet the “sales and use tax” practical expedient found in ASC 606-10-32-2a. As such, revenue including the tariff surcharge, and related tariff expense, would be recorded gross in the income statement.

### 3.2 Asset Impairment

Various asset impairment models—including those for inventory (ASC 330); intangibles (ASC 350); and property, plant and equipment (PP&E) (ASC 360)—rely on estimates of future cash flows to determine if impairment exists and, if so, the amount of impairment to recognize. These estimates could be impacted by tariff policies.

For example, when determining the net-realizable-value (NRV) of non-LIFO raw material and work-in-progress inventory (WIP) under ASC 330, an entity estimates its selling price, reduced by the reasonably predictable costs of completion, disposal and transportation of the product. Increased tariffs on inputs used to complete raw material and WIP inventory could result in increased completion costs for the product, thereby decreasing its NRV (and increasing the likelihood of its impairment), unless the entity is able to implement price increases to offset the increased costs.

Additionally, cost increases due to rising tariffs could reduce the estimated fair value of intangible assets subject to impairment testing under ASC 350, especially when using an income-based estimate to determine the fair value of the intangible asset. Assume that due to market conditions, an entity must absorb the cost of increased tariffs, rather than passing them onto their customers. This would result in reduced cash flows arising from the use of the intangible asset. These reduced cash flows would result in a reduced fair value for the asset, increasing the likelihood of the asset's impairment.

The assessment of impairment of PP&E under ASC 360 involves a two-step model that also considers future cash flows generated from the use of the asset group. An increase in costs due to elevated tariffs may lead to the carrying amount of the asset group assessed for impairment that includes PP&E exceeding the undiscounted net cash flows expected from utilization and eventual disposal of the asset group. If the carrying amount of the asset group is greater than the undiscounted cash flows as per Step 1 of the ASC 360 impairment test, the asset group is deemed not recoverable, necessitating the evaluation of whether an impairment loss must be recorded, which would be measured as any excess of the carrying amount over its fair value (Step 2 of the ASC 360 impairment test). Additionally, negative financial implications resulting from tariffs could diminish the estimated fair value of the asset group.

### 3.3 Risk Mitigation Activities

Increased uncertainty over tariff policies could lead to greater foreign exchange volatility, which may result in earnings volatility for entities with significant foreign currency exposure. To mitigate this risk, entities may use derivative instruments such as forward and futures contracts to, among other things:

- Hedge foreign currency exchange risk
- Hedge future purchase commitments in anticipation of the rising costs of goods

Entities seeking to also mitigate the potential earnings volatility that may result from the fair value accounting for investments in derivative instruments should familiarize themselves with the requirements to achieve hedge accounting treatment under ASC 815, *Derivatives and Hedging*.

Entities that have already entered into cash flow hedges under ASC 815-30 to mitigate price fluctuations on forecasted transactions should ensure that the transactions remain probable of occurring during the hedge period. If economic uncertainty changes the probability that a forecasted transaction will occur, entities may be required to discontinue cash flow hedge accounting. The accounting impact going forward depends on the revised probability. If the forecasted transaction is no longer probable of occurring, hedge accounting is discontinued. If the forecasted transaction is probable of not occurring, not only is hedge accounting discontinued, but the deferred hedge gains and losses must be reclassified from other comprehensive income to earnings.

Fair value hedging under ASC 815-25 applies to firm commitments (binding agreements for future transactions). If a firm commitment no longer qualifies under ASC 815-25, entities must discontinue fair value hedge accounting and immediately recognize previously recorded fair value adjustments related to the firm commitment in earnings.

### 3.4 Income Taxes

Entities should assess the impact of pre-tax tariff-related charges on amounts recorded under ASC 740, *Income Taxes*. For instance, the recognition of an impairment charge or other adjustments due to the impact of tariffs would likely affect deferred taxes related to the impacted asset.

Additionally, the recoverability of deferred tax assets (DTA) recorded under ASC 740 could be jeopardized if tariff-related uncertainty negatively impacts forecasted future earnings or if an entity amends transfer pricing agreements as a result of tariffs. Such earnings are a source of positive evidence supporting the recoverability of DTAs. Inability to support the use of the DTAs would require the establishment of a valuation allowance. Entities that use future earnings as their primary source of positive evidence to support the realizability of DTAs should assess the need to update such forecasts, especially if negative economic trends occur.

Changes to transfer pricing arrangements in response to tariffs could result in an entity reassessing its accounting for uncertain tax positions. Potential challenges by taxing authorities on changes in transfer pricing could revise an entity's assessment of the amount that is more likely than not of being sustained upon examination of the arrangement.

When preparing its interim income tax provision, an entity should assess the guidance in ASC 740-270-25-2 in determining whether the income tax effects of any impairment charges or other adjustments should be recognized discretely during the quarter of recognition or whether the adjustments are part of ordinary income to which the entity's estimated annual effective tax rate (ETR) is applied. An entity's response to tariffs could result in significant changes to its operations. Based on the estimated impact of these changes or adjustments, the entity should assess the need to update its ETR at subsequent reporting periods.

### 3.5 Performance-based Vesting Conditions

Tariff-induced economic uncertainty could impact entities that have granted share-based compensation awards. Many share-based awards accounted for under ASC 718, *Compensation – Stock Compensation*,



include performance-based vesting conditions. These awards vest based on the entity achieving a performance target such as profitability or other operating metrics. When the achievement of the performance condition is no longer probable of occurring, the entity would reverse compensation cost for the impacted awards.

## 4. Conclusion

The implications of evolving tariff policies in the U.S. and abroad are both wide-ranging and potentially significant. Entities should be proactive in monitoring policy changes, assessing the impact on their operations and updating assumptions used in developing accounting estimates, as necessary, to ensure proper recognition and disclosure of these effects in their financial statements.

Below are links to further RSM articles on the tariff topic.

- [How consumer businesses can strengthen resilience against tariff increases](#)
- [The impact of tariffs: Balancing costs, supply chains and profitability](#)

For additional information and analysis of tariff policy, visit the [Supply Chain Page](#) of RSM's The Real Economy blog.

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