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速成教育
SPEED UP EDUCATION

BUS 321

Intermediate accounting

导师： **Alex Chen**

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Income Tax

- Accounting income—also known as “income before taxes”, “income for financial reporting purposes” or “accounting profit”—is a pre-tax concept

- Taxable income—also known as “income for tax purposes” or “taxable profit”

Temporary differences

1. Taxable Difference-result in taxable amounts in future year
2. Deductible Difference- decrease tax in the future

Revenue of $18,000 is recognized in 2020 for financial reporting purposes. The customer pays $1,000 per month starting Jan 1, 2021.

Warranty worth $30,000 was provided on sales and recognized as expense in 2020. Actual warranty work was $20,000 in 2021 and $10,000 in 2022.

Permanent differences

1. Items included in accounting income that are never included in taxable income

A premium of $5,000 is paid in each of 2021 and 2022 for life insurance on key officers.

Taxable Income

	2020	2021	2022
Accounting income	$200,000	$200,000	$200,000
Adjustments:			
Revenue from 2020 sale	(18,000)	12,000	6,000
Warranty expense	30,000	(20,000)	(10,000)
Non-deductible insurance expense		5,000	5,000
Taxable income	$212,000	$197,000	$201,000

Current Income Tax

- Taxes payable method
    - Current rate of tax applied to the company's taxable income
    - Choice under A S P E
- Temporary difference approach
    - Adjusts current income taxes for effects of changes in deferred tax assets and deferred tax liabilities and recognizes them under deferred tax expense

Tax Base

- Tax base of an asset: amount that will be deductible for tax purposes against any taxable economic benefits when the asset’s carrying amount is recovered

- Tax base of a liability: carrying amount reduced by amount that will be deductible for tax purposes in future periods

- Tax base of revenue received in advance: carrying amount less any amount that will not be taxable in the future

deferred tax liability

- A deferred tax liability or future income tax liability is the future tax consequence of a taxable temporary difference
- Increase in taxes payable in future years as a result of a taxable temporary difference at the end of the current year

Example: Company reported $130,000 revenue in 2020. It reported only $100,000 of taxable revenue, which was the amount collected. Carrying amount of receivable = $30,000. Future tax rate is 25%. 20000 collected in 2021 10000 in 2022

2020 taxable income 40000 2021 taxable income 90000

	Future Year 2021	Future Year 2022	Total
Future taxable amounts	$20,000	$10,000	$30,000
Future tax rate	25%	25%	
Deferred tax liability at the end of 2020	$ 5,000	$ 2,500	$ 7,500

deferred tax asset

- A deferred tax asset or future income tax asset is the future tax consequence of a deductible temporary difference
- It represents the reduction in taxes payable or the increase in taxes refundable in future years as a result of a deductible temporary difference at the end of the year

- Company sells microwave ovens including a 2-year assurance warranty. In December 2021, they started selling a new microwave with estimated warranty expense of $500,000 related to the sales.
- Costs were exactly as expected: $300,000 in 2022; $200,000 in 2023
- Income tax payable: $600,000 in 2021; $440,000 in 2022
- Future tax rate is 25%
- Warranty costs are accounted for using the expense approach--$500,000 warranty expense recognized in 2021

Assume 2021 current income tax payable = 600000 2022 440000

Income Tax Loss Carryover Benefits

    - Loss carryback: carry a tax loss back against taxable income of the immediately preceding 3 years
    - Loss carryforward: carry losses forward to the 20 years immediately following the loss
    - If full amount of loss cannot be absorbed by carrybacks, then it can be carried forward
- If a loss is carried back, it is usually applied against the earliest available income

Loss Carry Forward

- If it appears ("more likely than not") there will be income in the future to offset the loss carryforward, the benefits should be recognized in the period of the loss
    - As a deferred tax benefit in the income statement
    - As a deferred tax asset on the statement of financial position
    - ASPE (not IFRS) allows a contra valuation allowance account
- If it appears there will be no future income, the benefits are not recognized in the financial statements

Year	**Taxable Income or Loss**	**Tax Rate**	**Tax Paid**
2017	$ 75,000	30%	$22,500
2018	50,000	25%	12,500
2019	100,000	30%	30,000
2020	200,000	20%	40,000
2021	(500,000)	—	−0−

Assume that in 2022 the company returns to profitability and has taxable income of $200,000 subject to a 20% tax rate. They can now realize the benefit of the tax loss carryforward that was recognized in 2021.

Carryforward with Valuation Allowance (A S P E)

Temporary difference approach

IFRS	ASPE
Temporary difference approach	**Future income taxes method**
Deferred tax assets	Future income tax assets
Deferred tax liabilities	Future income tax liabilities
Deferred tax expense	Future income tax expense