

st line vacuum dep 30% tax rate
 Acct Tax
 125,000 175,000
 Acctg 215 725,000 25,000
 Quiz #3
 17

DEFERRED TAXES

Company ABC, Inc. has reached its 1999 year-end and must calculate its tax expense and taxes payable. The GAAP (accounting) rules and the tax rules are identical, as they relate to ABC Inc., except for two items:

- \$200,000 of cash received is counted as revenue for tax purposes, but not for accounting purposes.
- The accounting books reflect straight-line depreciation of \$125,000 while the tax books reflect accelerated depreciation of \$175,000.

Given the above information and a 30% tax rate, answer the following questions.

(3 points) What is the difference between ABC Inc.'s pre-tax Book Income and its taxable income (TI) in 1999?

ABC's

pre-tax Book Income = 125,000 = 37,500

taxable Income = 375,000 = 112,500

$$\begin{array}{r} 12,500 \\ - 37,500 \\ \hline 95,000 \end{array}$$

(1 point) Is there a deferred tax asset or deferred tax liability involved in 1999?

deferred tax asset

(3 points) Provide the appropriate journal entry to record the 1999 deferred taxes.

Journal entry
accounts debit/credit
if it goes left

Tax Expense 37,500
 DTA 7,500
 Income Tax Payable 112,500

(3 points) Now, disregard everything that you did before now. Assume that in 1999 ABC Inc. recorded a \$10,000 deferred tax liability. In 2000, pre-tax book income was \$20,000 less than taxable income (TI). The tax rate is now 35%. What journal entry would ACB Inc. record in 2000?

pre-tax 20,000

TI

DTL 10,000

- 2

Tax Expense (TI - 20,000)

DTL debit

Income Tax Payable

12,000 7,000

(TI) 1,000

cash	merch	COGS
500,000		

Debt
equity

NI
sales

Cash	500,000
Merch	300,000
COGS	300,000
Rev	500,000

COGS	325,000
Merch	325,000

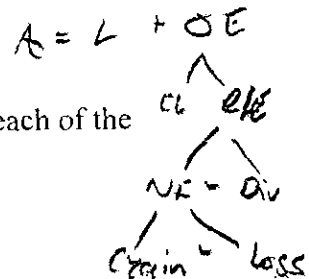
ERROR CORRECTION

In fiscal year 2001, Company XYZ sold merchandise for a total of \$500,000 cash. The cost of these goods was actually \$300,000, but \$325,000 of COGS was actually recorded.

(2 points) What journal entry should be made to correct this error?

~~What's wrong?~~
~~Cash 500,000~~
~~Rev 500,000~~
~~COGS 325,000~~
~~Merch 300,000~~

Merchandise 25,000
 COGS 25,000



(2 points each) If the above error isn't corrected, what will be the impact on each of the following ratios? Please circle.

↓ ↑
 CA - CL

Working Capital

5 - 3

Increase

Decrease

No Change

↑
 Debt
 equity

Debt to Equity

Increase

Decrease

No Change

Inventory Turnover

Increase

Decrease

No Change

Return on Sales (NI / Net Sales)

Increase

Decrease

No Change