

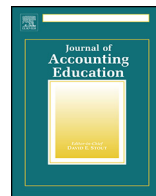


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Teaching and educational notes

Provision for income tax expense ASC 740: A teaching note [☆]



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ABSTRACT

This project requires students to think critically to synthesize concepts they learned in their financial reporting and tax classes. They will use and interpret accounting standards to prepare tax provisions, comparative financial statements and the appropriate footnote disclosures. Even a simple tax provision results in a challenging project.

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1. Introduction

The professional skill set required to create a complex provision for income tax expense (tax provision) requires many companies to retain outside accounting firms to prepare their respective tax provision. Because SEC regulations and auditing standards prohibit accounting firms from auditing their own professional work, a client-company must hire one accounting firm to prepare its tax provision and a different firm to audit its financial statements. The firm performing the audit often finds it necessary to use its tax accountants to assist in auditing the tax provision.

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2. Tax provision exercise

The following exercise for *STUMBLE & FALL, INC.*, is structured to develop the critical thinking skills essential to creating a tax provision. This exercise will require you to:

- Understand concepts from both accounting courses and tax courses,
- Apply your knowledge to prepare journal entries and financial statements,
- Analyze differences between the accounting book values and tax bases,
- Synthesize concepts from accounting and tax to prepare the required disclosures.

We encourage you to work as part of a team for this exercise because teamwork simulates the professional accounting firm experience. For example, one team member could read the sections of Accounting Standards Codification 740 (ASC 740) indicated in Table 1, while another member analyzes the relevant sections of Statement of Financial Accounting Standards No. 109 (SFAS 109), and a third member reads the course textbook. The foregoing approach – each team member's analysis of different authoritative resources on the same topic – will provide different perspectives for your team to approach the tax provision exercise. This team approach will also familiarize team members with the professional literature. Although SFAS 109 pre-existed the Financial Accounting Standard Board's issuance of Accounting Standard Updates (ASU), it is similar to an ASU and illustrates how accounting standards are issued.

Each team can decide how to best allocate the reading among the members. Instead of having different members read ASC 740, SFAS 109 and the textbook, a team may decide to allocate reading based on topics. For instance, one member might focus on the calculation of Deferred Tax Assets and Deferred Tax Liabilities, another might focus on the journal entries and the financial statement presentation, while the third might focus on disclosure requirements.

Table 1
Readings from Accounting Standards Codification and Statement of Financial Accounting Standards.

ASC 740 Income Taxes			SFAS No. 109 (as amended) Accounting for Income Taxes	
				Summary
740-10-05		Overview and Background	1–2	Introduction
740-10-10		Objectives	3–5	Scope
740-10-15		Scope and Scope Exceptions	6–9	Objectives and Basic Principles
740-10-25	1–7	Recognition	10–15	Temporary Differences
740-10-25	18–29	Temporary Differences	16	Recognition and Measurement'
740-10-30	47–45	Changes in Laws or Rates	17–25	Computation of Deferred Tax Liabilities and Assets
740-10-30	1–8	Initial Measurement	26	A Change in the Valuation Allowance
740-10-30	16–25	Establishment of a Valuation Allowance for DTA	27	An Enacted Change in Tax Laws or Rules
740-10-45	1–10	Other Presentation Matters	28–40	omit
740-10-50	1–2	Disclosure	41–42	Financial Statement Presentations
740-10-55	7–9	Recognition of Deferred Tax Assets and Liabilities	43–49	Financial Statement Disclosure
740-10-55	13–14	Pattern of Taxable or Deductible Amounts		
740-10-55	15–19	The Need to Schedule Temporary Difference Reversals	Appendix B	Application of the Standard
740-10-55	22–24	Measurement of Deferred Tax Liabilities and Assets		This may be a useful resource as it provides application guidance
740-10-553	34–37	Recognition of a Tax Benefit for Carrybacks and Carryforwards		

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