

CHAPTER 18

INCOME TAXES

ASSIGNMENT CLASSIFICATION TABLE

Topics	Brief Exercises	Exercises	Problems	Writing Assignments
1. Income taxes from a business perspective.	1			4
2. Difference between accounting income and taxable income, calculate taxable income.	2, 3, 4, 5	1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, 17, 18, 19	1, 2, 3, 5, 6, 7, 8, 9, 10, 11, 13, 14, 15	1, 2, 3
3. Taxable temporary differences, calculation of deferred/future income tax liabilities.	4, 6, 7	4, 5, 6, 7, 8, 9, 10, 11, 12	1, 2, 3, 5, 6, 7, 8, 9, 13, 14, 15	
4. Deductible temporary differences, calculation of deferred/future income tax assets.	8, 9	4, 5, 6, 7, 8, 13, 14, 15, 16, 17	1, 2, 3, 5, 6, 7, 8, 9, 13, 14, 15	
5. Deferred/future income tax balances.	3, 4, 5, 6, 7, 9, 10, 11	5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, 17, 18	1, 3, 4, 5, 6, 7, 8, 9, 10, 11, 13, 14, 15	
6. Multiple tax rates, tax rate changes.	12	12, 16, 17, 19, 20	2, 3, 4, 14	5, 6
7. Loss carrybacks.	13, 14, 15, 16, 17	21, 22, 23, 24	12	

ASSIGNMENT CLASSIFICATION TABLE (CONTINUED)

Topics	Brief Exercises	Exercises	Problems	Writing Assignments
8. Loss carryforwards.	14, 15, 16, 17	22, 23, 24	12, 15	
9. Valuation of deferred/future tax asset.		24, 25, 26		
10. Presentation and disclosure of income taxes.	18, 19, 20, 21	24, 27, 28, 29, 30, 31	1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15	1
11. Differences between IFRS and ASPE.	21, 22	18, 29, 30, 31	1, 2, 3, 5, 6, 7, 8, 9, 10, 11, 14	1, 2, 3, 6, 7

Please note: The simplifying assumption is made that all companies in the end-of-chapter brief exercises, exercises and problems use the term “deferred” rather than “future” for the tax-related accounts, even when applying ASPE.

ASSIGNMENT CHARACTERISTICS TABLE

Item	Description	Level of Difficulty	Time (minutes)
E18-1	Terminology, relationships, calculations, entries.	Simple	10-15
E18-2	One temporary difference through three years, one rate.	Simple	10-15
E18-3	Intraperiod tax allocation.	Moderate	15-20
E18-4	Identify temporary or permanent differences and direction of adjustment.	Simple	10-15
E18-5	Two temporary differences, future taxable amounts, one rate, no beginning deferred taxes.	Moderate	20-25
E18-6	Two temporary differences, future taxable amounts, one rate, beginning deferred taxes.	Moderate	20-25
E18-7	Two temporary differences, future taxable amounts, change in rate.	Moderate	20-25
E18-8	Reversing and permanent, future taxable amounts, no beginning balances.	Simple	20-25
E18-9	One temporary difference, future taxable amounts, one rate, no beginning deferred taxes, prepare statements	Simple	20-25
E18-10	One temporary difference, future taxable amounts, one rate, no beginning deferred taxes.	Simple	15-20
E18-11	One temporary difference, future taxable amounts, one rate, beginning deferred taxes.	Simple	15-20
E18-12	One temporary difference, future taxable amounts, change in rate.	Simple	15-20
E18-13	Permanent and reversing differences, calculate taxable income, entry for income taxes.	Simple	15-20
E18-14	One temporary difference, future deductible amounts, one rate, beginning deferred taxes.	Simple	15-20
E18-15	One temporary difference, future deductible amounts, one rate, beginning deferred taxes.	Simple	15-20
E18-16	One temporary difference, future taxable amount becomes future deductible amount, change in rate.	Moderate	20-25
E18-17	One temporary difference, future deductible amounts, change in rate	Moderate	20-25

ASSIGNMENT CHARACTERISTICS TABLE (CONTINUED)

Item	Description	Level of Difficulty	Time (minutes)
E18-18	Depreciation, temporary difference over five years, determine taxable income, taxes payable method.	Moderate	40-45
E18-19	Deferred tax liability, change in tax rate.	Complex	15-20
E18-20	One difference, multiple rates, beginning deferred taxes, change in rates.	Simple	20-25
E18-21	Loss carryback and carryforward..	Moderate	20-25
E18-22	Carryback and carryforward of tax losses.	Simple	15-20
E18-23	Loss carryback and carryforward.	Complex	30-35
E18-24	Loss carryback and carryforward using valuation allowance.	Moderate	30-35
E18-25	Deferred tax asset, different amounts to be realized.	Moderate	20-25
E18-26	Deferred tax asset, different amounts to be realized using valuation allowance.	Moderate	20-25
E18-27	Three differences, classify deferred taxes.	Simple	10-15
E18-28	Intraperiod tax allocation.	Moderate	25-30
E18-29	Taxes payable method-taxes payable reporting disclosures.	Simple	10-15
E18-30	Taxes payable method.	Simple	10-15
E18-31	Taxes payable method.	Moderate	15-20

ASSIGNMENT CHARACTERISTICS TABLE (CONTINUED)

Item	Description	Level of Difficulty	Time (minutes)
P18-1	Three temporary differences and two permanent differences, opening balance, statement disclosure.	Moderate	30-35
P18-2	Six differences, three years, two tax rates, income and statement of financial position reporting.	Complex	45-50
P18-3	Four differences, one rate, reconciliation of balances and comparative statement disclosure, reconcile tax rate.	Complex	50-60
P18-4	One temporary difference, tracked for four years, one permanent difference, change in rate.	Complex	50-60
P18-5	Second year of depreciation difference, two differences, single rate, earnings per share.	Moderate	40-45
P18-6	Several differences, two years, reversing differences, one rate, discontinued operations and financial statements.	Complex	50-60
P18-7	Two differences, two years, reversing differences, two assumptions, several rates and financial statements.	Complex	40-45
P18-8	Three differences, several rates, two years and statement disclosure.	Complex	50-60
P18-9	Two differences, two rates, future income expected.	Moderate	25-30
P18-10	Two differences, two years, calculate taxable income and pre-tax accounting income.	Complex	40-50
P18-11	Five differences, one year, income and retained earnings reporting, and effective tax rate.	Complex	50-60
P18-12	Losses carryback and carryforward expected to be realized and not expected to be realized.	Moderate	35-40
P18-13	Prior period error correction, recovery of prior year taxes, income statement and retained earnings statements disclosure.	Moderate	35-40
P18-14	One timing difference, change in tax rate, calculation of effective tax rate, all entries and balance sheet presentation under ASPE and IFRS	Moderate	50-60

ASSIGNMENT CHARACTERISTICS TABLE (CONTINUED)

Item	Description	Level of Difficulty	Time (minutes)
P18-15	Loss carryback with timing and permanent differences and a tax rate change. The tax benefit for only half of the loss carryforward can be recognized. Journal entries and tax reconciliation note is required.	Complex	60-75

SOLUTIONS TO BRIEF EXERCISES

BRIEF EXERCISE 18-1

- (a) Higher income tax expense results in lower profits.
- (b) Higher income taxes paid decreases cash flow from operations.
- (c) Considering only the effect of income taxes, Faber should register its company in Eastern Europe, where the company would be subject to a lower corporate income tax rate.

BRIEF EXERCISE 18-2

2014 taxable income	\$198,000
Tax rate	<u>X 25%</u>
12/31/2014 income tax payable	<u>\$ 49,500</u>

BRIEF EXERCISE 18-3

Accounting income	\$156,000
Permanent difference – insurance expense	<u>5,000</u>
	161,000
Reversing difference: CCA > Depreciation	<u>(14,000)</u>
Taxable income	<u>\$147,000</u>
Current income taxes at 25%	<u>\$ 36,750</u>

<u>Stmt of Fin Pos Account</u>	<u>(Taxable) Temporary Difference (change in)</u>	X	<u>Tax Rate</u>	<u>Deferred Tax (Liability) (change in)</u>
PP & E	(\$14,000)*		25%	(\$3,500)

* Carrying amount and tax base are not given in the exercise; only the net change in the temporary difference is given.

Current Tax Expense	36,750	
Income Tax Payable		36,750
Deferred Tax Expense.....	3,500	
Deferred Tax Liability		3,500

BRIEF EXERCISE 18-4

The \$40,000 reversing difference that occurs in the first fiscal year of Anugraham Corp. results in a taxable temporary difference at December 31, 2014. The carrying amount is greater than the UCC (tax base) by \$40,000 X 35% tax rate = \$14,000 deferred tax liability.

<u>Stmt of Fin Pos Account</u>	<u>(Taxable) Temporary Difference</u>	X	<u>Tax Rate</u>	<u>Deferred Tax (Liability)</u>
PP & E	(\$40,000)*		35%	(\$14,000)

* Carrying amount and tax base are not given in the exercise; only the net difference is provided.

BRIEF EXERCISE 18-5

		<u>@ 25%</u>	<u>Divided by Accounting Income</u>
Accounting income	\$156,000	\$39,000	25.0%
Non-deductible insurance expense	5,000	1,250	0.8%
		<u>\$ 40,250</u>	<u>25.8%</u>

Effective tax rate (\$40,250/\$156,000) 25.8%

BRIEF EXERCISE 18-6

<u>Balance Sheet Account</u>	<u>Tax Base</u>	-	<u>Carrying Amount</u>	=	<u>(Taxable) Temporary Difference</u>	X	<u>Tax Rate</u>	=	<u>Deferred Tax (Liability)</u>
Equip.	\$114,000		\$145,000		(31,000)		30%		(9,300)

BRIEF EXERCISE 18-7

Accounting income	\$ 275,000
Reversing difference: CCA > Deprec.	<u>(40,000)</u>
Taxable income	235,000
	<u>X 35%</u>
Income tax payable	<u><u>\$ 82,250</u></u>

Stmt of Fin Pos Account	(Taxable) Temporary Difference	X	Tax Rate	Deferred Tax (Liability)
PP & E	(\$40,000)*		35%	(\$14,000)

* Carrying amount and tax base are not given in the exercise, only the net difference is provided.

Current Tax Expense	82,250	
Income Tax Payable		82,250
Deferred Tax Expense.....	14,000	
Deferred Tax Liability		14,000

BRIEF EXERCISE 18-8

Balance Sheet Account	Tax Base	-	Carrying Amount	=	Deductible Temporary Difference	X	Tax Rate	=	Deferred Tax Asset
Warranty Liability	\$0	-	(170,000)	=	\$170,000	X	25%	=	\$42,500

BRIEF EXERCISE 18-9

Current tax expense for 2014		\$70,000
Deferred tax benefit for 2014		
Deferred tax asset, 12/31/2014	\$62,000	
Deferred tax asset, 12/31/2013	<u>40,000</u>	<u>(22,000)</u>
Total income tax expense for 2014		<u>\$48,000</u>

BRIEF EXERCISE 18-10

Current tax expense for 2014		\$53,000
Deferred tax expense for 2014		
Deferred tax liability, 12/31/2014	\$52,000	
Deferred tax liability, 12/31/2013	<u>35,000</u>	<u>17,000</u>
Total income tax expense for 2014		<u>\$70,000</u>

BRIEF EXERCISE 18-11

<u>Year</u>	<u>Future taxable amount</u>	<u>Rate</u>	<u>Deferred tax liability</u>
2015	\$53,000	25%	\$ 13,250
2016	310,000	25%	77,500
2017	352,000	31%	<u>109,120</u>
			<u>\$199,870</u>

BRIEF EXERCISE 18-12

Deferred Tax Asset.....	54,000	
Deferred Tax Benefit.....		54,000
(\$2,700,000 X 2%)		

BRIEF EXERCISE 18-13

Income Tax Receivable	184,500	
Current Tax Benefit		184,500
[\$136,500 + (\$160,000 X 30%) = \$184,500]		

BRIEF EXERCISE 18-14

Income Tax Receivable	161,000	
Current Tax Benefit		161,000
(\$460,000 X 35%)		
Deferred Tax Asset	42,000	
Deferred Tax Benefit		42,000
[(580,000 – 460,000) X 35%]		

BRIEF EXERCISE 18-15

(a)		
Income Tax Receivable	161,000	
Current Tax Benefit		161,000
(\$460,000 X 35%)		
(b)		
Income Tax Receivable	161,000	
Current Tax Benefit		161,000
(\$460,000 X 35%)		
Deferred Tax Asset	42,000	
Deferred Tax Benefit		42,000
Deferred Tax Expense		42,000
Allowance to Reduce Deferred Tax		
Asset to Expected Realizable Value		42,000
(\$120,000 X 35%)		

BRIEF EXERCISE 18-16

(a)		
Current Tax Expense	8,750	
Income Tax Payable		8,750
Income Tax Payable	8,750	
Current Tax Benefit		8,750
(\$25,000 X 35%)		
(b)		
Deferred Tax Expense.....	8,750	
Deferred Tax Asset		8,750
Allowance to Reduce Deferred Tax		
Asset to Expected Realizable Value.....	8,750	
Deferred Tax Benefit		8,750
(\$25,000 X 35%)		

BRIEF EXERCISE 18-17

(a)		
Deferred Tax Expense.....	70,000	
Deferred Tax Asset		70,000
(b)		
Deferred Tax Expense.....	70,000	
Allowance to Reduce Deferred Tax		
Asset to Expected Realizable Value....		70,000

BRIEF EXERCISE 18-18

Unrealized Gain or Loss - OCI	4,000	
FV-OCI Investments		4,000
Deferred Tax Asset	1,200	
Deferred Tax Benefit - OCI		1,200
(\$4,000 X 30%)		
Net income		\$55,000
Other comprehensive income:		
Unrealized loss, FV-OCI investments	\$4,000	
Less: Deferred tax benefit	(1,200)	2,800
Comprehensive income		<u>\$52,200</u>

BRIEF EXERCISE 18-19

(a) Income before income tax		\$230,000
Income tax expense		
Current	\$43,000	
Deferred	<u>27,000</u>	<u>70,000</u>
Net income		<u>\$160,000</u>
(b) Effective tax rate = \$70,000/\$230,000 = 30.4%		

BRIEF EXERCISE 18-20

Income from continuing operations before income tax		\$ 71,000
Income tax expense		<u>17,750</u>
Income from continuing operations		53,250
Discontinued operations:		
Loss from discontinued operations	\$10,000	
Less: applicable income tax savings	<u>2,500</u>	<u>7,500</u>
Net income		<u>\$ 45,750</u>

BRIEF EXERCISE 18-21

(a) Current assets	
Deferred tax asset	\$14,000
Long-term liabilities	
Deferred tax liability	\$69,000
(b) Long-term liabilities	
Deferred tax liability	\$55,000

BRIEF EXERCISE 18-22

Current Tax Expense	36,750	
Income Tax Payable		36,750

SOLUTIONS TO EXERCISES

EXERCISE 18-1 (10-15 minutes)

- (a) greater than
- (b) less than
- (c) $304,000 = (\$76,000 \text{ divided by } 25\%)$
- (d) are not
- (e) less than
- (f) benefit; \$15,000
- (g) $\$8,500 = [(\$100,000 \times 25\%) - \$16,500]$
- (h) debit
- (i) $\$59,000 = (\$82,000 - \$23,000)$
- (j) will not be
- (k) benefit
- (l) increase, increase
- (m) temporary, reversing

EXERCISE 18-2 (10-15 minutes)**(a)**

Year	Amount of Temporary Difference Originating or Reversing during the Year	Deductible Temporary Difference at Year-End
2014	\$160,000 – \$245,000 = \$85,000 originating	\$85,000
2015	\$139,000 – \$121,000 = \$18,000 reversing	67,000
2016	\$131,000 – \$125,000 = \$6,000 reversing	61,000

(b)

Date	Future Deductible Amounts	Tax Rate	Deferred Tax Asset*
12/31/2014	\$85,000	30%	\$25,500
12/31/2015	67,000	30%	20,100
12/31/2016	61,000	30%	18,300

- * The fact that the temporary difference will result in future deductible amounts is determined by the fact that in the year of origination, the temporary difference causes taxable income to exceed pre-tax accounting income. Therefore, in the period(s) of reversal, we can expect pre-tax accounting income to exceed taxable income.

EXERCISE 18-3 (15-20 minutes)

(a)

Unrealized Gain or Loss - OCI.....	28,000	
FV-OCI Investments.....		28,000
Deferred Tax Asset.....	8,400	
Deferred Tax Benefit - OCI		8,400
[(\$28,000 X 30%) – \$0]		

(b)

FV-OCI Investments	33,500	
Unrealized Gain or Loss - OCI		33,500
(\$28,000 + \$5,500)		
Deferred Tax Expense - OCI	10,050	
Deferred Tax Asset.....		8,400
Deferred Tax Liability		1,650
(\$5,500 X 30%)		

Balance, Dec. 31, 2015: (\$5,500 X 30%)		\$ (1,650)	L
Balance before adjustment		<u>8,400</u>	A
Adjustment to deferred tax asset/liability account and 2015 deferred tax expense - OCI		<u>\$10,050</u>	

(c)

Hang Technologies Inc.
Statement of Comprehensive Income
Year Ended December 31,

	<u>2015</u>	<u>2014</u>
Net income	<u>\$100,000</u>	<u>\$100,000</u>
Other comprehensive income (loss)		
Unrealized gains (losses) on FV-OCI investments	33,500	(\$28,000)
Less: Deferred tax (expense) benefit	<u>(10,050)</u>	<u>8,400</u>
Other comprehensive income (loss)	<u>23,450</u>	<u>(19,600)</u>
Comprehensive income	<u>\$123,450</u>	<u>\$80,400</u>

EXERCISE 18-4 (10-15 minutes)

	(a)	(b) Add or deduct from accounting income
		<hr/>
1.	ii	deduct
2.	i	add
3.	iii	add
4.	i	add
5.	ii	deduct
6.	ii	deduct
7.	i	add
8.	iii	deduct
9.	iii	deduct
10.	i	add
11.	i	add
12.	i	add

EXERCISE 18-5 (20-25 minutes)

(a)

Statement of Financial Position Account Dec 31, 2014	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	Current or Long-Term
PP & E	\$980,000	\$930,000	50,000	25%	\$ 12,500	LT
Construction in Process*	350,000	500,000	(150,000)	25%	(37,500)	C
Deferred tax liability, December 31, 2014					(25,000)	
Deferred tax liability before adjustment					<u>0</u>	
Incr. in deferred tax liability, and deferred tax expense for 2014					<u>(\$ 25,000)</u>	

* For the completed contract method, the construction in process account reports only construction costs excluding any gross profit recognized under the percentage-of-completion method.

(b)

Accounting income		\$195,000
Reversing differences:		
Property, plant, and equipment:		
Depreciation expense	\$170,000	
Capital cost allowance (\$1,100,000 – \$980,000)	<u>(120,000)</u>	50,000
Construction in Process:		
Gross profit—Percentage completion (\$500,000 – \$350,000)	(150,000)	
Gross profit—Completed contract method	<u>0</u>	<u>(150,000)</u>
Taxable income		<u>\$95,000</u>
Current income taxes at 25%		<u>\$23,750</u>

EXERCISE 18-5 (Continued)**(c)**

Current Tax Expense	23,750	
Income Tax Payable		23,750
Deferred Tax Expense.....	25,000	
Deferred Tax Liability		25,000

(d) Income before income tax		\$195,000
Income tax expense		
Current	\$23,750	
Deferred	<u>25,000</u>	<u>48,750</u>
Net income		<u><u>\$146,250</u></u>

(e) Refer to last two columns in table in part (a) above.

Non-current assets	
Deferred tax asset	\$12,500
Current liabilities	
Deferred tax liability	37,500

(f) Non-current liabilities	
Deferred tax liability	\$25,000

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

EXERCISE 18-6 (20-25 minutes)

(a)

Statement of Financial Position Account Dec. 31, 2015	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	Current or Long-Term
PP & E	\$620,000	\$640,000	(\$20,000)	25%	(\$5,000)	LT
Construction in Process	760,000	940,000 ^a	(180,000)	25%	<u>(45,000)</u>	C
Deferred tax liability, December 31, 2015					(50,000)	
Deferred tax liability before adjustment					<u>(25,000)</u>	
Incr. in deferred tax liability, and deferred tax expense for 2015					<u>(\$25,000)</u>	

^a \$350,000 + \$410,000 = \$760,000

(b)

Accounting income		\$120,000
Reversing differences:		
Property, plant, and equipment:		
Depreciation expense (\$460,000 – \$170,000)	\$290,000	
Capital cost allowance (\$980,000 – \$620,000)	<u>(360,000)</u>	(70,000)
Construction in Process:		
Gross profit – Percentage completion (\$440,000 – \$410,000)	(30,000)	
Gross profit – Completed contract method	<u>0</u>	<u>(30,000)</u>
Taxable income		<u>\$20,000</u>
Current income taxes at 25%		<u>\$5,000</u>

EXERCISE 18-6 (Continued)

(c)

Current Tax Expense	5,000	
Income Tax Payable		5,000
Deferred Tax Expense.....	25,000	
Deferred Tax Liability		25,000

(d)

	<u>2015</u>	<u>2014</u>
Income before income tax	<u>\$120,000</u>	<u>\$195,000</u>
Income tax expense		
Current	5,000	23,750
Deferred	<u>25,000</u>	<u>25,000</u>
	<u>30,000</u>	<u>48,750</u>
Net income	<u><u>\$90,000</u></u>	<u><u>\$146,250</u></u>

(e) Refer to last two columns in table in part (a) above.

	<u>2015</u>	<u>2014</u>
Non-current assets		
Deferred tax asset		\$12,500
Current liabilities		
Deferred tax liability	\$45,000	37,500
Non-current liabilities		
Deferred tax liability	5,000	

(f)

	<u>2015</u>	<u>2014</u>
Non-current liabilities	\$50,000	\$25,000

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

EXERCISE 18-7 (20-25 minutes)

(a)

Statement of Financial Position Account Sep. 15, 2015	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate Decrease	Decrease in Deferred Tax (Asset) Liability	Current or Long-Term
PP & E	\$980,000	\$930,000	\$50,000	5%	(\$2,500)	LT
Construction in Process	350,000	500,000	(150,000)	5%	<u>7,500</u>	C
Decrease in future tax liability due to decrease in tax rate					\$5,000	

September 15, 2015 adjustment to record the impact of the decrease in tax rate on the company's net taxable temporary difference:

Deferred Tax Liability.....	5,000	
Deferred Tax Benefit.....		5,000

EXERCISE 18-7 (Continued)

(b)

Statement of Financial Position Account Dec. 31, 2015	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	Current or Long-Term
PP & E	\$620,000	\$640,000	(\$20,000)	20%	(\$4,000)	LT
Construction in Process	760,000	940,000	(180,000)	20%	(36,000)	C
Deferred tax liability, December 31, 2015					(40,000)	
Sept. 15 deferred tax liability before adjustment (\$25,000 – \$5,000)					20,000	
Incr. in deferred tax liability, and deferred tax expense for 2015					<u>\$(20,000)</u>	

(c)

Accounting income		\$120,000
Reversing differences:		
Property, plant, and equipment:		
Depreciation expense (\$460,000 – \$170,000)	\$290,000	
Capital cost allowance (\$980,000 – \$620,000)	<u>(360,000)</u>	(70,000)
Construction in Process:		
Gross profit – Percentage completion (\$440,000 – \$410,000)	(30,000)	
Gross profit – Completed contract method	<u>0</u>	<u>(30,000)</u>
Taxable income		<u>\$20,000</u>
Current income taxes at 25% current rate		<u>\$5,000</u>

EXERCISE 18-7 (Continued)**(d)**

Current Tax Expense	5,000	
Income Tax Payable		5,000
Deferred Tax Expense.....	20,000	
Deferred Tax Liability		20,000

(e)

	<u>2015</u>	<u>2014</u>
Income before income tax	<u>\$120,000</u>	<u>\$195,000</u>
Income tax expense		
Current	5,000	23,750
Deferred *	<u>15,000</u>	<u>25,000</u>
	<u>20,000</u>	<u>48,750</u>
Net income	<u>\$100,000</u>	<u>\$146,250</u>

* Deferred tax expense for 2015 of \$15,000 is comprised of a future tax benefit of \$5,000 due to a decrease in tax rates effective September 15, 2015; and future tax expense of \$20,000 due to differences in the period of recognition of certain expenses for accounting purposes versus for income tax purposes.

(f) Refer to last two columns in table in part (b) above.

	<u>2015</u>	<u>2014</u>
Non-current assets		
Deferred tax asset		\$12,500
Current liabilities		
Deferred tax liability	\$36,000	37,500
Non-current liabilities		
Deferred tax liability	4,000	

EXERCISE 18-7 (Continued)**(g)**

	<u>2015</u>	<u>2014</u>
Non-current liabilities		
Deferred Tax Liability	\$40,000	\$25,000

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

EXERCISE 18-8 (20-25 minutes)**(a)**

Unrealized Gain or Loss	2,000	
FV-NI Investments		2,000
FV-OCI Investments	4,000	
Unrealized Gain or Loss—OCI		4,000

(b) All of Christina's investments must be reported on the statement of financial position at their fair value. The resulting difference between this and the tax base of the investments represents a temporary difference. The unrealized gain recognized is not taxable, and any unrealized loss recognized is not deductible, until the investments are sold at a gain or at a loss. The resulting taxable temporary difference must have the corresponding deferred tax recorded at the tax rate that Christina expects to pay (or recover in the case of a loss) on this gain or loss in future accounting periods. In this case the enacted rate is 30%; this rate needs to be applied to arrive at the amount of any deferred taxes.

EXERCISE 18-8 (Continued)

(c)

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Equipment	\$8,500	\$8,000*	\$500	30%	\$150
FV-NI Investments	60,000	58,000	2,000	30%	600
FV-OCI Investments	71,000	75,000	(4,000)	30%	(1,200)
Deferred tax liability, December 31, 2014					(450)
Deferred tax asset/liability before adjustment					<u>0</u>
Incr. in deferred tax liability, and deferred tax expense for 2014					<u>(\$450)</u>

* (CCA is \$10,000 X 30% X 1/2 year rule = \$1,500)

(d)

Accounting income [excludes entries in part (a) as no tax effect]		\$110,000
Permanent difference:		
50% of meals and entertainment of \$24,000		<u>12,000</u>
		122,000
Reversing difference:		
Depreciation expense	\$2,000	
Capital cost allowance	<u>(1,500)</u>	<u>500</u>
Taxable income		<u>\$122,500</u>
Current income taxes at 25%		<u>\$30,625</u>

EXERCISE 18-8 (Continued)**(e)**

Current Tax Expense	30,625	
Income Tax Payable		30,625
Deferred Tax Asset.....	750	
Deferred Tax Benefit.....		750
Deferred Tax Expense—OCI.....	1,200	
Deferred Tax Liability		1,200
[((\$4,000 X 30%) – \$0]		

EXERCISE 18-9 (20-25 minutes)

(a) The investments must be reported on the statement of financial position at their fair value. The resulting difference between this and the tax base of the investments (cost of \$314,450) represents a temporary difference. The unrealized gain recognized is not taxable, and any unrealized loss recognized is not deductible, until the investments are sold at a gain or at a loss. The resulting taxable temporary difference must have the corresponding deferred tax recorded at the tax rate that Raman expects to pay (or recover in the case of a loss) on this gain or loss in future accounting periods. In this case the enacted rate is 30% that needs to be applied to arrive at the amount of any deferred taxes.

(b)

<u>Stmnt of Fin Pos Account</u>	<u>Tax Base</u>	<u>Carrying Amount</u>	<u>(Taxable) Temporary Difference</u>	<u>X Tax Rate</u>	<u>Deferred Tax (Liability)</u>
Invest. (FV-NI)	\$314,450	\$318,200	(\$3,750)	30%	(\$1,125)

(c)

Accounting income	\$302,000
Reversing difference: Unrealized gain on Investments (FV-NI)	<u>(3,750)</u>
Taxable income	<u>\$298,250</u>
Current income taxes at 30%	<u>\$89,475</u>

(d)

Current Tax Expense	89,475	
Income Tax Payable		89,475
Deferred Tax Expense.....	1,125	
Deferred Tax Liability		1,125
(\$1,125 – opening balance of \$0)		

EXERCISE 18-9 (Continued)

(e)	Income before income tax		\$302,000
	Income tax expense		
	Current	\$89,475	
	Deferred	<u>1,125</u>	<u>90,600</u>
	Net income		<u>\$211,400</u>

(f)	Current liabilities:	
	Income tax payable	\$89,475
	Non-current liabilities:	
	Deferred tax liability	\$ 1,125

Under IFRS, all deferred tax assets and liabilities are reported as non-current items on a classified statement of financial position.

(g)	Current liabilities:	
	Income tax payable	\$89,475
	Deferred tax liability	1,125

Current income taxes are due well within 12 months of the statement of financial position date, therefore, they are classified as a current liability.

The classification for the deferred tax account must also be current since the temporary difference relates to an asset that is classified as current on the statement of financial position. Under ASPE, deferred tax assets and deferred tax liabilities are segregated into current and non-current categories, so Raman's deferred tax liability would be classified as current on a classified statement of financial position.

EXERCISE 18-10 (15-20 minutes)

(a)

Statement of Financial Position Account Dec. 31, 2014	Tax Base*	Carrying Amount*	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Equipment	(\$95,000)	\$0	(\$95,000)	30%	<u>(\$28,500)</u>
Deferred tax liability, December 31, 2014					(28,500)
Deferred tax liability before adjustment					<u>0</u>
Increase in deferred tax liability, and deferred tax expense for 2014					<u>(\$28,500)</u>

* Values not provided in this exercise (\$25,000 + \$30,000 + \$40,000 = \$95,000)

	Future years			
	Total	2015	2016	2017
(Taxable) temporary differences				
Depreciation in excess of CCA	\$95,000	\$25,000	\$30,000	\$40,000
Tax rate enacted for the year		30%	30%	30%
Deferred tax liability	<u>\$28,500</u>	<u>\$7,500</u>	<u>\$9,000</u>	<u>\$12,000</u>

EXERCISE 18-10 (Continued)

(b)		<u>2014</u>
	Accounting income	\$200,000
	Permanent differences:	-0-
	Reversing difference:	
	CCA greater than depreciation	<u>95,000</u>
	Taxable income	<u>105,000</u>
	Current income taxes – 30%	<u><u>\$31,500</u></u>

(c)		
	Current Tax Expense	31,500
	Income Tax Payable	31,500
	Deferred Tax Expense.....	28,500
	Deferred Tax Liability	28,500

(d)	Income before income tax		\$200,000
	Income tax expense		
	Current	\$31,500	
	Deferred	<u>28,500</u>	<u>60,000</u>
	Net income		<u><u>\$140,000</u></u>

EXERCISE 18-11 (15-20 minutes)

(a) 2015

Statement of Financial Position Account Dec. 31, 2015	Tax Base*	Carrying Amount*	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Equipment	(\$70,000)	0	(\$70,000)	30%	<u>(\$21,000)</u>
Deferred tax liability, December 31, 2015					(21,000)
Deferred tax liability before adjustment					<u>(28,500)</u>
Decrease in deferred tax liability, and deferred tax benefit for 2015					<u>\$7,500</u>

* Values not provided in this exercise (\$30,000 + \$40,000 = \$70,000)

	Future years		
	Total	2016	2017
(Taxable) temporary differences			
Depreciation in excess of CCA	\$70,000	\$30,000	\$40,000
Tax rate enacted for the year		30%	30%
Deferred tax liability	<u>\$21,000</u>	<u>\$9,000</u>	<u>\$12,000</u>

EXERCISE 18-11 (Continued)

(a) (Continued) 2016

Statement of Financial Position Account Dec. 31, 2016	Tax Base*	Carrying Amount*	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Equipment	(\$40,000)	0	(\$40,000)	30%	<u>(\$12,000)</u>
Deferred tax liability, December 31, 2016					(\$12,000)
Deferred tax liability before adjustment					<u>(21,000)</u>
Decrease in deferred tax liability, and deferred tax benefit for 2016					<u>\$9,000</u>

* Values not provided in this exercise

	<u>Future year</u>	
	<u>Total</u>	<u>2017</u>
(Taxable) temporary differences		
Depreciation in excess of CCA	\$40,000	\$40,000
Tax rate enacted for the year		30%
Deferred tax liability	<u>\$12,000</u>	<u>\$12,000</u>

EXERCISE 18-11 (Continued)

(b)

	<u>2015</u>	<u>2016</u>
Pre-tax accounting income	\$ 180,000	\$ 180,000
Reversing differences –		
CCA < depreciation expense	<u>25,000</u>	<u>30,000</u>
Taxable income	<u>\$ 205,000</u>	<u>\$ 210,000</u>
Taxable income	\$ 205,000	\$ 210,000
Enacted tax rate	<u>X 30%</u>	<u>X 30%</u>
Current income tax expense	<u>\$ 61,500</u>	<u>\$ 63,000</u>

(c)

2015

Current Tax Expense	61,500	
Income Tax Payable		61,500
Deferred Tax Liability	7,500	
Deferred Tax Benefit.....		7,500

2016

Current Tax Expense	63,000	
Income Tax Payable		63,000
Deferred Tax Liability	9,000	
Deferred Tax Benefit.....		9,000

EXERCISE 18-11 (Continued)**(d)**

		<u>2015</u>
Income before income tax		\$ 180,000
Income tax		
Current	\$ 61,500	
Deferred (Benefit)	<u>(7,500)</u>	<u>54,000</u>
Net Income		<u><u>\$ 126,000</u></u>
		<u>2016</u>
Income before income tax		\$ 180,000
Income tax		
Current	\$ 63,000	
Deferred (Benefit)	<u>(9,000)</u>	<u>54,000</u>
Net Income		<u><u>\$ 126,000</u></u>

- (e) The net income is identical for 2015 and 2016. Although the temporary balances have changed, their changes were accrued at the expected tax rates in 2014. Subsequent reversals of balances in the temporary differences reduce the deferred tax liability account at the expected amounts each subsequent year.**

This trend in net income is not a coincidence. The net income remains constant due to the consistent amount of income before income tax.

EXERCISE 18-12 (15-20 minutes)

(a) 2015

Statement of Financial Position Account Dec. 31, 2015	Tax Base*	Carrying Amount*	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Equipment	(\$70,000)	0	(\$70,000)	25%	<u>(\$17,500)</u>
Deferred tax liability, December 31, 2015					(17,500)
Deferred tax liability before adjustment					<u>(28,500)</u>
Decrease in deferred tax liability, and deferred tax benefit for 2015					<u>\$11,000</u>

* Values not provided in this exercise

	Future years		
	Total	2016	2017
(Taxable) temporary differences			
Depreciation in excess of CCA	\$70,000	\$30,000	\$40,000
Tax rate enacted for the year		25%	25%
Deferred tax liability	<u>\$17,500</u>	<u>\$7,500</u>	<u>\$10,000</u>

EXERCISE 18-12 (Continued)

(a) (Continued) 2016

Statement of Financial Position Account Dec. 31, 2016	Tax Base*	Carrying Amount*	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Equipment	(\$40,000)	0	(\$40,000)	25%	(\$10,000)
Deferred tax liability, December 31, 2016					(10,000)
Deferred tax liability before adjustment					<u>(17,500)</u>
Decrease in deferred tax liability, and deferred tax benefit for 2016					<u>\$ 7,500</u>

* Values not provided in this exercise

	<u>Total</u>	<u>Future year 2017</u>
(Taxable) temporary differences		
Depreciation in excess of CCA	\$40,000	\$40,000
Tax rate enacted for the year		<u>25%</u>
Deferred tax liability	<u>\$10,000</u>	<u>\$10,000</u>

EXERCISE 18-12 (Continued)

(b)

	<u>2015</u>	<u>2016</u>
Pre-tax accounting income	\$ 180,000	\$ 180,000
Reversing differences –		
CCA < depreciation expense	<u>25,000</u>	<u>30,000</u>
Taxable income	<u>\$ 205,000</u>	<u>\$ 210,000</u>
Taxable income	\$ 205,000	\$ 210,000
Enacted tax rate	<u>X 30%</u>	<u>X 25%</u>
Current income tax expense	<u>\$ 61,500</u>	<u>\$ 52,500</u>

(c)

2015

Current Tax Expense	61,500	
Income Tax Payable		61,500
Deferred Tax Liability	11,000	
Deferred Tax Benefit.....		11,000

2016

Current Tax Expense	52,500	
Income Tax Payable		52,500
Deferred Tax Liability	7,500	
Deferred Tax Benefit.....		7,500

EXERCISE 18-12 (Continued)**(d)**

		<u>2015</u>
Income before income tax		\$ 180,000
Income tax		
Current	\$ 61,500	
Deferred (benefit)	(11,000)	50,500
Net Income		<u>\$ 129,500</u>
		<u>2016</u>
Income before income tax		\$ 180,000
Income tax		
Current	\$ 52,500	
Deferred (benefit)	(7,500)	45,000
Net Income		<u>\$ 135,000</u>

EXERCISE 18-13 (15-20 minutes)

(a)

Accounting income	\$105,000
Permanent differences:	
Non-deductible fines	<u>15,000</u>
	120,000
Reversing differences:	
Excess of CCA over depreciation	(16,000)
Excess rent collected over rent earned	<u>24,000</u>
Taxable income	<u>\$128,000</u>
Current income taxes – 30%	<u>\$38,400</u>

(b)

Statement of Fin Pos Account	Deductible (Taxable) Temporary Differences	X Rate	Deferred Tax Asset (Liability)	Current or Long- Term
PP & E	(\$16,000)*	30%	(\$4,800)	LT
Unearned rent revenue	24,000	30%	<u>7,200</u>	C
Deferred tax asset, Dec. 31, 2014			2,400	
Deferred tax asset before adjustment			<u>0</u>	
Incr. in deferred tax asset, and deferred tax benefit for 2014			<u>\$ 2,400</u>	

* Carrying amount and tax base are not given in the exercise, only the net difference is provided.

(c)

Current Tax Expense.....	38,400	
Income Tax Payable.....		38,400
Deferred Tax Asset.....	7,200*	
Deferred Tax Benefit.....		2,400
Deferred Tax Liability.....		4,800*
* or a net debit to Deferred Tax Asset of \$2,400		

EXERCISE 18-14 (15-20 minutes)

(a)

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Warranty liability	0	(\$150,000)	\$150,000	25%	\$37,500
Deferred tax asset, December 31, 2014					37,500
Deferred tax asset before adjustment					0
Increase in deferred tax asset, and deferred tax benefit for 2014					<u>\$37,500</u>

	<u>Future years</u>			
	<u>Total</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
Deductible temporary difference				
Warranty liability	\$150,000	\$50,000	\$35,000	\$65,000
Tax rate enacted for the year		25%	25%	25%
Deferred tax asset	<u>\$37,500</u>	<u>\$12,500</u>	<u>\$8,750</u>	<u>\$16,250</u>

EXERCISE 18-14 (Continued)

(b)		<u>2016</u>
Accounting income		\$135,000
Permanent differences:		-0-
Reversing difference:		
Warranty expense > warranty costs incurred		150,000
Taxable income		<u>285,000</u>
Current income taxes – 25%		<u><u>\$71,250</u></u>

(c)		
Current Tax Expense	71,250	
Income Tax Payable		71,250
Deferred Tax Asset.....	37,500	
Deferred Tax Benefit.....		37,500

(d)			
Income before income tax			\$135,000
Income tax expense			
Current		\$71,250	
Deferred (benefit)		<u>(37,500)</u>	<u>33,750</u>
Net income			<u><u>\$101,250</u></u>

EXERCISE 18-15 (15-20 minutes)

(a) 2015

Statement of Financial Position Account Dec. 31, 2015	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Warranty liability	0	(\$100,000)	\$100,000	25%	<u>\$25,000</u>
Deferred tax asset, December 31, 2015					25,000
Deferred tax asset before adjustment					<u>37,500</u>
Decrease in deferred tax asset, and deferred tax expense for 2015					<u><u>(\$12,500)</u></u>

	Future years		
	Total	2016	2017
Deductible temporary difference			
Warranty liability	\$100,000	\$35,000	\$65,000
Tax rate enacted for the year		<u>25%</u>	<u>25%</u>
Deferred tax asset	<u>\$25,000</u>	<u>\$8,750</u>	<u>\$16,250</u>

EXERCISE 18-15 (Continued)

(a) (Continued) 2016

Statement of Financial Position Account Dec. 31, 2016	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Warranty liability	0	(\$65,000)	\$65,000	25%	<u>\$16,250</u>
Deferred tax asset, December 31, 2016					16,250
Deferred tax asset before adjustment					<u>25,000</u>
Decrease in deferred tax asset, and deferred tax expense for 2016					<u>(\$8,750)</u>

	Future year	
	Total	2017
Deductible temporary difference		
Warranty liability	\$65,000	\$65,000
Tax rate enacted for the year		25%
Deferred tax asset	<u>\$16,250</u>	<u>\$16,250</u>

EXERCISE 18-15 (Continued)**(b)**

	<u>2015</u>	<u>2016</u>
Pre-tax accounting income	\$ 155,000	\$ 155,000
Reversing difference – Warranty costs incurred > warranty expense	(50,000)	(35,000)
Taxable income	<u>\$ 105,000</u>	<u>\$ 120,000</u>
Taxable income	\$ 105,000	\$ 120,000
Enacted tax rate	X 25%	X 25%
Current income tax expense	<u>\$ 26,250</u>	<u>\$ 30,000</u>

(c)**2015**

Current Tax Expense	26,250	
Income Tax Payable		26,250
Deferred Tax Expense.....	12,500	
Deferred Tax Asset.....		12,500

2016

Current Tax Expense	30,000	
Income Tax Payable		30,000
Deferred Tax Expense.....	8,750	
Deferred Tax Asset.....		8,750

EXERCISE 18-15 (Continued)**(d)**

		<u>2015</u>
Income before income tax		\$ 155,000
Income tax		
Current	\$ 26,250	
Deferred	12,500	38,750
	<u> </u>	<u> </u>
Net Income		<u>\$ 116,250</u>
		<u>2016</u>
Income before income tax		\$ 155,000
Income tax		
Current	\$ 30,000	
Deferred	8,750	38,750
	<u> </u>	<u> </u>
Net Income		<u>\$ 116,250</u>

(e) The net income is identical for 2015 and 2016. Although the temporary balances have changed, their changes were accrued at the expected future income tax rates in 2014. Subsequent reversals of balances in the temporary differences reduce the deferred tax asset account at the expected amounts each subsequent year.

This trend in net income is not a coincidence. The net income remains constant due to the consistent amount of income before income tax.

EXERCISE 18-16 (20-25 minutes)

(a)

Unrealized Gain or Loss	2,000	
FV-NI Investments		2,000

(b) As discussed in Exercise 18-9 the difference between the carrying amount (\$40,000) and the tax base (\$42,000) at December 31, 2015 is a temporary difference. The loss is not deductible until the investments are sold. The resulting deductible temporary difference must have the corresponding deferred tax recorded at the tax rate that Raman expects to recover on this loss in future accounting periods. In this case the enacted rate of 30% needs to be applied to arrive at the amount of any deferred taxes.

(c)

<u>Stmnt of Fin Pos Account</u>	<u>Tax Base</u>	<u>– Carrying Amount</u>	<u>= Deductible Temporary Difference</u>	<u>X Tax Rate</u>	<u>Deferred Tax Asset (Liability)</u>
Invest. (FV-NI)	\$42,000	\$40,000	\$2,000	30%	\$600
Balance before adjustment					<u>(1,125)</u>
Adj. to deferred tax account, and deferred tax benefit for 2015					<u>\$1,725</u>

(d)

Accounting income	\$120,000
Reversing difference: Unrealized loss on Invest. (FV-NI)	2,000
Reversing difference: 2014 Unrealized gain realized in 2015	<u>3,750</u>
Taxable income	<u>\$125,750</u>
Current income taxes at 30%	<u>\$37,725</u>
 Current tax expense for 2015	 \$37,725

EXERCISE 18-16 (Continued)

(e)		
Current Tax Expense	37,725	
Income Tax Payable		37,725
Deferred Tax Asset.....	600*	
Deferred Tax Liability.....	1,125*	
Deferred Tax Benefit.....		1,725

*** Alternatively, if one statement of financial position account—a Deferred Tax Asset/Liability account—is used, a debit balance indicating an asset and a credit balance indicating a liability, the entry would be:**

Deferred Tax Asset/Liability	1,725	
Deferred Tax Benefit.....		1,725

(f)	Income before income tax		\$120,000
	Income tax expense		
	Current	\$37,725	
	Deferred (benefit)	<u>(1,725)</u>	<u>36,000</u>
	Net income		<u>\$84,000</u>

(g)	Non-current assets	
	Deferred tax asset	\$600

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

EXERCISE 18-16 (Continued)

(h)

<u>Stmnt of Fin Pos Account</u>	<u>Tax Base</u>	<u>–</u>	<u>Carrying Amount</u>	<u>=</u>	<u>Deductible Temporary Difference</u>	<u>X</u>	<u>Tax Rate</u>	<u>Deferred Tax Asset (Liability)</u>
Invest. (FV-NI)	\$42,000		\$40,000		\$2,000		28%	\$560
Balance before adjustment								<u>(1,125)</u>
Adj. to deferred tax account, and deferred tax benefit for 2015								<u>\$1,685</u>
Current Tax Expense						37,725		
Income Tax Payable								37,725
Deferred Tax Asset.....						560*		
Deferred Tax Liability.....						1,125*		
Deferred Tax Benefit.....								1,685
* or Deferred Tax Asset/Liability						1,685		
(i) Current assets								
Deferred tax asset						\$600		

The classification must be current since the temporary difference relates to an asset that is classified as current on the statement of financial position.

EXERCISE 18-17 (20-25 minutes)

(a) 2015

Statement of Financial Position Account Dec. 31, 2015	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Warranty liability	\$0	(\$100,000)	\$100,000	28%	<u>\$28,000</u>
Deferred tax asset, December 31, 2015					28,000
Deferred tax asset before adjustment					<u>37,500</u>
Decrease in deferred tax asset, and deferred tax expense for 2015					<u>(\$9,500)</u>

	Future years		
	Total	2016	2017
Deductible temporary difference			
Warranty liability	\$100,000	\$35,000	\$65,000
Tax rate enacted for the year		28%	28%
Deferred tax asset	<u>\$28,000</u>	<u>\$9,800</u>	<u>\$18,200</u>

EXERCISE 18-17 (Continued)

(a) (Continued) 2016

Statement of Financial Position Account Dec. 31, 2016	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Warranty liability	\$0	(\$65,000)	\$65,000	28%	<u>\$18,200</u>
Deferred tax asset, December 31, 2016					18,200
Deferred tax asset before adjustment					<u>28,000</u>
Decrease in deferred tax asset, and deferred tax expense for 2016					<u>(\$9,800)</u>

	<u>Total</u>	<u>Future year 2017</u>
Deductible temporary difference		
Warranty liability	\$65,000	\$65,000
Tax rate enacted for the year		28%
Deferred tax asset	<u>\$18,200</u>	<u>\$18,200</u>

EXERCISE 18-17 (Continued)

(b)

	<u>2015</u>	<u>2016</u>
Pre-tax accounting income	\$ 155,000	\$ 155,000
Reversing difference – Warranty costs incurred > warranty expense	<u>(50,000)</u>	<u>(35,000)</u>
Taxable income	<u>\$ 105,000</u>	<u>\$ 120,000</u>
Taxable income	\$ 105,000	\$ 120,000
Enacted tax rate	<u>X 25%</u>	<u>X 28%</u>
Current income tax expense	<u>\$ 26,250</u>	<u>\$ 33,600</u>

(c)

2015

Current Tax Expense	26,250	
Income Tax Payable		26,250
Deferred Tax Expense.....	9,500	
Deferred Tax Asset.....		9,500

2016

Current Tax Expense	33,600	
Income Tax Payable		33,600
Deferred Tax Expense.....	9,800	
Deferred Tax Asset.....		9,800

EXERCISE 18-17 (Continued)

(d)

		<u>2015</u>
Income before income tax		\$ 155,000
Income tax		
Current	\$ 26,250	
Deferred	9,500	35,750
	<hr/>	<hr/>
Net Income		\$ 119,250
		<hr/> <hr/>
		<u>2016</u>
Income before income tax		\$ 155,000
Income tax		
Current	\$ 33,600	
Deferred	9,800	43,400
	<hr/>	<hr/>
Net Income		\$ 111,600
		<hr/> <hr/>

EXERCISE 18-18 (40-45 minutes)

(a)

Basic Calculations of Capital Cost Allowance, Amounts and Balances:

<u>Year</u>	<u>(A) Base</u>		<u>(B) CCA</u>	<u>A – B UCC</u>	<u>(C) Deprec.</u>	<u>Carrying Amount</u>	<u>C – B Reversing Difference</u>
2014	\$600,000	X 40 % X .5	\$ 120,000	\$ 480,000	\$120,000	\$480,000	\$0
2015	480,000	X 40 %	192,000	288,000	120,000	360,000	(72,000)
2016	288,000	X 40 %	115,200	172,800	120,000	240,000	4,800
2017	172,800	X 40 %	69,120	103,680	120,000	120,000	50,880
2018	103,680	X 40 %	<u>41,472</u>	62,208	120,000	0	78,528
			<u>\$537,792</u>				

(b)

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>
Accounting income	\$ 340,000	\$340,000	\$340,000	\$340,000	\$ 340,000
Reversing difference	-0-	(72,000)	4,800	50,880	78,528
Taxable income	<u>\$ 340,000</u>	<u>\$268,000</u>	<u>\$344,800</u>	<u>\$390,880</u>	<u>\$ 418,528</u>
	X 34 %	X 34 %	X 34 %	X 34 %	X 34 %
Income tax payable	<u>\$115,600</u>	<u>\$91,120</u>	<u>\$117,232</u>	<u>\$132,899</u>	<u>\$142,300</u>

EXERCISE 18-18 (Continued)

**(c) and (d)
2014**

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Property, plant, & equipment	\$480,000	\$480,000	0	34%	\$0
Deferred tax asset/liability, December 31, 2014					0
Deferred tax asset/liability before adjustment					<u>0</u>
Increase in deferred tax liability, and deferred tax expense for 2014					<u>\$0</u>

Current Tax Expense	115,600	
Income Tax Payable		115,600
(\$340,000 X 34%) part (b)		

EXERCISE 18-18 (Continued)

**(c) and (d) continued
2015**

Statement of Financial Position Account Dec. 31, 2015	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Property, plant, & equipment	\$288,000	\$360,000	(72,000)	34%	<u>(\$24,480)</u>
Deferred tax liability, December 31, 2015					(24,480)
Deferred tax liability before adjustment					<u>0</u>
Increase in deferred tax liability, and deferred tax expense for 2015					<u>(\$24,480)</u>

Current Tax Expense	91,120	
Income Tax Payable		91,120
(\$268,000 X 34%) part (b)		
 Deferred Tax Expense.....	 24,480	
Deferred Tax Liability		24,480

EXERCISE 18-18 (Continued)

**(c) and (d) continued
2016**

Statement of Financial Position Account Dec. 31, 2016	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Property, plant, & equipment	\$172,800	\$240,000	(\$67,200)	34%	<u>(\$22,848)</u>
Deferred tax liability, December 31, 2016					(22,848)
Deferred tax liability before adjustment					<u>(24,480)</u>
Decrease in deferred tax liability, and deferred tax benefit for 2016					<u>\$1,632</u>

2016

Current Tax Expense	117,232	
Income Tax Payable		117,232
(\$344,800 X 34%) part (b)		
Deferred Tax Liability	1,632	
Deferred Tax Benefit.....		1,632

EXERCISE 18-18 (Continued)

**(c) and (d) continued
2017**

Statement of Financial Position Account Dec. 31, 2017	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Property, plant & equipment	\$103,680	\$120,000	(\$16,320)	34%	<u>(\$5,549)</u>
Deferred tax liability, December 31, 2017					(5,549)
Deferred tax liability before adjustment					<u>(22,848)</u>
Decrease in deferred tax liability, and deferred tax benefit for 2017					<u>\$17,299</u>

2017

Current Tax Expense	132,899	
Income Tax Payable		132,899
(\$390,880 X 34%) part (b)		
Deferred Tax Liability	17,299	
Deferred Tax Benefit.....		17,299

EXERCISE 18-18 (Continued)

**(c) and (d) continued
2018**

Statement of Financial Position Account Dec. 31, 2018	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Property, plant, & equipment	\$62,208	\$0	\$62,208	34%	\$21,151
Deferred tax asset, December 31, 2018					21,151
Deferred tax liability before adjustment					<u>(5,549)</u>
Increase in deferred tax asset, and deferred tax benefit for 2018					<u>\$26,700</u>

2018

Current Tax Expense	142,300	
Income Tax Payable		142,300
(\$418,528 X 34%) part (b)		
Deferred Tax Liability	5,549*	
Deferred Tax Asset	21,151*	
Deferred Tax Benefit		26,700

***Alternately, a net debit to Deferred Tax Asset/Liability of \$26,700 if only one account is used.**

EXERCISE 18-18 (Continued)

(e)

2014

Current Tax Expense.....	115,600	
Income Tax Payable.....		115,600
(\$340,000 X 34%)		

2015

Current Tax Expense.....	91,120	
Income Tax Payable.....		91,120
(\$268,000 X 34%)		

2016

Current Tax Expense.....	117,232	
Income Tax Payable.....		117,232
(\$344,800 X 34%)		

2017

Current Tax Expense.....	132,899	
Income Tax Payable.....		132,899
(\$390,880 X 34%)		

2018

Current Tax Expense.....	142,300	
Income Tax Payable.....		142,300
(\$418,528 X 34%)		

EXERCISE 18-19 (15-20 minutes)**(a)**

	Future Years		Total
	2015	2016	
	Current	Non-current**	
Future taxable amounts	\$1,650,000	\$1,650,000	<u>\$3,300,000</u>
Tax rate	30% *	29%	
Deferred tax liab.	<u>\$ 495,000</u>	<u>\$ 478,500</u>	<u>\$973,500</u>

* The prior tax rate of 30% is calculated by dividing the \$990,000 balance of the deferred tax liability account at January 1, 2014, by the \$3,300,000 temporary difference at that same date.

** One-half of the instalment receivable is classified as a current asset and one-half is non-current. Therefore, under ASPE the deferred tax liability related to the portion of the receivable coming due in 2015 is current and the deferred tax liability balance related to the portion of the receivable coming due in 2016 is non-current.

(b)

Under IFRS, all deferred tax balances are reported as non-current in a classified statement of financial position. Therefore, the non-current deferred tax liability is reported as \$973,500.

EXERCISE 18-19 (Continued)

(c)

Statement of Financial Position Account	(Taxable) Temporary Differences	X	Tax Rate	Deferred Tax (Liability)
Receivable	(\$3,300,000)*		several	<u>(\$973,500)</u>
Deferred tax liability, as revised				<u>(973,500)</u>
Deferred tax liability before rate adjustment				<u>(990,000)</u>
Decr. in deferred tax liability, and deferred tax benefit for 2014 from tax rate change				<u>\$16,500</u>
Deferred Tax Liability				16,500
Deferred Tax Benefit				16,500

EXERCISE 18-20 (20-25 minutes)

(a)

	Future Years				Total
	2015	2016	2017	2018	
Future taxable amounts	\$67,000	\$50,000	\$45,000	\$39,000	<u>\$201,000</u>
Enacted tax rate	<u>30%</u>	<u>30%</u>	<u>25%</u>	<u>25%</u>	
Future tax liability	<u>\$20,100</u>	<u>\$15,000</u>	<u>\$11,250</u>	<u>\$ 9,750</u>	<u>\$ 56,100</u>

(b)

Statement of Financial Position Account	(Taxable) Temporary Differences	X	Tax Rate	Deferred Tax (Liability)
Prop., plant, & equip.	(\$201,000)*		several	<u>(\$56,100)</u>
Deferred tax liability, Dec. 31, 2014				(56,100)
Deferred tax liability before adjustment				<u>(31,000)</u>
Incr. in deferred tax liability, and deferred tax expense for 2014				<u>(\$25,100)</u>

* Carrying amount and tax base are not given in the exercise, only the net difference is provided.

Deferred Tax Expense	25,100	
Deferred Tax Liability		25,100

EXERCISE 18-20 (Continued)

(c)

	Future Years				Total
	2015	2016	2017	2018	
Future taxable amounts	\$67,000	\$50,000	\$45,000	\$39,000	<u>\$201,000</u>
Enacted tax rate	<u>29%</u>	<u>27%</u>	<u>27%</u>	<u>27%</u>	
Future tax liability	<u>\$19,430</u>	<u>\$13,500</u>	<u>\$12,150</u>	<u>\$10,530</u>	<u>\$ 55,610</u>

Statement of Financial Position Account	(Taxable) Temporary Differences	X	Tax Rate	Deferred Tax (Liability)
Prop., plant, & equip.	(\$201,000)*		several	<u>(\$55,610)</u>
Deferred tax liability, revised balance				(55,610)
Deferred tax liability before adjustment [part (b)]				<u>(56,100)</u>
Decr. in deferred tax liability, and deferred tax benefit for 2015				<u>\$490</u>

* Carrying amount and tax base are not given in the exercise, only the net difference is provided.

Deferred Tax Liability	490	
Deferred Tax Benefit		490

Note to Instructor: The journal entry above is effective and should be made at the time the new rates were substantively enacted or, if financial statements are prepared only annually, it would be combined with other year-end adjustments for 2015 income tax that record the income tax expense.

EXERCISE 18-21 (20-25 minutes)

(a)

2011		
Current Tax Expense	30,000	
Income Tax Payable (\$120,000 X 25%) .		30,000
2012		
Current Tax Expense	22,500	
Income Tax Payable (\$90,000 X 25%) ...		22,500
2013		
Income Tax Receivable	52,500	
Current Tax Benefit		52,500*
* (25% X (\$120,000 + \$90,000))		

This leaves \$280,000 - \$210,000 = \$70,000 of tax losses available for carryforward. No entry can be made to record any tax benefit from the remaining \$70,000 of tax losses because it is not more likely than not that the company will actually benefit from them. However, the existence of the \$70,000 loss carryforward should be disclosed in a note.

2014

In 2014, the company earned \$40,000 of taxable income and it can deduct \$40,000 of the \$70,000 tax loss carryforward from this. They report a taxable income amount in 2014 of \$-0-. Because they are still uncertain about being able to benefit from the remaining \$30,000 of tax losses in the future, no entry is made to recognize the benefit in the year, but this amount must be disclosed in a note. Income tax expense in 2014 is \$-0-.

Alternatively, both a current tax expense of \$40,000 X 30% = \$12,000 and a current tax benefit from previously unrecognized tax losses available for carryforward of \$40,000 X 30% = \$12,000 could both be recognized and reported.

EXERCISE 18-21 (Continued)**(b)**

2011		
Income (loss) before income tax		\$120,000
Income tax expense – current		<u>30,000</u>
Net income		<u>\$90,000</u>

2012		
Income (loss) before income tax		\$90,000
Income tax expense – current		<u>22,500</u>
Net income		<u>\$67,500</u>

2013		
Income (loss) before income tax		\$(280,000)
Current tax benefit due to loss carryback		<u>52,500</u>
Net loss		<u>\$(227,500)</u>

2014		
Income (loss) before income tax		\$40,000
Current tax expense		<u>-0-</u>
Net income		<u>\$40,000</u>

Or, alternatively:

Income before income tax		\$40,000
Current tax expense	\$12,000	
Current tax benefit from unrecognized tax losses carried forward	<u>(12,000)</u>	<u>-0-</u>
Net income		<u>\$40,000</u>

EXERCISE 18-22 (15-20 minutes)

2011		
Current Tax Expense.....	22,400	
Income Tax Payable (\$80,000 X 28%)		22,400

2012		
Income Tax Receivable	51,200	
(\$160,000 X 32%)		
Current Tax Benefit		51,200

2013

The 2013 loss of \$380,000 is carried back \$250,000 to 2010 and \$80,000 to 2011, leaving \$50,000 to carry forward.

Income Tax Receivable	102,400	
Current Tax Benefit		102,400
(\$250,000 X 32% + \$80,000 X 28%)		

Deferred Tax Asset.....	14,000	
Deferred Tax Benefit.....		14,000
(\$50,000 X 28%) - \$-0-		

2014		
Current Tax Expense.....	22,400	
Income Tax Payable		22,400
[28% X (\$130,000 – \$50,000 loss carryforward)]		

Deferred Tax Expense.....	14,000	
Deferred Tax Asset		14,000
(\$0 – \$14,000)		

2015		
Current Tax Expense.....	40,600	
Income Tax Payable (\$145,000 X 28%)		40,600

EXERCISE 18-23 (30-35 minutes)

(a)

2012		
Current Tax Expense	40,800	
Income Tax Payable (\$120,000 X 34%)		40,800

2013		
Current Tax Expense	30,600	
Income Tax Payable (\$90,000 X 34%) ..		30,600

2014

The 2014 loss of \$280,000 is carried back, \$120,000 to 2012 and \$90,000 to 2013, leaving \$70,000 to carryforward.

Income Tax Receivable	71,400	
Current Tax Benefit		71,400*

Deferred Tax Asset	26,600	
Deferred Tax Benefit		26,600**

*[34% X \$120,000] + [34% X \$90,000] = \$71,400
 **38% X (\$280,000 – \$120,000 – \$90,000) = \$26,600

2015		
Current Tax Expense	57,000	
Income Tax Payable		57,000*
*[((\$220,000 – \$70,000) X 38%]		
Deferred Tax Expense	26,600	
Deferred Tax Asset.....		26,600
(\$0 – \$26,600)		

EXERCISE 18-23 (Continued)

(b)	2014	
	Income (loss) before income tax	\$(280,000)
	Income tax benefit	
	Current benefit due to loss carryback	\$71,400
	Deferred benefit due to loss carryforward	<u>26,600</u>
		<u>98,000</u>
	Net loss	<u><u>\$(182,000)</u></u>

	2015	
	Income (loss) before income tax	\$220,000
	Income tax	
	Current tax expense	\$57,000
	Deferred tax expense	<u>26,600</u>
		<u>83,600</u>
	Net income	<u><u>\$136,400</u></u>

(c)	2014	
	Income Tax Receivable	71,400
	Current Tax Benefit	71,400*
	Deferred Tax Asset	19,950
	Deferred Tax Benefit	19,950**

*[34% X \$120,000] + [34% X \$90,000] = \$71,400
 **38% X (\$280,000 – \$120,000 – \$90,000) =
 \$26,600 X 75% = \$19,950

	2015	
	Current Tax Expense	57,000
	Income Tax Payable	57,000
	[((\$220,000 – \$70,000) X 38%]	
	Deferred Tax Expense	19,950
	Deferred Tax Asset.....	19,950
	(\$0 – \$19,950)	

EXERCISE 18-23 (Continued)

(d)	2014	
Income (loss) before income tax		\$(280,000)
Income tax benefit		
Current benefit due to loss carryback	\$71,400	
Deferred benefit due to loss carryforward	<u>19,950</u>	<u>91,350</u>
Net loss		<u>\$(188,650)</u>

	2015	
Income (loss) before income tax		\$220,000
Income tax		
Current tax expense	\$57,000	
Deferred tax expense	<u>19,950</u>	<u>76,950</u>
Net income		<u>\$143,050</u>

Note: For tax planning purposes, if the corporation anticipates profitable years ahead, it may not carry back its losses in order to take advantage of the higher rates for 2015 and beyond. The loss carryback is optional.

EXERCISE 18-24 (30-35 minutes)

(a)		2014	
Income Tax Receivable	71,400		
Current Tax Benefit			71,400
[34% X \$120,000] + [34% X \$90,000] = \$71,400			
 Deferred Tax Asset.....	 26,600		
Deferred Tax Benefit			26,600
38% X (\$280,000 – \$120,000 – \$90,000) = \$26,600			
 Deferred Tax Benefit..	 6,650		
Allowance to Reduce Deferred Tax			
Asset to Expected Realizable Value ...			6,650
(\$26,600 X 25%)			
		2015	
Current Tax Expense.....	57,000		
Income Tax Payable.....			57,000*
*[((\$220,000 – \$70,000) X 38%]			
 Deferred Tax Expense.....	 26,600		
Deferred Tax Asset			26,600
(\$0 – \$26,600)			
 Allowance to Reduce Deferred Tax			
Asset to Expected Realizable Value	6,650		
Deferred Tax Expense			6,650

EXERCISE 18-24 (Continued)

(b)	2014	
	Operating loss before income tax	\$(280,000)
	Income tax benefit	
	Current benefit due to loss carryback	\$71,400
	Deferred benefit due to loss carryforward	<u>19,950</u>
		<u>91,350</u>
	Net loss	<u><u>\$(188,650)</u></u>

	2015	
	Operating income before income tax	\$220,000
	Income tax	
	Current tax expense	\$57,000
	Deferred tax expense	<u>19,950</u>
		<u>76,950</u>
	Net income	<u><u>\$143,050</u></u>

(c)		2014	2015
	Current assets:	<u> </u>	<u> </u>
	Deferred Tax Asset	\$ 26,600	-
	Less: Allowance to Reduce Deferred Tax Asset to Expected Realizable Value	(6,650)	-
	Deferred Tax Asset (net)	<u><u>\$ 19,950</u></u>	<u><u>-</u></u>

- (d) Both the Deferred Tax Asset account and the Allowance to Reduce Deferred Tax Asset to Expected Realizable Value account should be adjusted for the change in the enacted tax rates for 2015. This adjustment should be recorded in the accounts as soon as it is known and can be measured.**
- (e) The only difference is the deferred tax asset would be classified as a non-current asset on the statement of financial position, and a valuation allowance may not be used. Instead, the Deferred Tax Asset account would be \$19,950.**

EXERCISE 18-25 (20-25 minutes)

(a) Current Tax Expense	310,450	
Income Tax Payable		310,450

Taxable income	\$887,000
Enacted tax rate	X 35%
Income tax payable	<u>\$310,450</u>

<u>Statement of Financial Position Account</u>	<u>Deductible Temporary Differences</u>	X	<u>Tax Rate</u>	<u>Deferred Tax Asset</u>
Warranty Liabilities	\$315,000*		35%	<u>\$110,250</u>
Deferred tax asset, Dec. 31, 2014				110,250
Deferred tax asset before adjustment				<u>101,500</u>
Incr. in deferred tax asset, and deferred tax benefit for 2014				<u>\$8,750</u>

* Carrying amount and tax base are not given in the exercise, only the net difference

Deferred Tax Asset	8,750	
Deferred Tax Benefit		8,750

EXERCISE 18-25 (Continued)

(b) (1.)

	2014	
Current Tax Expense	310,450	
Income Tax Payable		310,450

Statement of Financial Position Account	Deductible Temporary Differences	X	Tax Rate	Deferred Tax Asset
Warranty Liabilities	\$315,000*		35%	\$110,250
Less amount not likely to be realized				<u>(25,000)</u>
Deferred tax asset, Dec. 31, 2014				85,250
Deferred tax asset before adjustment				<u>101,500</u>
Decr. in deferred tax asset and deferred tax expense for 2014				<u>(\$16,250)</u>

* Carrying amount and tax base are not given in the exercise, only the net difference

Deferred Tax Expense	16,250	
Deferred Tax Asset.....		16,250

(b) (2.)

	2015	
Deferred Tax Asset	25,000	
Deferred Tax Benefit		25,000

Note to instructor:

This entry would be combined with the other entries for the year that would be setting up any deferred tax asset or liability for current year activity.

EXERCISE 18-26 (20-25 minutes)

(a)		
Current Tax Expense.....	310,450	
Income Tax Payable.....		310,450
Deferred Tax Asset.....	8,750	
Deferred Tax Benefit		8,750
(\$110,250 – \$101,500)		
Deferred Tax Expense.....	25,000	
Allowance to Reduce Deferred Tax		
Asset to Expected Realizable Value		25,000
(b)		
Allowance to Reduce Deferred Tax		
Asset to Expected Realizable Value.....	25,000	
Deferred Tax Benefit.....		25,000

EXERCISE 18-27 (10-15 minutes)

(a)	Resulting		Related	(b)
Temporary	Deferred Tax		Stmt of	(ASPE)
Difference	Asset	Liability	Fin Pos	Classi-
Deprec.		(\$230,000)	Plant Assets	fication
Litigation			Lawsuit	
Loss	\$80,000		Obligation	Current
Instalment			Instalment	
Sale	<u> </u>	(225,000)	Receivable	Noncurrent
Totals	<u>\$80,000</u>	<u>(\$455,000)</u>		

Long-term liabilities

Deferred tax liability	\$ 375,000
(\$455,000 – \$80,000)	

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

(b)

Current assets

Deferred tax asset	\$ 80,000
--------------------	------------------

Long-term liabilities

Deferred tax liability	455,000
------------------------	----------------

Under ASPE, deferred tax assets and deferred tax liabilities are segregated into current and non-current categories. The classification of an individual deferred tax liability or asset as current or non-current is determined by the classification of the asset or liability underlying the specific temporary difference.

EXERCISE 18-28 (25-30 minutes)**(a)****Calculation of current income tax expense:**

	Income from Continuing Operations	Discon- tinued Operations	Total
Accounting income:			
Revenue	\$273,000	\$118,000	
Expenses	<u>216,000</u>	<u>110,500</u>	
	57,000	7,500	\$64,500
Permanent differences:			
Non-taxable dividends	(1,700)		(1,700)
Golf club dues	4,500		4,500
Reversing differences:			
CCA > depreciation	(3,700)		(3,700)
Litigation loss	<u> </u>	<u>5,100</u>	<u>5,100</u>
Taxable income	<u>\$56,100</u>	<u>\$12,600</u>	<u>\$68,700</u>
Current income taxes for 2014 @ 35%	<u>\$19,635</u>	<u>\$4,410</u>	<u>\$24,045</u>

Calculation of deferred tax expense, continuing operations:

Statement of Financial Position Account	(Taxable) Temporary Differences	X	Tax Rate	Deferred Tax (Liability)
PP&E	(\$3,700)*		35%	<u>(\$1,295)</u>
Deferred tax liability, Dec. 31, 2014				(1,295)
Deferred tax liability before adjustment				<u>0</u>
Incr. in deferred tax liability, and deferred tax expense for 2014 for continuing operations				<u>(\$1,295)</u>

* Carrying amount and tax base are not given in the exercise, only the net difference is provided.

EXERCISE 18-28 (Continued)**Calculation of deferred tax expense, discontinued operations:**

<u>Statement of Financial Position Account</u>	<u>Deductible Temporary Differences</u>	X	<u>Tax Rate</u>	<u>Deferred Tax Asset</u>
Litigation Liability	\$5,100*		35%	<u>\$1,785</u>
Deferred tax asset, Dec. 31, 2014				1,785
Deferred tax asset before adjustment				<u>0</u>
Incr. in deferred tax asset, and deferred tax benefit for 2014 – for Disc. Operations				<u>\$1,785</u>

* Carrying amount and tax base are not given in the exercise, only the net difference is provided.

(b) Current Tax Expense	19,635	
Current Tax Expense – Discontinued Operations	4,410	
Income Tax Payable		24,045
Deferred Tax Expense	1,295	
Deferred Tax Liability		1,295
Deferred Tax Asset	1,785	
Deferred Tax Benefit – Discontinued Operations		1,785

EXERCISE 18-28 (Continued)**(c)**

Income before income tax and discontinued operations			\$ 57,000
Income tax			
Current tax	\$ 19,635		
Deferred tax	1,295	20,930	
		<hr/>	
Income from continuing operations			36,070
Income from discontinuing operations	7,500		
Net of applicable income tax:			
Current tax	\$4,410		
Deferred tax	(1,785)	2,625	4,875
		<hr/>	
Net Income			<u>\$40,945</u>

Earnings per share:

Income from continuing operations	\$3.60
Income from discontinuing operations	<u>0.49</u>
Net Income	<u>\$4.09</u>

(d)

Non-current assets	
Deferred tax asset (\$1,785 – \$1,295)	\$490

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

EXERCISE 18-28 (Continued)

(e)

Current assets	
Deferred tax asset	\$1,785
Non-current liabilities	
Deferred tax liability	1,295

Under ASPE, deferred tax assets and deferred tax liabilities are segregated into current and non-current categories. The classification of an individual deferred tax liability or asset as current or non-current is determined by the classification of the asset or liability underlying the specific temporary difference.

EXERCISE 18-29 (15-20 minutes)

(a) Current Tax Expense	89,475	
Income Tax Payable		89,475

(b) Income before income tax	\$302,000	
Income tax expense		<u>89,475</u>
Net income		<u>\$212,525</u>

(c) Current liabilities:		
Income tax payable	\$89,475	

(d)

Additional disclosures would include a statement that the taxes payable method is being used and a brief description of what it entails, along with:

- 1. income tax expense or benefit included in determining income (loss) before discontinued operations; and the amount related to transactions recognized in equity;**
- 2. a reconciliation of the actual tax rate or expense or benefit to the statutory amount for income (loss) before discontinued operations, with information about major reconciling items;**
- 3. the amount of reserves to be included in taxable income in each of the next five years; and the amount of unused income tax credits and losses carried forward.**

(e) Raman is providing all of the necessary and relevant disclosure as mentioned in (d) above. Creditors can therefore interpret the effect of adopting the taxes payable or differential method of accounting for the income tax accounts. Creditors will also understand Raman’s motivation in adopting this method. The benefits of the alternative method are likely exceeded by unnecessary and possibly excessive costs of providing the additional information.

EXERCISE 18-30 (10-15 minutes)

(a)		
Accounting income		\$105,000
Permanent differences:		
Non-deductible fines		<u>15,000</u>
		120,000
Reversing differences:		
Excess of CCA over depreciation		<u>(16,000)</u>
Excess rent collected over rent earned		<u>24,000</u>
Taxable income		<u>\$128,000</u>
Current income taxes – 30%		<u><u>\$38,400</u></u>

(b)	Current Tax Expense	38,400
	Income Tax Payable	38,400

(c)	Income before income tax	\$105,000
	Income tax expense	<u>38,400</u>
	Net income	<u><u>\$66,600</u></u>

(d)	Current assets	
	Income tax receivable	\$3,600
	(\$42,000 – \$38,400)	

EXERCISE 18-31 (15-20 minutes)

(a)

Accounting income before adjustments	\$185,000
Add: 50% meals and entertainment	10,000
Less: CCA in excess of depreciation	(25,000)
Taxable income	<u>\$170,000</u>
Income tax expense @ 28%	<u>\$47,600</u>

Current Tax Expense	47,600
Income Tax Payable	47,600

(b)

Effective Tax Rate = \$47,600/\$185,000	25.7%
Adjustment for permanent differences	
= (\$10,000 x 28%)/\$185,000	(1.5%)
Adjustment for reversing differences	
= (\$25,000 x 28%)/\$185,000	<u>3.8%</u>
Statutory Tax Rate	<u>28.0%</u>

TIME AND PURPOSE OF PROBLEMS

Problem 18-1 (Time 30-35 minutes)

Purpose—to test a student's ability to differentiate between permanent and temporary differences, calculate and classify and record current and deferred taxes as well as prepare a partial income statement and statement of financial position. The student in this case is dealing with a single tax rate and opening balances to the deferred tax accounts related to a single temporary difference.

Problem 18-2 (Time 45-50 minutes)

Purpose—to test a student's ability to calculate and classify deferred taxes for five temporary differences, while dealing with an opening balance in the deferred tax asset account. Student must deal with three years and two tax rates and is required to draft the income statement for the year as well as arrive at statement of financial position amounts with appropriate classifications.

Problem 18-3 (Time 50-60 minutes)

Purpose—to provide the student with an understanding of how to calculate and properly classify deferred taxes when there are four types of temporary differences. A single tax rate applies. The student is required to calculate and classify deferred taxes. Also, the student must use data given to solve for both taxable income and pre-tax accounting income. Reconciliations of reversing differences and the resulting deferred tax accounts must be prepared in order to provide proper comparative statement of financial position disclosures. Finally the reconciliation of the effective tax rate is required.

Problem 18-4 (Time 50-60 minutes)

Purpose—to provide the student with a situation where: (1) a temporary difference originates over a three-year period and begins to reverse in the fourth period, (2) a change in an enacted tax rate occurs first in a year prior to the year in which the amount of the cumulative temporary difference originates and then second in a year in which there is a change in the amount of cumulative temporary difference, (3) the amount of originating or reversing temporary difference must be calculated each year in order to determine the cumulative temporary difference at the end of each year, and (4) there is a permanent difference along with a temporary difference each year. Journal entries are required for the first year in one instance and then for each of four years, including the entry for the adjustment of deferred taxes due to the change in the enacted tax rate. The income statement disclosure is also required for one year.

TIME AND PURPOSE OF PROBLEMS (CONTINUED)

Problem 18-5 (Time 40-45 minutes)

Purpose—to provide the student with an understanding of how future temporary differences for existing depreciable assets are considered in determining the future years in which existing temporary differences result in taxable or deductible amounts. The student is given information about pre-tax accounting income, one temporary difference, and one permanent difference. The student must calculate all amounts related to income taxes for the current year and prepare the journal entry to record them. In order to determine the beginning balance in a deferred tax account, the student must calculate deferred taxes for the prior year's statement of financial position. An income statement and statement of financial position presentation is also required along with earnings per share disclosure.

Problem 18-6 (Time 50-60 minutes)

Purpose—to provide the student with the opportunity to reconcile timing differences reversing over a two-year period stemming from several sources, but using a consistent tax rate. Discontinued operations are also dealt with in this problem. The production of entries, income statement and statement of financial position amounts are also a requirement in this challenging problem.

Problem 18-7 (Time 40-45 minutes)

Purpose—to develop an understanding of the concept of future taxable amounts and future deductible amounts. Also, to develop an understanding of how reversing timing differences affect the calculation of deferred tax assets and liabilities when there are multiple tax rates enacted for the various periods affected by existing temporary differences. Different assumptions as to the likelihood of realization of deferred tax assets accrued from future deductible amounts are used and lead to a variety of entries and financial statement balances to be reported for two years.

Problem 18-8 (Time 50-60 minutes)

Purpose—to provide the student with the opportunity to deal with several reversing differences reversing over a two-year period with several tax rates involved. The activity of some statement of financial position accounts over the two year period provide the necessary detail to trace the reversing timing differences. Reporting of comparative balances on the statement of income and statement of financial position at the end each of the two years must also be provided. A good understanding of the accounting and tax treatment is required to handle this challenging problem.

TIME AND PURPOSE OF PROBLEMS (CONTINUED)

Problem 18-9 (Time 25-30 minutes)

Purpose—to provide the student with an understanding of how the calculation and classification of deferred taxes are affected by the individual future year(s) in which future taxable and deductible amounts are scheduled to occur because of existing temporary differences. Two situations are given and the student is required to calculate, record and classify the deferred taxes for each. A net deferred tax asset results in both cases.

Problem 18-10 (Time 40-50 minutes)

Purpose—to test a student's understanding of the relationships that exist in the subject area of accounting for income taxes. The student is required to calculate and classify deferred taxes for two successive years. The journal entry to record income taxes is also required for each year. A draft of the income tax expense section of the income statement is also required for each year. An interesting twist to this problem is that the student must calculate taxable income for two individual periods based on facts about the tax rate and amount of taxes paid for each period and then combine that information with data on temporary differences to calculate pre-tax accounting income.

Problem 18-11 (Time 50-60 minutes)

Purpose—to test a student's ability to calculate, record and classify deferred taxes for three reversing differences and three permanent differences and to draft the income statement and a statement of retained earnings for the year. This problem also requires the reconciliation of the effective tax rate.

Problem 18-12 (Time 35-40 minutes)

Purpose—to provide the student with a situation involving an actual net operating loss which can be partially offset by prior taxes paid using the carryback provision. Journal entries for the loss year and two subsequent years are required. The benefits of the loss carryforward are realized in the year following the loss year in one case and unexpected in another. Income statement presentations are required for the loss year where the benefits of the carryback and the carryforward are recognized and the year following the loss year where the benefits of the carryforward are realized and for the case where the loss carryforward is not expected.

TIME AND PURPOSE OF PROBLEMS (CONTINUED)

Problem 18-13 (Time 35-40 minutes)

Purpose—To challenge the student to deal with an error in a prior period in a company following ASPE and using the future/deferred income taxes method of accounting. The problem also includes reversing (CCA vs depreciation and allowance for doubtful accounts) and permanent differences (income tax penalties and interest, and golf club dues). The student must consider refiling the prior year tax return as a result of the error and complete the statement of retained earnings with the after tax impact of the error shown. The student must also prepare the journal entry for the error.

Problem 18-14 (Time 50-60 minutes)

Purpose—To introduce the student to accounting for commercial real estate leases and deal with the reversing differences (prepaid rent and rent payable) as well as permanent differences (golf club dues and interest expense incurred to earn income not subject to tax). The student must deal with 2 years of information, calculate income tax expense and payable for 2 years and journalize all tax entries for 2 years. Also required is tax section of income statement and comparative statements of financial position for 2 years. The question emphasizes the few differences between the deferred approach to income taxes under both ASPE and IFRS.

Problem 18-15 (Time 60-75 minutes)

Purpose—To provide the students with a challenging problem that requires them to think through a number of issues: loss carryback in a situation where the company's accounting income and taxable income has differences due to timing and permanent differences, a change in tax rate, and a loss carryforward that cannot be recognized in its entirety. Students are asked to prepare entries and the income tax rate reconciliation note.

SOLUTIONS TO PROBLEMS

PROBLEM 18-1

(a)

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate (see below)	Deferred Tax Asset (Liability)	(ASPE) Current or Long- Term
Property, plant, & equip.	\$900,000*	\$936,000**	(\$36,000)	30%	(\$10,800)	LT
Prepaid rent (2015 expense)	-0-	25,000	(25,000)	30%	(7,500)	C
Prepaid rent (2016 expense)	-0-	25,000	(25,000)	30%	(7,500)	LT
Warranty liability	-0-	(6,000)	6,000	30%	<u>1,800</u>	C
Deferred tax liability, December 31, 2014					(24,000)	
Deferred tax liability before adjustment					<u>(6,000)</u>	
Incr. in Deferred tax liability, and Deferred tax expense for 2014					<u><u>(\$18,000)</u></u>	

* $\$1,200,000 - \$100,000 - \$200,000 = \$900,000$

** $\$1,200,000 - (\$1,200,000 \times 20\% \times 50\%) - \$216,000 = \$864,000$

Taxable temporary difference, Dec. 31, 2013 X tax rate = Deferred tax liability, Dec. 31, 2013

$(\$1,100,000 - \$1,080,000) \times \text{tax rate} = \$6,000$

Tax rate = 30%

PROBLEM 18-1 (Continued)**(b)**

Accounting income		\$80,000
Permanent differences:		
50% of meals expense (\$16,000 X 50%)	\$8,000	
Golf club fees	<u>12,000</u>	<u>20,000</u>
		100,000
Reversing differences:		
Depreciation	200,000	
Capital cost allowance	<u>(216,000)</u>	(16,000)
Rent paid	(75,000)	
Rent expense	<u>25,000</u>	(50,000)
Warranty expense	12,000	
Warranty payments	<u>(6,000)</u>	<u>6,000</u>
Taxable income		<u>\$40,000</u>
Current income taxes – 30%		<u>\$12,000</u>

(c) Current Tax Expense	12,000	
Income Tax Payable		12,000
Deferred Tax Expense	18,000	
Deferred Tax Liability		18,000

(d)

Income before income tax		\$80,000
Income tax		
Current	\$12,000	
Deferred	<u>18,000</u>	<u>30,000</u>
Net income		<u>\$50,000</u>

PROBLEM 18-1 (Continued)**(e)****Statement of financial position, December 31, 2014****Current liabilities:**

Deferred tax liability: (\$7,500 – \$1,800)	\$5,700
---	---------

Non-current liabilities:

Deferred tax liability (\$7,500 + \$10,800)	18,300
---	--------

Under ASPE, deferred tax assets and deferred tax liabilities are segregated into current and non-current categories. The classification of an individual deferred tax liability or asset as current or non-current is determined by the classification of the asset or liability underlying the specific temporary difference.

(f)

If Anthony reported under IFRS, the only difference would be in how any deferred tax asset or liability would be reported on the statement of financial position.

Statement of financial position, December 31, 2014**Non-current liabilities:**

Deferred tax liability (\$18,300 + \$5,700)	\$24,000
---	----------

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

PROBLEM 18-2

(a)

For non-current deferred taxes:

	Deferred Tax Asset (Liability)			
<u>Future taxable amounts: LT</u>	2015	2016	2017	Total
CCA vs. depreciation	(\$90,000)	(\$50,000)	(\$40,000)	(\$180,000)
Tax rate enacted for the year	30%	28%	28%	
Deferred tax liability	(\$27,000)	(\$14,000)	(\$11,200)	(\$52,200)
<hr/>				
<u>Future taxable amounts: LT</u>	2015	2016	2017	Total
Instalment accounts receivable		(\$36,000)	(\$36,000)	(\$72,000)
Tax rate enacted for the year		28%	28%	
Deferred tax liability		(\$10,080)	(\$10,080)	(\$20,160)
<hr/>				
<u>Future deductible amounts: LT</u>	2015	2016	2017	Total
Pension liability	\$ 30,000	\$ 20,000	\$ 10,000	\$ 60,000
Tax rate enacted for the year	30%	28%	28%	
Deferred tax asset	\$ 9,000	\$ 5,600	\$ 2,800	\$ 17,400
Deferred tax liability – non-current	(\$18,000)	(\$18,480)	(\$18,480)	(\$54,960)

PROBLEM 18-2 (Continued)

(a) (continued)

<u>For 'current' deferred taxes:</u>	<u>Deferred tax asset (liability)</u>
<u>Future deductible amounts: C</u>	<u>2015</u>
Unearned royalties	\$ 76,000
Tax rate enacted for the year	<u>30%</u>
Deferred tax asset	<u>\$ 22,800</u>
<u>Future deductible amounts: C</u>	<u>2015</u>
Various accrued expenses	\$ 24,000
Tax rate enacted for the year	<u>30%</u>
Deferred tax asset	<u>\$ 7,200</u>
<u>Future taxable amounts: C</u>	<u>2015</u>
Instalment accounts receivable	\$ (36,000)
Tax rate enacted for the year	<u>30%</u>
Deferred tax liability	<u>\$ (10,800)</u>
Deferred tax asset – current	<u>\$ 19,200</u>

PROBLEM 18-2 (Continued)
(a) (continued)

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	(Taxable) Deductible Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	(ASPE) Current or Long-Term
PP&E (table above)	*	*	(\$180,000)	Mixed	(\$52,200)	LT
Instal. accounts receivable	-0-	\$72,000	(72,000)	Mixed	(20,160)	LT
Pension liability	-0-	(\$60,000)	60,000	Mixed	17,400	LT
Unearned royalties	-0-	(\$76,000)	76,000	30%	22,800	C
Accrued liabilities	-0-	(\$24,000)	24,000	30%	7,200	C
Instal. accounts receivable	-0-	\$36,000	(36,000)	30%	<u>(10,800)</u>	C
Deferred tax liability, December 31, 2014					(35,760)	
Deferred tax asset before adjustment					<u>30,000</u>	
Incr. in deferred tax liability, and deferred tax expense for 2014					<u>(\$65,760)</u>	

* Amounts not given in the problem

Deferred Tax Expense 65,760
 Deferred Tax Liability 65,760

Statement of financial position classification: Refer to last two columns in tables above and summaries.

2014

Current assets
 Deferred tax asset \$19,200
 Long-term liabilities
 Deferred tax liability \$54,960

PROBLEM 18-2 (Continued)**(d) (Continued)****Calculation of accounting income, 2014:**

Accounting income	\$ X
Reversing differences	<u>(228,000)</u>
Taxable income – see part (c)	<u>\$ 600,000</u>

Therefore, accounting income:
 $\$600,000 + \$228,000 =$ \$ 828,000

Income before income tax		\$828,000
Income tax expense		
Current	\$180,000	
Deferred	<u>65,760*</u>	<u>245,760</u>
Net income		<u>\$582,240</u>

- * This can be further divided into the deferred taxes caused by a change in the rate of tax, and those caused by changes in the temporary differences themselves:

Caused by change in rate of tax:

Deferred tax asset, January 1, 2014			
\$100,000 @ 30%			\$30,000
Deferred tax asset, January 1, 2014			
\$100,000 @ 30% for 2014, 2015, and			
28% for 2016, 2017:			
\$40,000 @ 30%	\$12,000		
\$30,000 @ 30%	9,000		
\$20,000 @ 28%	5,600		
\$10,000 @ 28%	<u>2,800</u>		<u>29,400</u>
			<u>\$ 600</u>

Caused by changes in temporary differences:

$\$65,760 - \$600 =$ \$65,160

PROBLEM 18-3

(a)

<u>Excess CCA over Deprec.</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>Total</u>
Future taxable amounts	\$ 37,500	\$ 37,500	\$ 37,500	\$ 37,500	\$ 150,000
Tax rate enacted for the year	<u>25%</u>	<u>25%</u>	<u>25%</u>	<u>25%</u>	
Deferred tax liability	<u><u>\$ 9,375</u></u>	<u><u>\$ 9,375</u></u>	<u><u>\$ 9,375</u></u>	<u><u>\$ 9,375</u></u>	<u><u>\$ 37,500</u></u>

<u>Unearned Rent</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>Total</u>
Future deductible amounts	\$20,000	\$20,000	\$20,000	\$60,000
Tax rate enacted for the year	<u>30%</u>	<u>25%</u>	<u>25%</u>	
Deferred tax asset	<u><u>\$6,000</u></u>	<u><u>\$ 5,000</u></u>	<u><u>\$5,000</u></u>	<u><u>\$16,000</u></u>

PROBLEM 18-3 (Continued)

Statement of Financial Position Account Dec. 31, 2013	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	For (g) (ASPE) Current or Long-Term
PP&E (table above)	*	*	(\$150,000)	25%	(\$37,500)	LT
Unearned Rent (table above)	-0-	(\$20,000)	20,000	30%	6,000	C
Unearned Rent (table above)	-0-	(\$40,000)	40,000	25%	<u>10,000</u>	LT
Deferred tax liability, December 31, 2013					<u>(\$21,500)</u>	

* Amounts not given in the problem

PROBLEM 18-3 (Continued)

(b)

Calculation of effect of disposal of equipment on temporary differences:

Original cost of disposed equipment	\$ 105,000	
Accumulated Depreciation of disposed equipment	(37,000)	
Reduction in carrying amount of equipment	68,000	
Reduction in CCA pool (UCC) for proceeds	90,000	
Reversing difference in 2014	22,000	\$22,000
CCA > depreciation, 2014		100,000
Excess of carrying amount over tax base, January 1, 2014		150,000
Excess of carrying amount over tax base, Dec.31, 2014		\$272,000

Carrying amount > tax base, equipment

	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>Total</u>
Future taxable amounts	\$ 68,000	\$ 68,000	\$ 68,000	\$ 68,000	\$ 272,000
Tax rate enacted for the year	25%	25%	25%	25%	
Deferred tax liability	\$ 17,000	\$ 17,000	\$ 17,000	\$ 17,000	\$ 68,000

Unearned Rent

	<u>2015</u>	<u>2016</u>	<u>Total</u>
Future deductible amounts	\$20,000	\$ 20,000	\$40,000
Tax rate enacted for the year	25%	25%	
Deferred tax asset	\$5,000	\$ 5,000	\$10,000

PROBLEM 18-3 (Continued)

(b) (Continued)

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	(Taxable) Deductible Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	For (g) (ASPE) Current or Long-Term
PP&E (table above)	*	*	(\$272,000)	25%	(\$68,000)	LT
Unearned Rent (table above)	-0-	(\$20,000)	20,000	25%	5,000	C
Unearned Rent (table above)	-0-	(\$20,000)	20,000	25%	5,000	LT
LT Investment	*	*	75,000	25%	<u>18,750</u>	LT
Deferred tax liability, December 31, 2014					(39,250)	
Deferred tax liability before adjustment					<u>(21,500)</u>	
Incr. in deferred tax liability, and deferred tax expense for 2014					<u>(\$17,750)</u>	

* Amounts not given in the problem

(c)

Deferred Tax Expense	17,750
Deferred Tax Asset	12,750*
(\$18,750 + \$5,000 + \$5,000 – op. bal. \$16,000)	
Deferred Tax Liability	30,500*
(\$68,000 – op. bal. \$37,500)	
* Alternately – net the two	
Deferred Tax Asset/Liability	17,750

PROBLEM 18-3 (Continued)

(c) (continued)

Accounting income		\$633,000
Permanent differences:		
Dividends received that are not taxable	(\$15,000)	
Late interest penalties on tax instalments	<u>2,880</u>	<u>(12,120)</u>
		620,880
Reversing differences:		
Gain on disposal of equipment		(22,000)
Impairment loss on investments		75,000
Excess of rent revenue over cash received (\$60,000 – \$40,000)		(20,000)
CCA > Depreciation		<u>(100,000)</u>
Taxable income		<u>\$553,880</u>
Current income taxes at 30% current rate		<u>\$166,164</u>
Current Tax Expense.....	166,164	
Income Tax Payable.....		166,164

PROBLEM 18-3 (Continued)

(d)

Statement of financial position classification:

	<u>2014</u>	<u>2013</u>
Long-term liabilities		
Deferred tax liability	39,250	21,500

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

(e)

Income statement presentation:

Income before income tax		\$633,000
Income tax		
Current tax	\$ 166,164	
Deferred tax	<u>17,750</u>	<u>183,914</u>
Net income		<u>\$449,086</u>

(f)

		<u>@ 30%</u>	<u>÷ Account- ing Income</u>
Accounting income	\$633,000	\$189,900	30.0%
Non-taxable dividends	(15,000)	(4,500)	(0.7)%
Non-deductible penalties	2,880	864	0.1%
		<u>\$186,264</u>	<u>29.4%</u>
Net taxable temporary differences taxed at lower 25% rate:			
(\$272,000 – \$150,000) X 5% =	(\$6,100)		
\$75,000 X 5% =	<u>3,750</u>	(2,350)	(0.4)%
		<u>\$183,914</u>	<u>29.0%</u>
Effective tax rate (\$183,914 / \$633,000)			29.0%

The effective tax rate differs from the statutory rate because there is no tax effect on the permanent differences, and because of the deferment of taxes to the future at a 25% rate rather than the current rate of 30%.

PROBLEM 18-3 (Continued)**(g)**

A company reporting under ASPE may use different terminology, but none of the calculations would differ except for the classification of the deferred tax assets and liabilities in the statement of financial position, as explained below.

Statement of financial position classification: (see tables in (a) and (b))

	<u>2014</u>	<u>2013</u>
Current assets		
Deferred tax asset	\$5,000	\$6,000
Long-term liabilities		
Deferred tax liability	44,250	27,500

Under ASPE, deferred tax assets and deferred tax liabilities are segregated into current and non-current categories. The classification of an individual deferred tax liability or asset as current or non-current is determined by the classification of the asset or liability underlying the specific temporary difference.

PROBLEM 18-4

(a) Before deferred taxes can be calculated, the amount of the reversing differences originating (reversing) each period and the resulting temporary difference at each year-end must be calculated:

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
Accounting income	\$ 460,000	\$ 420,000	\$ 390,000	\$ 460,000
Permanent difference	40,000	40,000	40,000	40,000
	500,000	460,000	430,000	500,000
Taxable income (given)	299,000	294,000	304,200	644,000
Reversing difference for the year	(\$201,000)	(\$166,000)	(\$125,800)	\$144,000
Tax rate enacted for the year	25%	30%	30%	30%
Current income tax (% X taxable income)	\$74,750	\$88,200	\$91,260	\$193,200
(Taxable) temporary				
Difference – beginning of year	(\$ 0)	(\$201,000)	(\$367,000)	(\$492,800)
(Excess) CCA in year	(201,000)	(166,000)	(125,800)	144,000
(Taxable) temporary				
Difference – end of year	(\$201,000)	(\$367,000)	(\$492,800)	(\$348,800)

PROBLEM 18-4 (Continued)

(a) and (b)
2014

Statement of Financial Position Account Dec. 31, 2014	Tax Base*	Carrying Amount*	(Taxable) Temporary Differences	Tax Rate	Deferred Tax (Liability)	(ASPE) Current or Long-Term
Property, plant, & equip.			(\$201,000)	25%	<u>(\$50,250)</u>	LT
Deferred tax liability, December 31, 2014					(50,250)	
Deferred tax liability before adjustment					<u>0</u>	
Incr. in deferred tax liability, and deferred tax expense for 2014					<u>(\$50,250)</u>	

* Amounts not given in the problem

2014

Current Tax Expense.....	74,750	
Income Tax Payable.....		74,750
[(refer to table in part (a))		
Deferred Tax Expense	50,250	
Deferred Tax Liability.....		50,250

PROBLEM 18-4 (Continued)

(a) and (b) (continued)
2015

Statement of Financial Position Account Dec. 31, 2015	Tax Base*	Carrying Amount*	(Taxable) Temporary Differences	Tax Rate	Deferred Tax (Liability)	(ASPE) Current or Long-Term
Property, plant, & equip.			(\$367,000)	30%	<u>(\$110,100)</u>	LT
Deferred tax liability, December 31, 2015					(110,100)	
Deferred tax liability before adjustment (\$50,250 + \$10,050^a)					<u>(60,300)</u>	
Incr. in deferred tax liability, and deferred tax expense for 2015					<u>(\$49,800)</u>	

* Amounts not given in the problem

2015

^a Deferred Tax Expense 10,050

Deferred Tax Liability..... 10,050

[To record the adjustment for the increase in the enacted tax rate recorded when known:
 \$201,000 × (30% – 25%)]

Current Tax Expense..... 88,200

Income Tax Payable..... 88,200

[(refer to table in part (a))]

Deferred Tax Expense 49,800

Deferred Tax Liability..... 49,800

PROBLEM 18-4 (Continued)

(a) and (b) (continued)
2016

Statement of Financial Position Account Dec. 31, 2016	Tax Base*	Carrying Amount*	(Taxable) Temporary Differences	Tax Rate	Deferred Tax (Liability)	(ASPE) Current or Long- Term
Property, plant, & equip.			(\$492,800)	30%	<u>(\$147,840)</u>	LT
Deferred tax liability, December 31, 2016					(147,840)	
Deferred tax liability before adjustment					<u>(110,100)</u>	
Incr. in deferred tax liability, and deferred tax expense for 2016					<u>(\$37,740)</u>	

* Amounts not given in the problem

2016

Current Tax Expense.....	91,260	
Income Tax Payable.....		91,260
[(refer to table in part (a))		
Deferred Tax Expense.....	37,740	
Deferred Tax Liability.....		37,740

PROBLEM 18-4 (Continued)

(a) and (b) (continued)
2017

Statement of Financial Position Account Dec. 31, 2017	Tax Base*	Carrying Amount*	(Taxable) Temporary Differences	Tax Rate	Deferred Tax (Liability)	(ASPE) Current or Long-Term
Property, plant, & equip.			(\$348,800)	30%	(\$104,640)	LT
Deferred tax liability, December 31, 2017					(104,640)	
Deferred tax liability before adjustment					(147,840)	
Decr. in deferred tax liability, and deferred tax benefit for 2017					<u>\$43,200</u>	

* Amounts not given in the problem

2017

Current Tax Expense.....	193,200	
Income Tax Payable.....		193,200
[(refer to table in part (a))]		
Deferred Tax Liability	43,200	
Deferred Tax Benefit		43,200

PROBLEM 18-4 (Continued)

(c)	<u>2015</u>		
Income before income tax			\$420,000
Income tax expense			
Current		\$88,200	
Deferred		<u>59,850*</u>	<u>148,050</u>
Net income			<u>\$271,950</u>
*(\$49,800 + \$10,050)			

PROBLEM 18-5

(a)
Basic Calculations of Capital Cost Allowance, Depreciation and Balances:

<u>Year</u>	<u>(A)</u> <u>Base</u>		<u>(B)</u> <u>CCA</u>	<u>(A – B)</u> <u>UCC</u>	<u>(C)</u> <u>Deprec.</u>	<u>(A – C)</u> <u>Carrying</u> <u>Amount</u>	<u>C-B</u> <u>Reversing</u> <u>Difference</u>
2013	\$1,000,000	X 20 % X .5	\$100,000	\$ 900,000	\$125,000	\$875,000	\$25,000
2014	900,000	X 20 %	180,000	720,000	125,000	750,000	(55,000)

(b)
2014

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	(Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	For (f) (ASPE) Current or Long- Term
Property, plant, & equip.	\$720,000	\$750,000	(\$30,000)	35%	<u>(\$10,500)</u>	LT
Deferred tax liability, December 31, 2014					(10,500)	
Deferred tax asset before adjustment (\$25,000 X 35%)					<u>8,750</u>	
Incr. in deferred tax liability, and deferred tax expense for 2014					<u>(\$19,250)</u>	

PROBLEM 18-5 (Continued)

(b) (continued)

<u>Calculation of current income tax expense:</u>	
Accounting income	\$ 1,400,000
Permanent difference – tax exempt interest	<u>(60,000)</u>
	1,340,000
Reversing difference - [part (a)]	<u>55,000</u>
Taxable income on regular operations	<u>1,285,000</u>
Income tax expense and payable @ 35 %	<u><u>\$ 449,750</u></u>

(c)

Current Tax Expense	449,750	
Income Tax Payable		449,750
Deferred Tax Expense	19,250	
Deferred Tax Liability.....		10,500*
Deferred Tax Asset.....		8,750*
* Alternately		
Deferred Tax Asset/Liability		19,250

PROBLEM 18-5 (Continued)

(d) Income before income tax		\$1,400,000
Income tax expense		
Current	\$449,750	
Deferred	<u>19,250</u>	<u>469,000</u>
Net income		<u>\$ 931,000</u>
Earnings per share:		
Net Income		<u>\$9.31</u>

- (e) Net deferred tax liability at December 31, 2014.
(See part (b))**

<u>Long-term liabilities</u>	
Deferred tax liability	\$10,500

- (f) The only difference, aside from different terminology that might be used (future taxes instead of deferred taxes) would be in the classification of the deferred tax account(s) on the statement of financial position. In this case, the statement of financial position disclosure would be the same under ASPE's future/deferred income tax method as under IFRS since all temporary differences relate to differences between the tax base and carrying amount of property, plant and equipment which are classified as non-current. Therefore, the deferred tax liability would be included with non-current liabilities.**

PROBLEM 18-6

(a)

PP&E	UCC	Carrying Amount	Difference	Tax 30%	Deferred Tax
Bal. Dec. 31, 2013	\$ 998,000	\$ 1,256,000	\$ (258,000)	\$ (77,400)	Liability
For 2014	(192,000)	(175,000)	(17,000)	(5,100)	
Bal. Dec. 31, 2014	806,000	1,081,000	(275,000)	(82,500)	Liability
For 2015	(163,500)	(180,000)	16,500	4,950	
Bal. Dec. 31, 2015	\$ 642,500	\$ 901,000	\$ (258,500)	\$ (77,550)	Liability
Restructuring Charges	Tax Base	Accrued Liability	Difference	Tax 30%	Deferred Tax
Bal. Dec. 31, 2013	\$ 0	\$ (199,500)	\$199,500	\$59,850	Asset
For 2014	0	131,500	(131,500)	(39,450)	
Bal. Dec. 31, 2014	0	(68,000)	68,000	20,400	Asset
For 2015	0	68,000	(68,000)	(20,400)	
Bal. Dec. 31, 2015	\$-0-	\$ -0-	\$ -0-	\$ -0-	

PROBLEM 18-6 (Continued)

(a) (continued)

Profit on Property Sale	Deferred Profit for Tax	Deferred G/P deducted from A/R	Difference	Tax 30%	Deferred Tax
Bal. Dec. 31, 2013	\$ -0-	-0-	-0-	-0-	
For 2014	(46,800)	\$ -0-	\$ (46,800)	\$ (14,040)	
Bal. Dec. 31, 2014	(46,800)	-0-	(46,800)	(14,040)	Liability
For 2015	15,600	-0-	15,600	4,680	
Bal. Dec. 31, 2015	(31,200)	\$ -0-	\$ (31,200)	\$ (9,360)	Liability

PROBLEM 18-6 (Continued)

(b)

Continuing operations:	<u>2014</u>	<u>2015</u>
Accounting income	\$850,000	\$525,000
Permanent differences:		
Non-deductible life insurance	11,000	11,000
Non-taxable dividends	<u>(3,250)</u>	<u>(3,500)</u>
	857,750	532,500
Reversing differences:		
CCA & depreciation	(17,000)	16,500
Restructuring charges	(131,500)	(68,000)
Profit on property sale	<u>(46,800)</u>	<u>15,600</u>
Taxable income	<u>662,450</u>	<u>496,600</u>
Current income taxes – 30%	<u><u>\$198,735</u></u>	<u><u>\$148,980</u></u>
 Discontinued operations:		
Accounting income	\$ 18,800	\$0
Permanent differences	0	0
Reversing differences	<u>0</u>	<u>0</u>
Taxable income	<u>18,800</u>	<u>0</u>
Current income taxes – 30%	<u><u>\$ 5,640</u></u>	<u><u>\$0</u></u>

PROBLEM 18-6 (Continued)
(a) and (c)

Statement of Financial Position Account Dec. 31, 2013	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	(ASPE) Current or Long-Term
PP&E	\$998,000	\$1,256,000	(\$258,000)	30%	(\$77,400)	LT
Restructuring Liability	-0-	(199,500)	199,500	30%	<u>59,850</u>	C*
Deferred tax liability, December 31, 2013					<u>(\$17,550)</u>	

*At Dec. 31/13, the total liability was expected to be current.

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	(ASPE) Current or Long-Term
PP&E	\$806,000	\$1,081,000	(\$275,000)	30%	(\$82,500)	LT
Restructuring Liability	-0-	(68,000)	68,000	30%	20,400	C
Deferred G/P on Sale (A/R)	-0-	46,800-	(46,800)	30%	<u>(14,040)</u>	mixed**
Deferred tax liability, December 31, 2014					(76,140)	
Deferred tax liability before adjustment					<u>(17,550)</u>	
Incr. in deferred tax liability, and deferred tax expense for 2014					<u>\$58,590</u>	

** 1/3 of the remaining G/P of \$46,800 is expected to be realized in each of 2015, 2016, and 2017, making 30% of (1/3 X \$46,800) = \$4,680 a current amount, and 30% of (2/3 X \$46,800) = \$9,360 a long-term amount at Dec. 31/14.

PROBLEM 18-6 (Continued)

(a) and (c) (Continued)

Statement of Financial Position Account Dec. 31, 2015	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	(ASPE) Current Long-Term
PP&E	\$642,500	\$901,000	(\$258,500)	30%	(\$77,550)	LT
Restructuring Liability	-0-	-0-	-0-	30%	-0-	C
Deferred G/P on Sale (A/R)	-0-	31,200	(31,200)	30%	(9,360)	mixed*
Deferred tax liability, December 31, 2015					(86,910)	
Deferred tax liability before adjustment					(76,140)	
Incr. in deferred tax liability, and deferred tax expense for 2015					(\$10,770)	

* 1/2 of the remaining G/P of \$31,200 is expected to be realized in each of 2016 and 2017, making 30% of (1/2 X \$31,200) = \$4,680 a current amount, and 30% of (1/2 X \$31,200) = \$4,680 a long-term amount at Dec. 31/15.

PROBLEM 18-6 (Continued)**(c) December 31, 2014**

Current Tax Expense	198,735	
Current Tax Expense – Discontinued Operations	5,640	
Income Tax Payable		204,375
Deferred Tax Expense.....	58,590	
Deferred Tax Liability.....		58,590

December 31, 2015

Current Tax Expense	148,980	
Income Tax Payable (\$495,350 X .30)		148,980
Deferred Tax Expense.....	10,770	
Deferred Tax Liability		10,770

PROBLEM 18-6 (Continued)**(d)****Balance sheet 2014****Current assets:**

Deferred tax asset (\$20,400 – \$4,680)	\$15,720
---	----------

Non-current liabilities:

Deferred tax liability (\$9,360 + \$82,500)	91,860
---	--------

Balance sheet 2015**Current liability:**

Deferred tax liability	\$4,680
------------------------	---------

Non-current liabilities:

Deferred tax liability (\$4,680 + \$77,550)	82,230
---	--------

Under ASPE, deferred tax assets and deferred tax liabilities are segregated into current and non-current categories. The classification of an individual deferred tax liability or asset as current or non-current is determined by the classification of the asset or liability underlying the specific temporary difference.

PROBLEM 18-6 (Continued)**(e)****Income Statement – 2014**

Income from continuing operations before income tax		\$850,000
Income tax		
Current tax	\$198,735	
Deferred tax	58,590	257,325
		<hr/>
Income from continuing operations		592,675
Discontinued operations		
Gain on disposal of operations	18,800	
Less applicable income tax	5,640	13,160
		<hr/>
Net income		<u><u>\$605,835</u></u>

Income Statement – 2015

Income before income tax		\$525,000
Income tax		
Current tax	\$ 148,980	
Deferred tax	10,770	159,750
		<hr/>
Net income		<u><u>\$365,250</u></u>

PROBLEM 18-6 (Continued)**(f)**

None of the calculations would change, although different terminology might be used (future taxes instead of deferred taxes). The only difference would be the classification of the deferred accounts on the statement of financial position.

Balance sheet 2014**Non-current liabilities:**

Deferred tax liability ($\$82,500 + \$14,040 - \$20,400$) **\$76,140**

Balance sheet 2015**Non-current liabilities:**

Deferred tax liability ($\$77,550 + \$9,360$) **\$86,910**

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

PROBLEM 18-7

- (a) Future taxable amounts increase future taxable income relative to pre-tax accounting income due to existing taxable temporary differences. Future deductible amounts decrease future taxable income relative to pre-tax accounting income due to existing deductible temporary differences.

A deferred tax liability should be recorded for the future income tax consequences attributable to the future taxable amounts scheduled and a deferred tax asset should be recorded for the future tax consequences attributable to the future deductible amounts scheduled.

- (b) See next two pages for deferred taxes.

Current Tax Expense	15,000	
Income Tax Payable		15,000
(\$50,000 taxable income X 30%)		

- (c) I might be concerned that the company will not generate enough taxable income in the future from which to deduct the future deductible amounts. If this were the case, their future deductibility would not qualify as having asset value.

To the extent that the deferred tax asset will not be realized, an allowance to reduce the deferred tax asset account to the expected realizable value should be created. It becomes a valuation account, which will then ensure that the asset is reduced to the realizable value for financial statement reporting purposes. The use of the allowance account is optional. An alternative approach would be to establish a deferred tax asset only for the portion of the future taxes estimated more likely than not to be realized.

PROBLEM 18-7 (Continued)

(b)

Mixed rates

	Deferred Taxes				Total
	2015	2016	2017	2018	
Future taxable amounts	(\$75,000)	(\$75,000)	(\$75,000)	(\$75,000)	(\$300,000)
Tax rate enacted for the year	28%	26%	24%	24%	
Deferred tax (liability)	(\$21,000)	(\$19,500)	(\$18,000)	(\$18,000)	(\$76,500)
	2015	2016	2017	2018	Total
Future deductible amounts			\$2,400,000		\$2,400,000
Tax rate enacted for the year	28%	26%	24%	24%	
Deferred tax asset	–	–	\$576,000	–	\$576,000

PROBLEM 18-7 (Continued)

(b) (continued)

Balance Sheet Account Dec. 31, 2014	Tax Base*	Carrying Amount*	(Taxable) Deductible Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	(ASPE) Current or Long-Term
Unknown* see table in (b)	0	0	(\$75,000)	28%	(\$21,000)	C ⁽¹⁾
Unknown* see table in (b)	0	0	(225,000)	Mixed	(55,500)	LT
Unknown* see table in (b)	0	0	2,400,000	24%	<u>576,000</u>	LT
Deferred tax asset, December 31, 2014					499,500	
Deferred tax asset/liability before adjustment					<u>0</u>	
Incr. in deferred tax asset, and deferred tax benefit for 2014					<u>\$499,500</u>	

* Not given in the problem

⁽¹⁾ This assumes that either 1/4 of the related balance sheet account is reported in a current classification on the balance sheet, or there is no related balance sheet account reported.

Deferred Tax Asset	576,000*	
Deferred Tax Benefit		499,500
Deferred Tax Liability		76,500*

* Alternately

Deferred Tax Asset/Liability	499,500
------------------------------------	---------

PROBLEM 18-7 (Continued)

(d)

Deferred Tax Expense.....	480,000	
Allowance to Reduce Deferred Tax		
Asset to Expected Realizable Value		480,000
(\$2,000,000 X 24% = \$480,000)		

(e)

	Future Taxes		
	<u>2017</u>	<u>2018</u>	<u>Total</u>
Future deductible amounts	\$600,000	\$1,500,000	\$2,100,000
Tax rate enacted for the year	<u>24%</u>	<u>24%</u>	
Future tax asset (net)	<u>\$144,000</u>	<u>\$360,000</u>	<u>\$504,000</u>

Temporary difference – future deductible amount:

Required balance (net above)	\$504,000
Opening balance recorded in 2014	<u>576,000</u>
Required balance in allowance	<u><u>\$ 72,000</u></u>

Allowance to Reduce Deferred Tax		
Asset to Expected Realizable Value	408,000	
Deferred Tax Benefit.....		408,000
(\$480,000 – \$72,000 = \$408,000)		

PROBLEM 18-7 (Continued)

(f) 2015 mixed rates	Future Taxes			
	2016	2017	2018	Total
Future taxable amounts	(\$75,000)	(\$75,000)	(\$75,000)	(\$225,000)
Tax rate enacted for the year	26%	24%	24%	
Deferred tax (liability)	<u>(\$19,500)</u>	<u>(\$18,000)</u>	<u>(\$18,000)</u>	<u>(\$55,500)</u>
	2016	2017	2018	Total
Future deductible amounts		\$600,000	\$1,500,000	\$2,100,000
Tax rate enacted for the year	26%	24%	24%	
Deferred tax asset		<u>\$144,000</u>	<u>\$360,000</u>	<u>\$504,000</u>

Balance Sheet Account Dec. 31, 2015	Tax Base*	Carrying Amount*	(Taxable) Deductible Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	(ASPE) Current or Long-Term
Unknown* see table above	0	0	(\$75,000)	26%	(\$19,500)	C
Unknown* see table above	0	0	(150,000)	24%	(36,000)	LT
Unknown* see table above	0	0	2,100,000	24%	<u>504,000</u>	LT
Deferred tax asset, December 31, 2015					448,500	
Deferred tax asset (net) before adjustment (\$499,500 – \$480,000)					<u>19,500</u>	
Incr. in deferred tax asset, and future tax benefit (net) for 2015					<u>\$429,000</u>	

* Not given in the problem

PROBLEM 18-7 (Continued)**(f) (continued)****Balance sheet classification****Refer to last two columns in tables in part (b) and (f) above.**

	<u>2015</u>	<u>2014</u>
Non-current assets		
Deferred tax asset (net of allowance)	\$468,000 ²	\$40,500 ¹
Current liabilities		
Deferred tax liability	19,500	21,000

¹Balance of Deferred Tax accounts December 31, 2014:

Deferred tax asset – LT	\$ 576,000
Less: Allowance to reduce deferred tax asset to expected realizable value-part (d)	<u>(480,000)</u>
	96,000
Less: Deferred tax liability – LT	<u>(55,500)</u>
Net deferred tax asset – non-current	<u>\$40,500</u>

²Balance of Deferred Tax accounts December 31, 2015:

Deferred tax asset – LT	\$576,000
Less: Allowance to reduce deferred tax asset to expected realizable value-part (e)	<u>(72,000)</u>
	504,000
Less: Deferred tax liability – LT	<u>(36,000)</u>
Net deferred tax asset – non-current	<u>\$468,000</u>

If the company did not use the allowance method, the amounts reported for the deferred tax asset account would have been reported on the balance sheet as the same net amount as indicated above. If no allowance is used, only the realizable amount is recognized initially.

PROBLEM 18-7 (Continued)**(g)**

	<u>2015</u>	<u>2014</u>
Non-current assets		
Deferred tax asset	\$448,500 ²	\$19,500 ¹

¹ See calculations in (f) above: \$40,500 – \$21,000

² See calculations in (f) above: \$468,000 – \$19,500

Note that strict application of IFRS would require that no allowance account be used. Instead, a deferred tax asset would be recognized only to the extent that it is probable that taxable income will be available against which the deductible temporary difference can be used.

Also, IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

PROBLEM 18-8

(a) 2013 balances with mixed tax rates:

	Deferred Taxes			
	2014	2015	2016	Total
<u>Future taxable amounts:</u>				
CCA vs. depreciation	(\$17,500)	(\$12,500)	(\$2,000)	(\$32,000)
Tax rate enacted for the year	30%	29%	28%	
Deferred tax liability	(\$5,250)	(\$3,625)	(\$560)	(\$9,435)
<u>Future deductible amounts</u>	2014	2015	2016	Total
Pension liability	11,000	11,000	12,600	34,600
Tax rate enacted for the year	30%	29%	28%	
Deferred tax asset	\$ 3,300	\$ 3,190	\$ 3,528	\$ 10,018

PROBLEM 18-8 (Continued)

(a) (continued)

Statement of Financial Position Account Dec. 31, 2013	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)		For (e) Current or Long-Term
Property, plant, & equipment	\$93,000	\$125,000	(\$32,000)	Mixed	(\$9,435)	(1)	LT
Warranty Liability	-0-	(18,500)	18,500	30%	5,550		C
Pension Liability	-0-	(34,600)	34,600	Mixed	<u>10,018</u>	(1)	LT
Deferred tax asset, December 31, 2013					\$6,133		

(1) from table above

Statement of financial position classification:

Non-current assets:

Deferred tax asset \$6,133
 (\$5,550 + \$10,018 – \$9,435)

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

PROBLEM 18-8 (Continued)

(b) 2014 future taxes – mixed tax rates

	Deferred Taxes		
	2015	2016	Total
Future taxable amounts:			
CCA vs. Depreciation	(\$12,500)	(\$2,000)	(\$14,500)
Tax rate enacted for the year	29%	28%	
Deferred tax liability	(\$3,625)	(\$560)	(\$4,185)
Future deductible amounts			
Pension liability	11,000	12,600	23,600
Tax rate enacted for the year	29%	28%	
Deferred tax asset	\$ 3,190	\$ 3,528	\$ 6,718

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)		For (e) Current or Long- Term
Property, plant, & equipment	*	*	(\$14,500)	Mixed	(\$4,185)	(1)	LT
Warranty Liability	-0-	(22,300)	22,300	29%	6,467		C
Pension Liability	-0-	(23,600)	23,600	Mixed	<u>6,718</u>	(1)	LT
Deferred tax asset, December 31, 2014					9,000		
Deferred tax asset before adjustment					6,133		
Incr. in deferred tax asset, and deferred tax benefit for 2014					<u>\$2,867</u>		

* not given in the problem (1) from table above

PROBLEM 18-8 (Continued)**(c)****Calculation of current tax expense 2014:**

Accounting income		\$ 109,400
Permanent difference – dividends		(4,300)
Permanent difference – golf dues		<u>20,000</u>
		125,100
Reversing differences		
Warranty Expense	\$28,300	
Warranty Payments	<u>(24,500)</u>	3,800
Pension Expense Recognized	59,000	
Tax Deductible Pension Payments	<u>(70,000)</u>	(11,000)
Depreciation > CCA		<u>17,500</u>
Taxable income		<u>\$135,400</u>
Current income taxes – 30%		<u>\$40,620</u>
Current Tax Expense	40,620	
Income Tax Payable		40,620
Deferred Tax Asset.....	2,867	
Deferred Tax Benefit.....		2,867

(d)**Income statement presentation 2014:**

Income before income tax		\$109,400
Income tax		
Current tax	\$ 40,620	
Deferred tax (benefit)	<u>(2,867)</u>	<u>37,753</u>
Net income		<u>\$ 71,647</u>

PROBLEM 18-8 (Continued)

(d) (continued)

Statement of financial position classification:

Non-current assets:	<u>2014</u>	<u>2013</u>
Deferred tax asset	\$9,000¹	\$6,133²
Current liabilities:		
Income tax payable	\$8,620	not given
[\$40,620 – (4 X \$8,000)]		

¹ \$6,467 + \$2,533

² \$5,550 + \$583

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

(e)

From part (a)

Statement of financial position classification:

Current assets:	
Deferred tax asset	\$5,550
Non-current assets	
Deferred tax asset	\$583
(\$10,018 – \$9,435)	

PROBLEM 18-8 (Continued)

(e) (continued)

From part (d)

Statement of financial position classification:

Current assets:	<u>2014</u>	<u>2013</u>
Deferred tax asset	\$6,467	\$5,550
 Non-current assets:		
Deferred tax asset	\$2,533	\$583
(\$6,718 – \$4,185)		
 Current liabilities:		
Income tax payable	\$8,620	not given
[\$40,620 – (4 X \$8,000)]		

Under ASPE, deferred tax assets and deferred tax liabilities are segregated into current and non-current categories. The classification of an individual deferred tax liability or asset as current or non-current is determined by the classification of the asset or liability underlying the specific temporary difference.

In addition, although none of the calculations would change (except for the classification described above), companies applying ASPE may use different terminology—that is, future income tax accounts instead of deferred tax accounts.

PROBLEM 18-9

Part 1. (a) Mixed tax rates

	Future years					
	2015	2016	2017	2018	2019	Total
Future taxable amounts	(\$300)	(\$300)	(\$300)	(\$200)	(\$100)	(\$1,200)
Tax rate enacted for the year	30%	30%	30%	35%	35%	
Deferred tax (liability)	(\$90)	(\$90)	(\$90)	(\$70)	(\$35)	(\$375)

	Future years					
	2015	2016	2017	2018	2019	Total
Future deductible amounts				\$1,800		\$1,800
Tax rate enacted for the year	30%	30%	30%	35%	35%	
Deferred tax asset	-	-	-	\$ 630	-	\$ 630

PROBLEM 18-9 (Continued)

Part 1. (a)

Statement of Financial Position Account Dec. 31, 2014	Tax Base*	Carrying Amount*	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Property, plant, & equipment			(\$1,200)	Mixed	(\$375)
Litigation liability			1,800	35%	<u>630</u>
Deferred tax asset (net), December 31, 2014					255
Deferred tax liability before adjustment					<u>(500)</u>
Increase in deferred tax asset, and deferred tax benefit for 2014					<u><u>\$755</u></u>

* not given in the problem

Alia will report a Deferred Tax Asset of \$255 in non-current assets on the statement of financial position.

Part 1. (b)

Current Tax Expense	1,200	
Income Tax Payable		1,200
(\$4,000 X 30%)		
Deferred Tax Liability	500*	
Deferred Tax Asset	255*	
Deferred Tax Benefit.....		755

***Alternately: one debit to Deferred Tax Asset/Liability for \$755**

PROBLEM 18-9 (Continued)

Part 2. (a) Mixed tax rates

	Future years				
	2015	2016	2017	2018	Total
Future taxable amounts	(\$400)	(\$400)	(\$400)	(\$400)	(\$1,600)
Tax rate enacted for the year	30%	30%	30%	35%	
Deferred tax (liability)	(\$120)	(\$120)	(\$120)	(\$140)	(\$500)

	Future years				
	2015	2016	2017	2018	Total
Future deductible amounts			\$3,000		\$3,000
Tax rate enacted for the year	30%	30%	30%	35%	
Deferred tax asset	—	—	\$900	—	\$900

PROBLEM 18-9 (Continued)

Part 2. (a)

Statement of Financial Position Account Dec. 31, 2014	Tax Base*	Carrying Amount*	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)
Property, plant, & equipment			(\$1,600)	Mixed	(\$500)
Litigation liability			3,000	30%	<u>900</u>
Deferred tax asset, December 31, 2014					400
Deferred tax asset before adjustment					<u>600</u>
Decrease in deferred tax asset, and deferred tax expense for 2014					<u><u>\$200</u></u>

* not given in the problem

Part 2. (b)

Current Tax Expense	1,200	
Income Tax Payable		1,200
(\$4,000 X 30%)		
Deferred Tax Expense.....	200	
Deferred Tax Asset		200

PROBLEM 18-9 (Continued)**(c)**

Part 1 – All statement of financial position deferred tax accounts are presented as non-current, regardless of origin.

**Alia Corp.
Statement of Financial Position (partial)
December 31, 2014**

Non-current assets	
Deferred tax asset	\$255

Part 2 – All statement of financial position deferred tax accounts are presented as non-current, regardless of origin.

**Khoi Corp.
Statement of Financial Position (partial)
December 31, 2014**

Non-current assets	
Deferred tax asset	\$400

(d)

Under ASPE, the classification is contingent on the balance sheet classification of the temporary difference underlying the deferred tax amount. In both cases, the property, plant and equipment and the litigation liability are non-current items, so all the deferred tax accounts would also be presented as non-current. Therefore, there would be no difference, except for a possible use of different terminology (future taxes instead of deferred taxes).

PROBLEM 18-10

(a)
Basic Calculations of Capital Cost Allowance, Depreciation and Balances:

<u>Year</u>	<u>(A)</u> <u>Base</u>		<u>(B)</u> <u>CCA</u>	<u>A – B</u> <u>UCC</u>	<u>(C)</u> <u>Deprec.</u>	<u>Carrying</u> <u>Amount</u>	<u>C – B</u> <u>Reversing</u> <u>Difference</u>
2014	\$400,000	X 25 % X .5	\$ 50,000	\$ 350,000	\$80,000	\$320,000	\$30,000
2015	350,000	X 25 %	87,500	262,500	80,000	240,000	(7,500)

(b)
 2014

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	Deductible Temporary Differences	Tax Rate	Deferred Tax Asset	(j) (ASPE) Current or Long- Term
Property, plant, & equip.	\$350,000	\$320,000	\$30,000	30%	<u>\$9,000</u>	LT
Deferred tax asset, December 31, 2014					9,000	
Deferred tax account before adjustment					<u>0</u>	
Incr. in deferred tax asset, and deferred tax benefit for 2014					<u>\$9,000</u>	

(c)

Deferred Tax Asset.....	9,000	
Deferred Tax Benefit.....		9,000

PROBLEM 18-10 (Continued)**(c) (continued)**

Current Tax Expense.....	105,000	
Income Tax Payable.....		105,000
(amount given in the problem)		

\$105,000 tax due for 2014 ÷ 30% (2014 tax rate) = \$350,000 taxable income for 2014.

(d) Income before income tax			\$320,000^a
Income tax expense			
Current	\$105,000		
Deferred (benefit)	<u>(9,000)</u>		<u>96,000</u>
Net income			<u><u>\$224,000</u></u>

^a Pre-tax accounting income		\$	X
Excess depreciation per books [from (a) above]			<u>30,000</u>
Taxable income [from (c) above]			<u><u>\$350,000</u></u>

Solving for X; X + \$30,000 = \$350,000; X = \$320,000 pre-tax accounting income.

PROBLEM 18-10 (Continued)

(e)
2015

Statement of Financial Position Account Dec. 31, 2015	Tax Base	Carrying Amount	Deductible Temporary Differences	Tax Rate	Deferred Tax Asset	(j) (ASPE) Current or Long-Term
Property, plant & equip.	\$262,500	\$240,000	\$22,500	30%	\$6,750	LT
Unearned Rev. – current	-0-*	(75,000)	75,000	30%	22,500	C
Unearned Rev. – non-curr.	-0-*	(75,000)	75,000	30%	<u>22,500</u>	LT
Deferred tax asset, December 31, 2015					51,750	
Deferred tax asset before adjustment					<u>9,000</u>	
Incr. in deferred tax asset, and deferred tax benefit for 2015					<u>\$42,750</u>	

* \$150,000 unearned at end of 2015 divided by 2 years (2016 and 2017)

(f)

Deferred Tax Asset.....	42,750	
Deferred Tax Benefit.....		42,750

PROBLEM 18-10 (Continued)

(f) continued

Current Tax Expense.....	84,000	
Income Tax Payable.....		84,000
(amount given in the problem)		

\$84,000 tax due for 2015 ÷ 30% (2014 tax rate) = \$280,000 taxable income for 2015

(g) Income before income tax		\$137,500^d
Income tax expense		
Current	\$84,000	
Deferred (benefit)	<u>(42,750)</u>	<u>41,250</u>
Net income		<u><u>\$ 96,250</u></u>

^d Pre-tax accounting income		\$ X
CCA in excess of depreciation [from (a) above]		(7,500)
Excess rent collected over rent earned		<u>150,000</u>
Taxable income [from (f) above]		<u><u>\$280,000</u></u>

Solving for X:

$$X + \$150,000 - \$7,500 = \$280,000$$

$$X = \$137,500 \text{ pre-tax accounting income.}$$

(h) Refer to last column in tables of part (a) and (e) above.

	<u>2015</u>	<u>2014</u>
Non-current assets		
Deferred tax asset	\$51,750	\$9,000
(\$22,500 + \$22,500 + \$6,750)		

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

PROBLEM 18-10 (Continued)

- (i) When financial statements of several legal entities are consolidated into one for financial reporting purposes, the possibility exists that deferred tax accounts on the individual statements of financial position could be related to taxes from different jurisdictions. Since there is no right to offset taxes between jurisdictions, there is a possibility of having more than one account for deferred taxes reported on a statement of financial position (one for each legal entity). Under ASPE, there could also be one current and one long term deferred tax asset/liability account for each legal entity.

(j)

Refer to last column in tables of part (a) and (e) above.

	<u>2015</u>	<u>2014</u>
Current assets		
Deferred tax asset	\$22,500	
Non-current assets		
Deferred tax asset.....	29,250*	\$9,000
*(\$22,500 + \$6,750)		

Under ASPE, deferred tax assets and deferred tax liabilities are segregated into current and non-current categories. The classification of an individual deferred tax liability or asset as current or non-current is determined by the classification of the asset or liability underlying the specific temporary difference.

PROBLEM 18-11

(a)

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	(ASPE) Current or Long- Term
Warranty liability	-0-	(3,000)	\$3,000	30%	\$900	C
Construction in process	270,000*	300,000	(30,000)	30%	(9,000)	C
Property, plant, & equipment	220,000	240,000	(20,000)	30%	(6,000)	LT
Land	not given	not given	34,500**	30%	<u>10,350</u>	LT
Deferred tax liability, December 31, 2014					(3,750)	
Deferred tax liability before adjustment					<u>0</u>	
Incr. in deferred tax liability, and deferred tax expense for 2014					<u><u>(\$3,750)</u></u>	

* (Construction costs \$270,000 + Gross profit \$30,000)

** \$46,000 X 75%

Total deferred tax expense—2014	\$ 3,750
Deferred tax benefit—\$10,350 – \$0	<u>(10,350)</u>
Deferred tax expense	<u><u>\$ 14,100</u></u>

PROBLEM 18-11 (Continued)

(b)

	<u>Net income</u>	<u>Retained Earnings</u>	<u>Total</u>
Accounting income	\$64,000	(\$5,700)	\$58,300
Permanent difference:			
Non-taxable dividends	(1,400)		(1,400)
Non-deductible fines	3,500		3,500
Non-deductible loss in land value \$46,000 X 25%	11,500		11,500
Reversing differences:			
Warranties: excess of expense over claims paid (\$15,000 – \$12,000)	3,000		3,000
Property, plant, and equipment: excess of CCA over depreciation expense (\$80,000 – \$60,000)	(20,000)		(20,000)
Construction in Process: Excess of reported construction profit over completed contract method (\$30,000 – \$0)	(30,000)		(30,000)
Loss on land not deductible until future years	<u>34,500</u>		<u>34,500</u>
Taxable income	<u>\$65,100</u>	<u>(\$5,700)</u>	<u>\$59,400</u>
Current income taxes at 30%	<u>\$19,530</u>	<u>(\$1,710)</u>	<u>\$17,820</u>

PROBLEM 18-11 (Continued)

(c)

Current Tax Expense	19,530	
Income Tax Payable		17,820
Retained Earnings (tax effect)		1,710
Deferred Tax Expense	3,750	
Deferred Tax Liability		3,750*

***Alternately, if a company kept a separate deferred tax account for each temporary difference:**

Deferred Tax Expense	14,100	
Deferred Tax Asset (Warranty)	900	
Deferred Tax Liability (C.I.P.)		9,000
Deferred Tax Liability (PP&E)		6,000
Deferred Tax Asset (Land writedown)	10,350	
Deferred Tax Benefit		10,350

(d)

Income statement presentation:

Income before income tax		\$64,000
Income tax		
Current tax	\$19,530	
Deferred tax	3,750	23,280
	<hr/>	<hr/>
Net income		\$40,720

PROBLEM 18-11 (Continued)**(e)****Statement of Retained Earnings**

Balance January 1, 2014		-0-
Add: Net income		\$40,720
Less: Financing charge	(\$5,700)	
Less applicable tax	1,710	(3,990)
Balance December 31, 2014		<u>\$36,730</u>

(f) Statement of Financial Position**Refer to last two columns of table in (a).**

Non-current assets		
Deferred tax asset (\$10,350 – \$6,000)		\$4,350
Current liabilities		
Income tax payable		17,820
Deferred tax liability (\$9,000 – \$900)		8,100

Under ASPE, deferred tax assets and deferred tax liabilities are segregated into current and non-current categories. The classification of an individual deferred tax liability or asset as current or non-current is determined by the classification of the asset or liability underlying the specific temporary difference.

PROBLEM 18-11 (Continued)

		<u>@ 30%</u>	<u>Divided by Accounting Income</u>
Accounting income	\$64,000	19,200	30.0%
Non-taxable dividends	(1,400)	(420)	(0.7)%
Non-deductible fines	3,500	1,050	1.6%
Non-deductible land writedown	11,500	3,450	5.4%
		<u>23,280</u>	<u>36.3%</u>

Effective tax rate ($\$23,280 / \$64,000$) 36.3%

The effective tax rate differs from the statutory rate in this case because of the effect of the permanent differences of dividends, fines and 25% of the loss due to writedown of land.

(h) Statement of Financial Position

Current liabilities	
Income tax payable	\$17,820
Non-current liabilities	
Deferred tax liability	3,750
(\$8,100 – \$4,350)	

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

PROBLEM 18-12

(a)		<u>2013</u>	
	Income Tax Receivable—2010		5,000
	(\$25,000 X 20%)		
	Income Tax Receivable—2011		12,000
	(\$60,000 X 20%)		
	Income Tax Receivable—2012		24,000
	(\$80,000 X 30%)		
	Current Tax Benefit		41,000

Note: An acceptable alternative is to record only one Income Tax Receivable account for the amount of \$41,000.

	Deferred Tax Asset		13,500
	Deferred Tax Benefit		
		13,500
	(\$210,000 – \$25,000 – \$60,000 – \$80,000 = \$45,000)		
	(\$45,000 X 30% = \$13,500)		

		<u>2014</u>	
	Current Tax Expense		7,500
	Income Tax Payable		7,500
	[(\$70,000 – \$45,000) X 30%]		
	Deferred Tax Expense		13,500
	Deferred Tax Asset		13,500
	(\$13,500 – \$0)		

		<u>2015</u>	
	Current Tax Expense		22,500
	Income Tax Payable (\$90,000 X 25%)		22,500

PROBLEM 18-12 (Continued)

- (b) An income tax receivable account totalling \$41,000 will be reported under current assets on the statement of financial position at December 31, 2013. This type of receivable is usually listed immediately above inventory in the current asset section. This receivable is normally collectible within two months of filing the amendment to the tax returns reflecting the carryback. Under ASPE, a deferred tax asset of \$13,500 should also be classified as a current asset because the benefits of the loss carryforward are expected to be realized in the year that immediately follows the loss year, which means the benefits are expected to be realized in 2014. A current deferred tax asset is usually listed at or near the end of the list of current assets on the balance sheet. Also, retained earnings is increased by \$54,500 (\$41,000 + \$13,500) as a result of the entries to record the benefits of the loss carryback and the loss carryforward.

If Carly Inc. reports under IFRS, the deferred tax asset related to the loss carryforward would be classified as a non-current asset on the statement of financial position.

(c) <u>2013 Income Statement</u>		
Operating loss before income tax		(\$210,000)
Income tax benefit		
Current benefit due to loss carryback	\$41,000	
Deferred benefit due to loss carryforward	<u>13,500</u>	<u>54,500</u>
Net loss		<u>(\$155,500)</u>

(d) <u>2014 Income Statement</u>		
Income before income tax		\$70,000
Income tax expense		
Current	\$7,500 ^a	
Deferred	<u>13,500</u>	<u>21,000</u>
Net income		<u>\$49,000</u>
^a [(\$70,000 – \$45,000) X 30%]		

PROBLEM 18-12 (Continued)

(e)	<u>2013</u>	
Income Tax Receivable—2010	5,000	
(\$25,000 X 20%)		
Income Tax Receivable—2011	12,000	
(\$60,000 X 20%)		
Income Tax Receivable—2012	24,000	
(\$80,000 X 30%)		
Current Tax Benefit		41,000

Note: An acceptable alternative is to record only one Income Tax Receivable account for the amount of \$41,000. Although its related possible income tax benefit is not recognized in the accounts, Carly Inc. has a tax loss carryforward of \$45,000 which is required to be disclosed.

	<u>2014</u>	
Current Tax Expense	7,500	
Income Tax Payable		7,500
[(\$70,000 – \$45,000) X 30%]		

	<u>2015</u>	
Current Tax Expense	22,500	
Income Tax Payable (\$90,000 X 25%)		22,500

(f) 2013: entry for current taxes – no change
2013: if a valuation allowance is used, the full income tax benefit and deferred tax asset related to the tax loss carryforward is recognized and then offset by the allowance, as follows.

Deferred Tax Asset	13,500	
Deferred Tax Benefit		13,500
(\$45,000 X 30% = \$13,500)		

PROBLEM 18-12 (Continued)

(f) (Continued)

Deferred Tax Expense.....	13,500	
Allowance to Reduce Deferred Tax Asset to Exp. Realizable Value		13,500
(\$13,500 – \$0)		

2014: entry for current taxes – no change

2014: because the tax loss carryforward has now been used, both the amount in the deferred tax account and in its allowance account must be removed, as follows.

Deferred Tax Expense	13,500	
Deferred Tax Asset		13,500

Allowance to Reduce Deferred Tax Asset to Exp. Realizable Value...	13,500	
Deferred Tax Benefit		13,500

Alternatively, one entry could have been made:

Allowance to Reduce Deferred Tax Asset to Exp. Realizable Value...	13,500	
Deferred Tax Asset		13,500

2015: No change to part (e) entry.

PROBLEM 18-12 (Continued)**(g)****2013 Income Statement**

Operating loss before income tax	(\$210,000)
Income tax benefit	
Current benefit due to loss carryback	<u>41,000</u>
Net loss	<u>(\$169,000)</u>

2014 Income Statement

Income before income tax	\$70,000
Income tax expense – Current ^a	<u>7,500</u>
Net income	<u>\$62,500</u>

^a [(\$70,000 – \$45,000) X 30%]

- (h) Using the valuation allowance instead of applying the reduction in value directly does not have any impact on cash flows. The use of the contra allowance simply permits the recording of the full benefits associated with all future deductible amounts in the asset account. This facilitates tracking for management purposes. It has no use for financial reporting purposes except, perhaps, for the transparency of the information. Readers can see the total possible benefits and the extent to which management has judged they will not be realized. Use of the allowance has no impact on cash flows.**

PROBLEM 18-13

- (a) $\$135,000 \times 35\% = \$47,250$, deferred tax liability, December 31, 2013.
- (b) The prior period error has the following effect on the December 31, 2013 statement of financial position: The land is understated by \$40,000, retained earnings is understated by the \$40,000 error in the expenses on the 2013 income statement and overstated by the income tax effect (35% of \$40,000 = \$14,000), and the income tax payable account is understated by \$14,000.

Land	40,000	
Retained Earnings		40,000
Retained Earnings	14,000	
Income Tax Payable		14,000

To recognize additional income tax payable on the amount deducted in error in 2013.
(2013 tax return is refiled)

(c)

Accounting Income		\$1,645,000
Add:		
Golf club dues		4,500
Non deductible interest costs		2,500
Depreciation expense		365,000
Excess of year's bad debt expense over tax deductible amount		20,000
Less: CCA		<u>(300,000)</u>
Taxable Income		\$1,737,000

PROBLEM 18-13 (Continued)**(c) (continued)**

Asset / Liability	Tax Base	Carrying Amount	Deductible / (Taxable) Temporary Difference	Tax Rate	Deferred Tax (Liability) Asset
Property, plant, and equipment	\$933,000*	\$1,352,000 + \$16,000 – \$365,000 = \$1,003,000	\$ (70,000)	35%	\$ (24,500)
Allowance for doubtful accounts	not given	not given	20,000	35%	<u>7,000</u>
Deferred tax liability, Dec. 31, 2014					<u>\$(17,500)</u>
Balance before adjustment					<u>(47,250)</u>
Adjustment required to deferred tax liability, and deferred tax benefit, 2014					\$ 29,750

*Carrying amount, Dec. 31, 2013	\$1,352,000
Future taxable amount, Dec. 31, 2013	<u>(135,000)</u>
UCC, Dec. 31, 2013	1,217,000
2014 addition to class	16,000
Less 2014 CCA	<u>(300,000)</u>
UCC, Dec. 31, 2014	\$ 933,000

PROBLEM 18-13 (Continued)**(c) (continued)****Current tax expense = \$1,737,000 x 35% = \$607,950****Future tax expense = \$29,750 (benefit)****Total income tax expense = \$607,950-29,750 = \$578,200**

Current tax expense	607,950	
Income tax payable		607,950
Deferred tax liability	29,750	
Deferred tax benefit		29,750

(d)**Income Statement:**

Net income before income tax		\$1,645,000
Less: Income tax expense		
Current tax expense	\$607,950	
Deferred tax (benefit)	(29,750)	578,200
Net Income		<u>\$1,066,800</u>

Statement of Retained Earnings:

Retained Earnings, January 1, 2014		\$5,678,000
As previously reported		\$5,678,000
Correction of prior period error, net of income tax of \$14,000		26,000
Restated balance of Retained Earnings		<u>5,704,000</u>
Add: Net Income		<u>1,066,800</u>
Retained Earnings, December 31, 2014		<u>\$6,770,800</u>

PROBLEM 18-14

(a)

2014:

Statement of Financial Position Account Dec. 31, 2014	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	(ASPE) Current or Long- Term
Prepaid Rent	-0-	\$89,000	(\$89,000)	27%	(\$24,030)	C
Rent Payable	-0-	(146,000)	146,000	27%	<u>39,420</u>	LT
Deferred tax asset, December 31, 2014					15,390	
Deferred tax asset before adjustment					<u>0</u>	
Incr. in deferred tax asset, and deferred tax benefit for 2014					<u>\$ 15,390</u>	

2015:

Statement of Financial Position Account Dec. 31, 2015	Tax Base	Carrying Amount	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	(ASPE) Current Long- Term
Prepaid Rent	-0-	\$92,000	(\$92,000)	29%	(\$26,680)	C
Rent Payable	-0-	(133,000)	133,000	29%	<u>38,570</u>	LT
Deferred tax asset, December 31, 2015					11,890	
Deferred tax asset before adjustment					<u>15,390</u>	
Decr. in deferred tax asset, and deferred tax expense for 2015					<u>(\$ 3,500)</u>	

PROBLEM 18-14 (Continued)**(b)****2014:**

Accounting income		\$884,000
Permanent differences:		
Golf club dues	\$13,000	
Interest incurred to earn exempt income	<u>4,000</u>	<u>17,000</u>
		901,000
Reversing differences:		
Prepaid rent deductible when paid		(89,000)
Accrued rent expense not yet deductible		<u>146,000</u>
Taxable income		<u>\$958,000</u>
Current income taxes at 28%		<u>\$268,240</u>

2015:

Accounting income		\$997,000
Permanent differences:		
Golf club dues	\$11,000	
Interest incurred to earn exempt income	<u>6,000</u>	<u>17,000</u>
		1,014,000
Reversing differences:		
Excess of rent paid over rent expense recognized		
(\$92,000 – \$89,000)		(3,000)
Excess of rent paid over rent expense recognized		
(\$146,000 – \$133,000)		<u>(13,000)</u>
Taxable income		<u>\$998,000</u>
Current income taxes at 29%		<u>\$289,420</u>

PROBLEM 18-14 (Continued)

(c)

2014 Journal entries:

Current Tax Expense.....	268,240	
Income Tax Payable.....		268,240
Deferred Tax Asset.....	15,390	
Deferred Tax Benefit.....		15,390

2015 Journal entries:

Current Tax Expense.....	289,420	
Income Tax Payable.....		289,420
Deferred Tax Expense.....	3,500	
Deferred Tax Asset.....		3,500

PROBLEM 18-14 (Continued)**(d)**

	<u>2015</u>	<u>2014</u>
Income before income tax	<u>\$997,000</u>	<u>\$884,000</u>
Income tax expense		
Current	289,420	268,240
Future (benefit)	<u>3,500</u>	<u>(15,390)</u>
	<u>292,920</u>	<u>252,850</u>
Net income	<u>\$704,080</u>	<u>\$631,150</u>

(e) Refer to last two columns in tables in part (a) above.

	<u>2015</u>	<u>2014</u>
Non-current assets		
Deferred tax asset	\$38,570	\$39,420
Current liabilities		
Deferred tax liability.....	26,680	24,030

Under ASPE, deferred tax assets and deferred tax liabilities are segregated into current and non-current categories. The classification of an individual deferred tax liability or asset as current or non-current is determined by the classification of the asset or liability underlying the specific temporary difference.

PROBLEM 18-14 (Continued)

		<u>@ 29%</u>	<u>Divided by Accounting Income</u>
Accounting income	\$997,000	\$289,130	29.0%
Non-deductible dues	11,000	3,190	0.3%
Non-deductible interest	6,000	<u>1,740</u>	<u>0.2%</u>
		294,060	29.5%
Change in tax rate (\$146,000 – \$89,000) × (29% – 27%)	57,000	<u>(1,140)</u>	<u>(0.1%)</u>
		<u>\$292,920</u>	<u>29.4%</u>
Effective tax rate (\$292,920/\$997,000)			29.4%

The effective tax rate differs from the statutory rate because of the effect of the permanent differences of golf club dues and interest, and because of the effect of the change in tax rate during the year on the deferred tax accounts.

(g)

The responses to (a) to (f) would not change in amount, although different terminology might be used (that is, IFRS would tend to use the terms deferred, while ASPE preparers might use the terms related to future taxes). The only calculation differences would be related to the classification of the deferred accounts on the statement of financial position. Under IFRS, these would be:

	<u>2015</u>	<u>2014</u>
Non-current assets		
Deferred tax asset	\$11,890**	\$15,390*

* (\$39,420 – \$24,030 = \$15,390)

** (\$38,570 – \$26,680 = \$11,890)

IFRS require that all deferred tax assets and liabilities be reported as non-current items on a classified statement of financial position.

PROBLEM 18-15

Prior year tax rate: \$616,000 / \$2,200,000 = 28%

Statement of Financial Position Account Dec. 31, 2014	Tax Base*	Carrying Amount*	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	If (ASPE) Current Long- Term
PP&E before change in tax rate			(\$2,200,000)	28%	(\$616,000)	LT
Increase in deferred tax liability due to change in tax rate (\$2,200,000 X 2%), and deferred tax expense adjustment Deferred tax liability (related to PP&E), Dec. 31/14					(44,000) <u>(\$660,000)</u>	

* not provided; no change in amount of PP&E temporary difference since Dec. 31/13

Statement of Financial Position Account Dec. 31, 2014	Tax Base*	Carrying Amount*	Deductible (Taxable) Temporary Differences	Tax Rate	Deferred Tax Asset (Liability)	If (ASPE) Current Long- Term
PP&E			(\$2,200,000)	30%	(\$660,000)	LT
Pension liability			(24,000)	30%	(7,200)	LT
Warranty liability			31,000	30%	<u>9,300</u>	C
Deferred tax liability, Dec. 31/14					(\$657,900)	
Deferred tax liability before adjustment					<u>(660,000)</u>	
Decrease (net) needed in deferred tax liability, and net deferred tax benefit					<u>\$ 2,100</u>	

* not given in the problem.

PROBLEM 18-15 (Continued)

Calculation of loss for tax purposes and loss carryforward:

Accounting loss	(\$494,000)
Permanent differences:	
Development costs (50% X \$150,000)	75,000
Meals and entertainment (50% X \$38,000)	19,000
Reversing differences:	
Warranty expense	31,000
Pension funding > expense	<u>(24,000)*</u>
Loss for income tax purposes	(393,000)
Carryback to prior years	<u>123,000</u>
Loss available for carryforward	(270,000)
50% realization probable	<u>50%</u>
Portion of loss to recognize as benefit	(135,000)
Tax rate	<u>30%</u>
Deferred tax asset and current benefit	<u>(\$40,500)</u>
* (\$87,000 – \$111,000 = –\$24,000)	

2014 Income tax journal entries:

Income Tax Receivable (\$123,000 x 28%).....	34,440	
Current Tax Benefit		34,440
Deferred Tax Expense.....	44,000	
Deferred Tax Liability (incr. in tax rate)....		44,000
Deferred Tax Liability	2,100	
Deferred Tax Benefit		2,100
Deferred Tax Liability (loss carryforward).....	40,500	
Deferred Tax Benefit (loss carryforward).		40,500

Instead of the three deferred tax entries above, one entry could have been made as follows:

Deferred Tax Expense	1,400	
Deferred Tax Liability		1,400
(\$44,000 - \$2,100 - \$40,500)		

PROBLEM 18-15 (Continued)**Income statement (partial)**

Loss before income tax			(\$494,000)
Income tax benefit (expense)			
Current – loss carryback	\$34,440		
Deferred	(1,400)*	33,040	
Net income (loss)			<u>(\$460,960)</u>

* $(\$40,500 - \$44,000 + \$9,300 - \$7,200 = \$1,400)$

Note to the financial statements: The deferred tax expense increased by \$44,000 due to a change in the tax rate in 2014.

Reconciliation – Statutory rate to effective rate:

		<u>@ 30%</u>	<u>÷ Account- ing loss</u>
Income before taxes	\$494,000	\$148,200	30.00%
Non-deductible:			
Development costs	75,000	(22,500)	(4.55%)
Meals/entertainment	19,000	<u>(5,700)</u>	<u>(1.15%)</u>
		120,000	24.30%
Tax rate adjustment on reversing differences (\$2,200,000 x .02)	2,200,000	<u>(44,000)</u>	<u>(8.91%)</u>
½ of loss carryforward recovery not probable	135,000	<u>(40,500)</u>	<u>(8.20%)</u>
Tax rate adjustment on loss carryback (\$123,000 x .02)	123,000	<u>(2,460)</u>	<u>(0.50%)</u>
		<u>\$33,040</u>	<u>6.69%</u>
Effective tax rate (\$33,040 / \$494,000 = 6.69%)			<u>6.69%</u>

PROBLEM 18-15 (Continued)

Quirk Inc.'s effective tax rate differs from the statutory rate due to permanent differences that will never be subject to tax; a change in tax rate that impacts temporary differences that are being carried forward; not recognizing the deferred tax benefit of half of the loss carryforward; and, recovery of prior year income taxes at a tax rate different than the current year rate.

CASES

Note: See the Case Primer on the Student website, as well as the Summary of the Case Primer in the front of the text. Note that the first few chapters in volume 1 lay the foundation for financial reporting decision making.

CA 18-1 BAKER COMPANY LIMITED

Overview

- Assume that GAAP is a constraint since the financial statements are being audited. As a private company, the company could use ASPE or IFRS and therefore differences will be identified.
- The role is that of company auditor and, therefore, the auditor would ensure transparency.
- Management has high expectations of the company's ability to turn around and continue to grow—and may be biased to show this.
- Users include shareholders/investors who will want transparent statements. Given loss situation—they will be looking to decide whether to divest or not.

Analysis and Recommendations

Issue: The issue is whether the benefit from the losses should be recognized in the current financial statements.

To the extent that taxes were paid in previous years, the losses would first be carried back to recover these taxes and a partial benefit could be recognized.

The real issue is whether there is sufficient certainty to recognize the benefits that might be realized if the losses are carried forward. The benefits may be recognized if it is more likely than not that the benefits will be realized (under ASPE) or probable (under IFRS). This ultimately depends on the existence of sufficient taxable income in the carryforward period to be able to utilize the loss and shelter future taxable income. Note that under ASPE, the entity has a choice to use the taxes payable method or future income taxes method.

CA 18-1 (Continued)

Recognize benefit of losses	Do not
<ul style="list-style-type: none"> - On the one hand, management has big plans to expand into new markets with new products. Two new products are scheduled to be introduced and there are sufficient customers lined up to purchase the products, such that the company is predicting at least a break even situation using conservative estimates. - The fact that the company did not suffer pre-recession losses in its first two years is a signal that they must be doing something right. With respect to the economists, it might be argued that no one can really predict the future. Management has better insight into its own company and customers and, therefore, might be in a better position to predict the future. - The fact that numerous competitors have gone under will hopefully open up new markets and help increase market share. - In addition, this option would not be allowable under the taxes payable method (ASPE). 	<ul style="list-style-type: none"> - Forming a conclusion that the benefits are likely to be realized is difficult when certain unfavourable evidence exists. - In this case, unfavourable evidence would include the fact that there is a history of marginal profits only (and, of course, the loss) and the fact that this company is still in its formative years. It is not unusual for companies to sustain losses in the start-up period. - Furthermore, it might be argued that the current state of the economy is unsettled. Unemployment is still high and consumer spending has still not increased significantly. The fact that economists are predicting that it might take two to three more years for consumer spending to recover results in more uncertainty. - In addition, if using the taxes payable method (ASPE), would only recognize taxes receivables based on current and/or refiled tax returns. Therefore no tax assets would be recorded in advance.

In conclusion, although management might be able to make a strong case for profitability, it is still a projection at best and, given that the economy still appears to be slow, it might be more conservative not to recognize the benefit. This is in keeping with the role of auditor. The unrecognized benefits and expiry dates would be note disclosed.

CA 18-2 CRINGLE INC. (CI)

Overview

- Role – controller – potential bias towards making company look better since looking for new capital and to potentially refinance loan.
- Bank and potential investors are key users who will be relying on statements to make decisions – need transparency.
- Public company since shares trade on TSX – IFRS is a constraint.
- For investments, company must decide whether to follow IFRS 9 (early adopt) or IAS 39.

Analysis and recommendations

Issue: Investment in common shares

Equity method	At fair value with gains and losses through income or OCI
<ul style="list-style-type: none"> - 20% - borderline for significant influence. - Representation on Board (1/4) may allow influence. - Original intent was for strategic purposes. 	<ul style="list-style-type: none"> - 20% inconclusive. - No longer being held for strategic purposes – i.e. intent to sell/trade is share prices rise above certain point. - If FVOCI – revalue to fair value and gains/losses to OCI (if following IFRS 9 must elect). - If FVTPL (HFT) – revalue to fair value and gains/losses to net income. - Option to treat as either (FVTPL and/or FVOCI) under IAS 39 or IFRS 9.

Recommendations:

Could select any of the options however, given the intent to sell if the shares reach a certain price, consider measuring at fair value with gains/losses through income (easier). This option is available under IFRS 9 and IAS 39.

CA 18-2 (Continued)

Issue: Investment in bonds

Amortized cost	Fair value (with gains/losses booked to income)
<ul style="list-style-type: none"> - Under IAS 39 - Intent to hold to maturity expressed and ability to hold given new potential influx of cash (raising capital). - Amortized cost – amortize premium as an adjustment to interest cost. - Under IAS 39 – may have to segregate the conversion option and value at fair value (embedded derivative). NB. This is generally beyond the scope of the text. 	<ul style="list-style-type: none"> - Under IFRS 9 – use amortized cost only if company manages cash flows on the basis of yield to maturity and contractual cash flows include principal and interest. In this case it is not clear that the entire business model includes managing debt instruments on a yield to maturity basis and thus this would not be valued at amortized cost. - In addition, since these are debt instruments, the option to value at FVOCI is not available under IFRS 9. IFRS 9 only allows this option for equity instruments. - Under IAS 39 if classified as HTM (amortized cost) and sell prior to maturity, it may invoke tainting provisions (if significant). If this is the case, would no longer be able to value this and other debt securities at amortized costs. Therefore do not measure at amortized cost upfront and avoid risk of tainting. - More transparent to value at FVTPL since business model seems to indicate the investments are incidental to main business.

Recommendations:

To value at fair value with gains/losses through income.

CA 18-2 (Continued)

Issue: Revenue recognition – Non-refundable fees

Recognize upfront fee	Do not
<ul style="list-style-type: none"> - Multiple element arrangement? - Proprietary info considered separable unit – transferable per company and therefore must have standalone value. - Objective and reliable evidence of undelivered item since issued renewal contracts to others this year. - Persuasive evidence of contract – since deal is done and likely documented. - Measurable since no material uncertainties. - Delivery of proprietary info already occurred. - Would have to bifurcate. 	<ul style="list-style-type: none"> - Proprietary info may not be transferable separately and therefore considered an integral part of the whole transaction (has no value otherwise if not transferrable). - Recognize over time – straight line unless other pattern. - May use percentage of completion method.

Recommendations:

To recognize entire contract amount over time as more reflective of the bundled nature of the transaction.

CA 18-2 (Continued)

Issue: Hedging

Hedge accounting – discussion of theory as requested by client	No hedge accounting
<ul style="list-style-type: none"> - Meant to ensure that gains/losses from hedged items offset gains/losses from hedging items in income in same period. - Must use if do not already do so. - Modifies normal accounting. - Must ID hedging relationship between hedged and hedging item - Must ensure effective. 	<ul style="list-style-type: none"> - Optional. - Costs and complexity are significant. - No need to use hedge accounting since gains and losses of hedged (US AR) and hedging items (forward contract) already essentially offset (forward contract recognized, valued at fair value and gains/losses to net income already. US AR revalued to spot rate with gains and losses to net income). - Natural hedge does not require special accounting since US AP also revalued to spot rate with gains/losses to income.

Recommendations:

There is no need to use hedge accounting. Risk that counterparties will fail to complete transaction – forward contract – would mean still exposed to risk.

Issue: Recognize benefit of LCF

Yes	No
<ul style="list-style-type: none"> - Due to a one-time loss. - Otherwise expected to be profitable. 	<ul style="list-style-type: none"> - Not sure if company will be profitable next year.

TIME AND PURPOSE OF WRITING ASSIGNMENTS

WA 18-1 (Time 20–25 minutes)

Purpose—to have the student explain the objectives when accounting for income taxes in the financial statements and the basic principles that are applied in meeting the objectives. The student is required to use the conceptual framework and the current definitions of assets and liabilities to explain the recognition of future tax accounts on the balance sheet.

WA 18-2 (Time 20–25 minutes)

Purpose—to develop an understanding of both reversing and permanent differences. The student is required to explain the nature of eight differences and to explain why each is a permanent or reversing difference. Also, the nature of and the classification of future tax accounts are examined along with differences under IFRS and ASPE.

WA 18-3 (Time 20–25 minutes)

Purpose—to develop an understanding of future income taxes resulting from the differences, which exist between taxable income and pre-tax accounting income. This case involves a list of items, each of which the student is required to identify as either a temporary difference or a permanent difference. Additionally, the student must decide, for each temporary difference, whether it will result in future taxable or deductible amounts and whether it will usually give rise to a future income tax liability or future income tax asset. Differences between ASPE and IFRS are also highlighted.

WA 18-4 (Time 15–20 minutes)

Purpose—to provide the student with an ethics case for which to conclude whether or not a business is rightfully deferring income taxes by managing the reversing of acquisitions and disposals of property, plant, and equipment.

WA 18-5 (Time 15–20 minutes)

Purpose—to develop an understanding of future taxes and balance sheet disclosure. The student must demonstrate an understanding of how to determine the appropriate tax rate to use in computing future taxes when different tax rates are enacted for various years affected by existing temporary differences.

TIME AND PURPOSE OF WRITING ASSIGNMENTS (Continued)

WA 18-6 (Time 20–25 minutes)

Purpose—to develop an understanding of specific differences under IFRS and ASPE for reporting subsequent future income tax differences resulting from a prior period adjustment, a revaluation adjustment and an equity investment.

WA 18-7 (Time 20–25 minutes)

Purpose—to assist students to understand the differences between IFRS and ASPE for reporting income taxes and the conceptual reasons for these differences.

SOLUTIONS TO WRITING ASSIGNMENTS

WA 18-1

- (a) The following are objectives in accounting for income taxes:
1. To recognize the amount of taxes payable or refundable for the current year.
 2. To recognize deferred/future income tax liabilities and assets for the future tax consequences of events that have been recognized in the financial statements or tax returns.
- (b) The following basic principles are applied in accounting for income taxes at the date of the financial statements:
1. A current income tax liability or asset is recognized for the estimated taxes payable or refundable on the tax return for the current year.
 2. A deferred/future income tax liability or asset is recognized for the estimated future tax effects attributable to temporary differences and carry-forwards using the enacted (or substantially enacted) tax rates.
 3. The measurement of current and deferred/future tax liabilities and assets is based on provisions of the enacted tax law; the effects of future changes in tax laws or rates are not anticipated.
 4. If necessary, and based on available evidence, deferred/future income tax assets are adjusted to remove tax benefits that are not expected to be realized.
- (c) Under the future income tax method (ASPE) or the temporary difference approach (IFRS) of accounting for income taxes, the deferred (or future) income tax outflows and inflows related to the realization of assets and the settlement of liabilities for their carrying amounts are recognized as deferred tax liabilities and deferred tax assets. (Note: we use the term deferred here and below for both IFRS and ASPE to simplify the discussion)

These deferred tax liabilities and deferred tax assets meet the conceptual definitions of liabilities and assets. In other words, temporary differences between an asset or liability's carrying amount and its tax base, unused tax losses, and income tax reductions may generate deferred benefits in the form of reduced tax payments in later periods. Such items would be recognized as deferred tax assets when the appropriate criteria are met, since they satisfy the conceptual definition of assets.

This method is considered to be more effective in achieving the objective of financial reporting—communicating information that is useful to users—as the method provides users with information about a company's economic

WA 18-1 (Continued)

resources and obligations regarding income tax consequences of all transactions and events.

In reporting deferred tax assets and liabilities, there is one difference between ASPE and IFRS. ASPE (under this alternative) will report future tax assets or future tax liabilities as either current or non-current. This classification will depend on when the future tax amount is expected to reverse. Under IFRS, all deferred tax assets and liabilities are classified as non-current.

(d) An asset provides an economic benefit to the entity, the entity controls and it results from past transactions or events. Currently, there are two issues with respect to deferred tax assets, as discussed below:

- The value of this asset will be received sometime in the future. As such, it should be discounted to approximate the current value of the benefit to be received. Ideally, some measurement using probabilities of likely outcomes would be used to determine the best estimate of the economic resource.
- Does the entity control the asset? In the case of loss carry forward benefits, the company has not yet made a profit, the government does not yet owe the company this amount, and the realization of this asset is very dependent on a future event that may or may not happen. Consequently, the right is not “controllable”. Perhaps it would be better thought of as a “conditional right to receive the benefits”. Given this strict definition, perhaps the deferred tax asset arising from the use of loss carry forwards should not be recorded.

A liability represents a present duty or responsibility that obligates the company, giving it little discretion to avoid the obligation and that results from a past transaction. Similar issues arise in looking at this definition as follows:

- The value of this liability will be paid sometime in the future. As such, it should be discounted to approximate the current value of the benefit to be received. In addition, there are a variety of different outcomes. As a result, it could be argued that the entity should estimate the amount and timing of the obligation under each of these different outcomes, determine the present values of each of these outcomes, and then estimate the probability of each outcome.

WA 18-1 (Continued)

Does this represent a represent an enforceable obligation? The company does not yet owe these taxes. The amount of the deferred tax liability will depend on future taxable profits, and when these temporary differences will reverse. For example, if a company continues to invest in property, plant and equipment and the capital cost allowance claim is always greater than the depreciation for tax purposes, then it may be a long time (if ever) that this liability for payment will arise. Consequently, the obligation is not presently enforceable. This liability represents a “conditional obligation to pay”, given certain future events occur. As described above, using a measurement that considers the probability of different outcomes would likely better reflect the amount of the future obligation.

WA 18-2

- (a) 1. Reversing difference. The full, estimated, three years of warranty costs reduce the current year's pre-tax accounting income, but they will reduce taxable income in varying amounts each respective year, as paid. Assuming the estimate as to each warranty is valid, the total amounts deducted for accounting and for tax purposes will be equal over the three-year period for a given warranty. This is an example of an expense that in the first period reduces pre-tax accounting income more than taxable income and in later years reverses. This type of temporary difference will result in future deductible amounts, which will give rise to the current recognition of a future income tax asset. Another way to evaluate this situation is to compare the carrying value of the warranty liability with its tax basis (which is zero). When the liability is settled in a future year, an expense will be recognized for tax purposes but none will be recognized for financial reporting purposes. Therefore, tax benefits for the tax deductions should result from the future settlement of the liability.
2. Reversing difference. While the change in value is included in income in the current year, it will not be taxable/deductible until sold. Therefore, it is a reversing difference.
3. Permanent difference. The difference is not due to different methods of depreciation, but due to different amounts accepted as "cost". Since only the amount accepted originally as its tax cost can be amortized in the future, the difference is a permanent one.
4. Permanent difference. The investor's share of earnings of an investee accounted for by the equity method is included in accounting income, while dividends received from taxable Canadian corporations are excluded from taxable income. The amount included in accounting income is a permanent difference deducted when computing taxable income.
5. Reversing difference. The write down in the inventory is recognized for accounting purposes in the current year, but the loss is not allowed to be deducted for tax purposes until the inventory is sold. Hence, it is a reversing difference.
6. Permanent and reversing difference. Any loss from a litigation accrual would not be deductible for tax purposes until paid. This is a reversing difference arising in the year accrued. The portion of the loss that is expected to be a penalty, which cannot be used as a deductible expense for tax purposes, will be a permanent difference.

WA 18-2 (Continued)

7. Reversing difference under IFRS only (ASPE does not allow the revaluation model to be used). This write down for the properties will cause the deferred tax accounts to change, but the loss is not reported for current tax purposes. Once the land and buildings are actually disposed, the taxable income will be impacted by difference between the original cost and the proceeds on disposal. (At this time, a portion of the difference may be shown as recaptured capital cost allowance and a portion as capital gains, but this will not be known until the actual sale proceeds are determined.)
8. Reversing difference – When the retirement obligation is settled, the full cash amount paid will be reflected as a reduction of taxable income. However, in the accounting records, this has been reported each year since the obligation was originally accrued, along with the gain on settlement in the final year. As a result, there will be an amount in deferred tax liabilities with respect to this obligation. When the obligation is paid, this future tax liability will be reversed, and the full amount of taxes now owing will be recorded as income taxes payable.

WA 18-2 (Continued)

(b)

Deferred tax accounts

1. The estimated warranty costs will be deductible in future periods and cause taxable income to be less than accounting income in the future.
→ Deferred tax asset (Classified as non-current, assuming the three-year warranty liability is classified as non-current liability) under both IFRS and ASPE.
2. Holding/unrealized gains → will be taxable when realized → deferred tax liability.
Holding/unrealized losses → will be deductible when realized → deferred tax asset.
(Similar treatment under ASPE and IFRS).
3. No related deferred tax accounts.
4. No related deferred tax accounts.
5. The impairment loss will be deductible in future periods and cause taxable income to be less than accounting income in the future.
→ Deferred tax asset (Classified as current under ASPE and non-current under IFRS).
6. The penalty portion does not have related deferred tax accounts. The rest of it results in deferred tax asset. (Classified as current or non-current based on the expected reversal date under ASPE and non-current under IFRS).
7. This is not allowed under ASPE. Under IFRS, the loss will be deductible in future periods and cause taxable income to be less than accounting income in the future.
→ Deferred tax asset (or a reduction in the related future tax liability account) (Classified as non-current under IFRS).
8. The cash settlement of the retirement obligation results in the current taxable income being lower than the current accounting income. As such, there will be a reduction in the future tax asset account that had been increasing in previous years as the expense was recorded for accounting purposes but not yet for tax purposes. The related future tax asset should be eliminated with this settlement.

WA 18-3

	(a)	(b)	
1.	Reversing diff.	Future deductible amounts	Deferred tax asset
2.	Reversing diff.	Future deductible amounts	Deferred tax asset
3.	Permanent diff.	No effect on future tax returns	No deferred taxes
4.	Permanent diff.	No effect on future tax returns	No deferred taxes
5.	Reversing diff.	Future taxable amounts	Deferred tax liab.
6.	Reversing diff.	Future taxable amounts	Deferred tax liab.
7.	Permanent diff.	No effect on future tax returns	No deferred taxes
8.	Permanent diff.	No effect on future tax returns	No deferred taxes
9.	Permanent diff.	No effect on future tax returns	No deferred taxes
10.	Reversing diff.	Future deductible amounts	Deferred tax asset
11.	Reversing diff.	Unrealized gains: future taxable amounts	Deferred tax liab.
		Holding/unrealized losses: future deductible amounts	Deferred tax asset
12.	Reversing diff.	Future deductible amounts	Deferred tax asset
13.	Reversing diff.	Future taxable amounts	Deferred tax liab.

WA 18-4

- (a) Accelerated depreciation, such as the double declining balance method used for income tax purposes, allows a company to deduct substantial capital cost allowance early in the asset's life. Yearly CCA declines to a point where the accelerated CCA amount is lower than the depreciation expense computed under the straight-line method. The reversing point occurs when the accelerated CCA matches the straight-line rate. Some companies are motivated to sell assets prior to this point to maximize the CCA benefit provided in terms of income taxes. As long as the company is growing, the company may receive a prolonged deferral of income taxes.
- (b) The deferral of income taxes means that, due to temporary differences caused by the difference in financial accounting principles and tax laws, a company will be able to defer paying its income taxes until future periods. The practice of selling-off assets before the differences reverse means that the company may pay a lesser amount of taxes to the government.
- (c) Shareholders would be harmed by Mesa's income tax practice. In order to maintain this policy, and using the mechanism described in (a) above, the company has to systematically acquire new assets at a cost higher than the previously disposed assets. To repurchase assets at a lower cost could also trigger recaptured CCA in some cases. This means that management is probably embarking on a short-term policy of improving its financial picture at the cost of a damaging cash management policy, or it is indebting itself. One would also have to question whether there is a legitimate need for these new assets. This would be demonstrated by a decrease in the effectiveness of their use of assets in declining return-of-assets or asset-turnover ratios.
- (d) As an ethical accountant, Henrietta is obligated to uphold objectivity and integrity in the practice of financial reporting. If she thinks that this practice is unethical, then she needs to communicate her concerns to the highest levels of management within Mesa, including members of the Board and/or the Audit Committee. However, it would appear here that Mesa is simply trying to minimize its income taxes, which probably would not be considered unethical.
- Current tax legislation permits taxpayers to arrange their affairs in order to pay the minimum amount of tax—when it is done within tax rules. However, transactions whose sole purpose is to avoid paying income taxes and have no bona fide business purpose can be caught under GAAR (General anti-avoidance rules). These transactions, if caught, could be re-assessed by Canada Revenue Agency.

WA 18-5

(a)

- (1) The 35% tax rate would be used in calculating the deferred tax liability at December 31, 2014, if a net operating loss expected in 2015 is to be carried back to 2014 (the enacted tax rate is 35% in 2014). (See discussion below.)
- (2) The 30% tax rate would be used in calculating the deferred tax liability at December 31, 2014, if taxable income is expected in 2015 (the tax rate enacted for 2015 is 30% and 2015 is the year in which the future taxable amount is expected to occur). (See discussion below.)
- (3) The 24% tax rate would be used in calculating the deferred tax liability at December 31, 2014, if a net operating loss expected in 2015 is to be carried forward to 2016 (the tax rate enacted for 2016 is 24%). (See discussion below.)

Discussion:

In determining the future tax consequences of temporary differences, it is helpful to prepare a schedule that shows in which future years existing temporary differences will result in taxable or deductible amounts. The appropriate enacted tax rate is applied to these future taxable and deductible amounts. In determining the appropriate tax rate, you must make assumptions about whether the entity will report taxable income or losses in the various future years expected to be affected by the reversal of existing temporary differences. So, you calculate the taxes payable or refundable in the future due to existing temporary differences. In making these calculations, you apply the provisions of the tax laws and enacted tax rates for the relevant periods.

For future taxable amounts:

1. If taxable income is expected in the year that a future taxable amount is scheduled, use the enacted rate for that future year to calculate the related deferred tax liability.
2. If an operating loss is expected in the year that a future taxable amount is scheduled, use the enacted rate of what would be the prior year that the operating loss would be carried back to (or the enacted rate of the future year to which the carryforward would apply, whichever is appropriate), to calculate the related deferred tax liability.

For future deductible amounts:

1. If taxable income is expected in the year that a future deductible amount is scheduled, use the enacted rate for that future year to calculate the related deferred tax asset.

WA 18-5 (Continued)

2. If an operating loss is expected in the year that a future deductible amount is scheduled, use the enacted rate of what would be the prior year that the operating loss would be carried back to (or the enacted rate of the future year to which the carryforward would apply, whichever is appropriate), to calculate the related deferred tax asset.

(b)

(1) Assuming that the company will recover the asset value through use, the company will generate taxable income of \$ 8 million, but only be able to deduct CCA of \$3,500,000. Consequently, a temporary taxable difference between the current carrying value and the tax value is \$8,000,000 minus \$3,500,000 which is \$4,500,000. At a tax rate of 30%, a deferred tax liability of \$1,350,000 will be reported. As the gain on this fair value adjustment is reported in net income, any change in the deferred tax liability account required to report a total amount of \$1,350,000 would also be reported in net income.

(2) If the company expects to recover the value of the asset through a sale in the next year, the proceeds on this sale will attract different income tax rates. The deferred tax liability should be calculated based on the applicable tax rates to be paid. Given the above information, the deferred tax liability is calculated as follows:

\$1,500,000 will be recaptured and taxed at 30% = \$450,000

\$3,000,000 will be taxed as capital gains and attract a tax rate of 15% (as given in the question) = \$450,000

Total deferred tax liability will be \$900,000 (= \$450,000 + \$450,000).

Any change required to adjust the deferred tax liability will be reported in net income, as the fair value adjustment was reported in net income.

(c) If this property was measured using the revaluation method, the same numbers would apply as calculated above. However, changes required to adjust the deferred tax liability account will be reflected in other comprehensive income, since the revaluation adjustment was reported via the other comprehensive income account.

WA 18-6

(1) An adjustment of \$30,000 [$\$1 \text{ million} \times (28\% - 25\%)$] is required to increase the deferred tax liability. However, there is a difference in how the offsetting amount to this entry is recorded under IFRS and ASPE. Under IFRS, using backward tracing, as the error correction was originally recorded in retained earnings, then the related income tax impact of \$30,000 must also be recorded against retained earnings. In contrast, under ASPE, the offsetting adjustment would be posted through the current net income.

(2) Under ASPE, the assets are not revalued, (except one time on transition which is being ignored as part of this question). Consequently, under ASPE, the company will not increase the value of the property to its fair value. Under IFRS, the company has the option to adopt the revaluation method. Using the revaluation method, the increase in the fair value of \$3.5 million (10 million less \$6.5 million) is reported as a revaluation surplus. There is now a total temporary difference of \$4.3 million between the accounting value (\$10 million) and the tax value \$5.7 million ($\$8 \text{ million} - \2.3 million) of the asset. The related tax impact would be to increase the deferred tax liability by \$980,000 ($\$3.5 \text{ million} \times 28\%$) and the offsetting entry would be to other comprehensive income. The total deferred tax liability related to this asset would now be: \$1,204,000 ($10 \text{ million} - \$5.7 \text{ million} \times 28\%$). This would have been recorded as follows:

In previous years: $(\$6.5 \text{ million} - \$5.7 \text{ million}) \times 28\% = \$224,000$
 This year's adjustment: \$980,000
 Total deferred tax liability: \$1,204,000

(3) Under ASPE, the company has the option to report this equity investment at fair market value through net income or at cost. The company also has the option to use the taxes payable method or the future income tax method for reporting income taxes. Below, these different combinations of alternatives are examined:

- i. Equity investment at cost and taxes payable method is used: In this case, there is no impact on the income taxes for the company. Since LGS has not sold the investment, there are no taxes to be paid. In addition, since the investment has not been revalued, there is no impact on the accounting income for the year ended December 31, 2015. The tax value and the accounting value of the asset are the same, and there are no reversing differences to recognize.
- ii. Equity investment at cost and the future income tax method is used for taxes. Under these methods, the investment carrying value remains at \$340,000, and no increase in value is reported in the net income. Also, since the gain is only reported for tax purposes when realized, there is no impact on taxes payable. As a result, the tax value and accounting value

WA 18-6 (Continued)

- of the asset are the same at \$340,000, and there is no deferred tax liability.
- iii. Equity investment is adjusted to fair value, and the company uses the taxes payable method. In this case, the asset would be increased to \$510,000, and the resulting holding gain of \$170,000 ($\$510,000 - \$340,000$) would be reported in net income. However, since the company has chosen to follow the taxes payable method, only the actual amount of taxes due is recorded as an expense which is not impacted by unrealized holding gains. There is no future income tax liability that must be reported even though there is a difference between the tax value and the accounting value of the investment.
 - iv. Equity investment is adjusted to fair value and the future income tax method is used. In this case, the asset would be increased to \$510,000, and the resulting unrealized gain of \$170,000 ($\$510,000 - \$340,000$) would be reported in net income. The tax value of the investment is \$340,000, the accounting value is \$510,000, and therefore there is a temporary difference of \$170,000. At a tax rate of 28%, the future taxes liability account would be increased by \$47,600 ($\$170,000 \times 28\%$). This tax impact would also be reported in net income.

Under IFRS, the company must report the investment at fair value, since the investment does not have contractual cash flows. The company must report this investment as FV through NI since it is held for trading. In this case, the accounting is exactly the same as (iv) above:

In this case, the asset would be increased to \$510,000, and the resulting unrealized gain of \$170,000 ($\$510,000 - \$340,000$) would be reported in net income. The tax value of the investment is \$340,000, the accounting value is \$510,000, and therefore there is a temporary difference of \$170,000. At a tax rate of 28%, the deferred tax liability account would be increased by \$47,600 ($\$170,000 \times 28\%$). This tax impact would also be reported in net income.

WA 18-7

There are many differences between IFRS and ASPE with respect to measurement and reporting for income taxes. Primarily, ASPE has been written to keep recognition and measurement issues simple and therefore requiring less cost and time to calculate and report. This concept is reflected in private enterprises having a choice of using either the taxes payable method or the future income taxes method. The taxes payable method is definitely much simpler since temporary differences do not have to be measured, and only the actual amount of taxes payable needs to be reported as an expense. However, private enterprises can also choose to adopt the future income taxes method, which is similar to the IFRS method. Finally, there are differences in disclosure. Given that private enterprise reports have a limited number of users who are primarily creditors, then disclosure is simplified in comparison to IFRS.

These differences are highlighted below:

- There is a difference in terminology – ASPE has retained terms used in practice in Canada for many years, including: *accounting income* (*accounting profit* under IFRS), *future income taxes* (*deferred taxes* under IFRS), *tax benefit* (*tax income* under IFRS) and *taxable income* (*taxable profit* under IFRS).
- With respect to the accounting for loss carryforwards, ASPE requires an assessment as to whether the loss is “more likely than not” going to result in a benefit. (Again, this results from the practice that has been used in Canada for many years.) IFRS uses the assessment of “probable” i.e., is it probable that the loss carryforwards will result in a benefit. It is generally agreed that the terms have the same meaning and that the losses reported as benefits would be the same under both definitions. One difference is that ASPE allows full recognition of all future income tax assets arising from losses and temporary differences, and then a valuation allowance can be used to adjust these future tax assets to the amount more likely than not to be realized. Under IFRS, there is no valuation allowance that can be recorded, but the company is required to record the probable amount of deferred tax assets to be realized.
- Under IFRS, backward tracing is required for adjustment to deferred taxes where the original transactions were posted directly to equity, either through OCI or retained earnings. This is not required under ASPE. The reason for the difference is due to generally accepted Canadian practice. It is likely that this will eventually change under IFRS, to be similar to the ASPE requirements.

WA 18-7 (Continued)

- Under ASPE, future tax accounts can be classified as current or non-current, based on either the underlying asset or liability, or on the expected time of reversal. Under IFRS, only non-current classification is available. Again, ASPE is based on past practice accepted in Canada, and it is likely that IFRS will eventually adopt this classification with future changes to IAS 12.
- Under ASPE, intraperiod tax allocation is only between discontinued and continued operations and equity items. IFRS would also have income taxes allocated to other comprehensive income items, which are not used under ASPE.
- Finally, the disclosure list is quite extensive under IFRS, and much more limited under ASPE. Generally ASPE only requires disclosure on tax rates (if using the taxes payable method) and loss carry forwards. IFRS requires disclosure to include reconciliations of the deferred tax accounts and the income tax accounts and calculation of rates, just to name a few.

RESEARCH AND FINANCIAL ANALYSIS

RA18-1 STORA ENSO OYJ.

This was taken from the financial statements of Stora Enso Oyj for the year ended December 31, 2011. (All amounts in millions of euros.)

(a)	<u>Balance Sheet: millions of EUR</u>	
	Deferred taxes (non-current asset)	121.9
	Tax receivables (current asset)	6.2
	Deferred taxes (long-term liability)	401.0
	Tax liabilities (current liability)	73.5

Under IFRS, deferred taxes can only be classified as non-current. The deferred tax asset represents the expected amount of the reduction in the amount of the taxes that will be paid in the future when the temporary differences giving rise to future deductible amounts reverse. The deferred tax liability represents the amount of the taxes that are expected to be paid in the future when the temporary differences giving rise to future taxable amounts reverse. The tax liabilities account represents the amount still owing to the government as of December 31, 2011, and the tax receivable account represents overpayment of taxes and still receivable as a refund from the government as of December 31, 2011.

RA18-1 (Continued)(b) (From Note 9)
Deferred tax assets

(in millions of EUR)

Fixed assets	-521.8
Financial Instruments	4.1
Untaxed provisions	-41.0
Pensions and provisions	75.0
Tax losses and tax credits carried forward	196.8
Other deferred tax	<u>7.8</u>
Total	<u>-279.1</u>
Shown on statement of financial positions as:	
Assets	<u>121.9</u>
Liabilities	<u>-401.0</u>

The fixed asset depreciation is included in the deferred tax liabilities account since it is a large **negative** balance. It is common for companies to deduct more tax depreciation than GAAP depreciation, resulting in significant amounts that will be taxable in the future. The pension provisions and **other** provisions along with the tax loss carryforwards are included in deferred tax assets. All of these represent future deductions that might be available to the company to reduce future taxes payable.

RA18-1 (Continued)

(c) In millions of EUR (From Note 9)

		Deferred Tax
Balance Jan 1, 2011		-311.6
Translation Differences		-1.8
Companies acquired/disposals		-3.9
OCI		40.8
Income statement – continuing operations		<u>-2.6</u>
Balance – December 31, 2011		-279.1

The largest adjustments are the OCI adjustment for deferred taxes, and the adjustment for investments.

- (d) As discussed in Note 9, the company has recognized tax benefits related to gross losses carried forward in the amount of EUR 1,846 million. Stora Enso has the following gross losses available for carry forward:

RA18-1 (Continued)

millions of EUR	Expiry date
891	No expiry date
22	2011 – 2016
933	2016 and later
Total 1,846	

- (e) Stora Enso has allocated tax within the period to continuing operations, OCI items, pensions and provisions, financial instruments and equity hedging.
- (f) The actual amount of income taxes paid was EUR129.1million. This was disclosed on the cash flow statement as an operating cash outflow .
- (g) As found in Note 9, the statutory tax rate for Stora Enso was 22.9% in 2011, and 23.3% in 2010. The effective tax rates were: 18.7% in 2011, and 13.1% in 2010. . The major causes of the differences between the statutory and effective tax rates and the amounts are presented below.

	2011	2010
Profit before Tax	420.9	885.3
Tax at statutory rates applicable to profits in the country concerned	-96.4	-206.5
Non-deductible expenses and tax exempt income	15.0	1.3
Valuation of deferred tax assets	-30.4	51.7
Taxes from prior years	9.7	9.3
Changes in tax rates and tax laws	-4.6	-0.1
Profits from equity accounted investments	31.4	23.7
Other	<u>-3.4</u>	<u>4.6</u>
Total Tax	<u>-78.7</u>	<u>-116.0</u>
Effective Tax Rate	<u>18.7%</u>	<u>13.1%</u>
Statutory Tax Rate	<u>22.9%</u>	<u>23.3%</u>

RA18-2 GILDAN ACTIVEWEAR INC.

- (a) The amount of the income tax expense (recovery) for 2012 was a recovery of US\$4,337,000 and for 2011 a recovery of US\$19,223,000. The company used intraperiod tax allocation relating to its OCI items (see Note 16 (d), but the amounts allocated to income taxes on OCI items were small. There are no amounts of income taxes payable for each fiscal year, but there was an amount receivable of US\$353,000 at the end of fiscal 2012 (2011 = US\$515,000). The company reports a change in non-cash working capital balances relating to income taxes receivable for the 2012 and 2011 years of inflow (outflow) US\$2,440,000 and (US\$5,341,000), respectively. This information was found in the operating activities section of the statement of cash flows. Further information is found in note 23 (a).

- (b) The statutory tax rates and effective tax rates for 2012 and 2011 are presented below. There are significant differences between the rates in both years.

	2012	2011
(US\$ in thousands)		
Income taxes at applicable stat rate	\$39,246	\$61,901
Reduction due to different tax rates in foreign subsidiaries	(51,640)	\$(83,276)
Income tax (recovery) charge for prior years' taxation	974	(413)
Effect of non-deductible expenses and other	1,173	(7)
Non-recognition of tax benefits related to tax losses and temp diff	<u>5,910</u>	<u>2,572</u>
Total income tax recovery	<u>(4,337)</u>	<u>(19,223)</u>
Canadian Statutory rate	27.2%	28.8%
Effective Tax Rate (recovery)	(3.0%)	(8.9%)

The Company's applicable statutory rate is the Canadian combined rate applicable in jurisdictions in which the Company operates. The decrease in statutory tax rate is mainly due to the reduction of the Canadian Federal income tax rate applicable to the Company effective Jan 1, 2012 from 16.5% to 15% (Note 20).

The single most significant cause of the effective rate being so much lower than the Canadian statutory rate in each year is the effect of subsidiaries operating in countries with much lower tax rates. It appears that there have been very

RA18-2 (Continued)

significant refunds or other tax benefits that have been recognized in each year in those other countries.

(c) A schedule of the deferred tax balances reported on the 2012 SFP, along with their causes and the related asset or liability with different tax and book values is reported below. Under IFRS all deferred tax balances on the SFP are considered non-current. Under ASPE, it would be based on the classification of the related asset or liability. Where there is no related asset or liability, the classification of the tax balance would be based on when the related temporary difference was expected to reverse.

Amounts in thousands of US\$

Underlying item	Amount	SFP item
<u>Deferred Tax Assets</u>		
Non capital losses	66,386	N/A – for loss carry forwards
Reserves and accruals	27,405	No details given
Other	9,357	No details given
Unrecognized deferred tax assets	(12,053)	
<u>Deferred Tax Liabilities</u>		
Property, plant, and equip	(189)	PP&E and intangible accounts
Intangible assets	<u>(87,535)</u>	PP&E and intangible accounts
Total	3,371	

This net balance has been classified in Non-current assets – US\$ 3,371 thousand. There are no current deferred tax accounts.

(d) Gildan as of Sept 30, 2012 has tax credits, capital and non-capital loss carryforwards and other taxable temporary differences available to reduce future taxable income for tax purposes representing a tax benefit of approximately \$12.1 million, for which no deferred tax asset has been recognized. The tax credits and capital and non-capital loss carryforwards expire between 2019 and 2032. (Note 20)

RA18-3 COMPARATIVE ANALYSIS

- (a) All three companies operate in the retail food industry. Loblaw and Empire operate grocery stores in Canada and Alimentation Couche-Tard (“Alimentation”) operates convenience stores in North America.
- (b) A schedule of the total income tax provision for each company for 2012 (2011 for Loblaw) is presented below.

(millions of \$)	Alimentation	Loblaw	Empire
Total income tax provision	US\$146.3	CDN\$ 215.0	CDN\$122.3

A schedule of the total income tax provision for each company is presented below. All three companies included income tax provisions in current net earnings and other comprehensive income items. Loblaw also had a prior period adjustment which included an income tax adjustment.

(in millions of \$)	Alimentation US\$	Loblaw CAD\$	Empire CAD\$
Total tax provision shown in statement of earnings	146.3	215.0	122.3
Tax provision in other comprehensive income (i)	-6.8	-8.0	-14.0
Total income tax provision	<u>139.5</u>	<u>207.0</u>	<u>108.3</u>

(i) Note – this was totaled from each of the OCI items found either in the notes or on the statement of comprehensive income. For Loblaw view page 84 of Annual Report.

- (c) A schedule of the companies’ deferred income tax assets and liabilities as at the most recent balance sheet date, along with the underlying temporary differences, is presented below. One would expect companies in the same industry to have similar temporary differences and these three companies do have some temporary differences in common. Although the companies use different wording to describe the underlying temporary differences and report in varying degrees of detail, there are some similarities especially with property, plant and equipment and goodwill and intangibles.

RA18-3 (Continued)

(in millions of \$)	Alimentation Couche-Tard US\$	Loblaw CAD\$	Empire CAD\$
Property, plant, and equipment	(255.8)	(311)	(75.3)
Investments			(18.9)
Future employee benefits obligations			38.6
Deferred credits	8.6		
Goodwill and intangibles	(94.8)		(86.4)
Asset retirement obligation	23.3		
Inventories			0.9
Derivative financial liability			0.8
Other	8.9	13	(85.5)
Trade and other payables		65	2.0
Other liabilities		322	6.5
Other assets		(9)	
Loss carry forwards		162	
Revenues taxable next year	(3.9)		
Expenses deductible in next year	66.7		
Unrealized exchange gain	(4.2)		
Tax attributes	3.5		
Current provisions			6.3
Long-term provisions			15.3
Long-term debt/liabilities			42.2
Net deferred tax assets (liabilities)	(247.7)	242	(153.5)

(d) Yes, one would expect the three companies to be subject to similar income tax legislation and tax rates, particularly with respect to federal legislation and rates, since all three are Canadian companies. On review of the schedule below, there are only very small differences between the companies' statutory rates and their effective tax rates.

	Alimentation Couche-Tard	Loblaw	Empire
Statutory rate	27.9%	26.0%	27.6%
Effective rate	24.2%	24.9%	25.8%

RA18-4 INTERNATIONAL COMPARISON

Below, is the schedule of information on statutory and effective income tax rates for five companies operating in the railroad industry, but in different countries.

	Country	Year end	Statutory income tax rate	Effective income tax rate
Deutsche Bahn	Germany	Dec 2011	30.5%	2.0%
East Japan Railway	Japan	Mar 2011	40.5%	40.5%
NSB Group	Norway	Dec 2011	28.0%	28.0%
Canadian National Railway	Canada	Dec 2010	18.0%	26.8%
National Railway Passenger (Amtrak)	United States	Sept 2011	35.0%	0%

From the above, most countries in the list have a similar statutory rate of 30 – 35%, except Japan that has a rate of 40.5% and Canada that has a rate of 18.0%, significantly higher and lower respectively than the others. The effective rate was most different from National Railway (Amtrak) which decreased to 0% due to valuation allowance and substantial losses from current operations for the company.

LEGAL NOTICE

Copyright © 2013 by John Wiley & Sons Canada, Ltd. or related companies. All rights reserved.



The data contained in these files are protected by copyright. This manual is furnished under licence and may be used only in accordance with the terms of such licence.

The material provided herein may not be downloaded, reproduced, stored in a retrieval system, modified, made available on a network, used to create derivative works, or transmitted in any form or by any means, electronic, mechanical, photocopying, recording, scanning, or otherwise without the prior written permission of John Wiley & Sons Canada, Ltd.

(MMXIII iv FI)