Financial Accounting and Reporting
Accounting for Income Taxes

Jeff-Mike Smith V. Sule

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Also refer:
SIC-25 *Income Taxes - Changes in the Tax Status of an Entity or its Shareholders*, IFRIC 23 *Uncertainty over Income Tax Treatments*

Effective Date
Periods beginning on or after 1 January 1998

IAS 12 *Income Taxes*

CURRENT TAX

- Recognise liability for unsettled portion of tax expense
- Recognise an asset to the extent amounts paid exceed amounts due
- Tax loss which can be used against future taxable income can be recognised as an asset (deferred tax asset).

CURRENT TAX MEASUREMENT

Measure the asset/liability using the tax rates that are enacted or substantially enacted at the reporting date.

Disclose current tax expense (income) related to Pillar Two income taxes.

REBUTTABLE PRESUMPTION - FOR INVESTMENT PROPERTY AT FAIR VALUE UNDER IAS 40

Presumption - for investment properties at fair value, deferred tax is calculated assuming the recovery of the carrying amount of the investment property, will ultimately be entirely through sale - regardless of whether this is actually managements intention or not.

Presumption is rebutted and the carrying amount will ultimately be recovered through use over the life of the asset rather than sale:

If the asset is depreciable; and

The asset is held in order to consume the assets benefits over the life of the asset.

Land - land is not depreciable and therefore the recovery of land is always through sale.

DEFINITIONS - TEMPORARY DIFFERENCE AND TAX BASE

Temporary difference: Difference between the carrying amount of an asset/liability and its tax base.

Tax base of an asset	Tax base of a liability	Tax base of income received in advance
• Is the amount that will be deductible for tax purposes against any taxable economic benefits that will flow to the entity when it recovers the carrying amount of the asset • If those economic benefits will not be taxable, the tax base of the asset is equal to its carrying amount.	Is its carrying amount Less any amount that will be deductible for tax purposes in respect of the liability in future periods.	• Is its carrying amount • Less any revenue that will not be taxable in the future.

TEMPORARY DIFFERENCES

Taxable temporary differences will result in taxable amounts in future when the carrying amount of an asset is recovered or liability is settled.

Deductible temporary differences will result in deductible amounts in future when the carrying amount of an asset is recovered or a liability is settled.

DEFERRED TAX

Deferred tax liabilities

Recognise liabilities for all taxable temporary differences, except to the extent it arises from:

- Initial recognition of goodwill; or
- Initial recognition of an asset/liability that does not affect accounting or taxable profit, the transaction is not a business combination and at the time of the transaction, does not give rise to equal taxable and deductible temporary differences.
- Liabilities from undistributed profits from investments in subsidiaries, branches and associates, and interests in joint ventures where company can control the timing of the reversal.

Deferred tax assets

Recognise for deductible temporary differences, unused tax losses, unused tax credits to the extent that taxable profit will be available against which the asset can be used, except to the extent it arises from the initial recognition of an asset/liability that:

- Is not a business combination;
- does not affect accounting/taxable profit; and
- does not give rise to equal taxable and deductible temporary differences.

Recognise for deductible temporary differences arising from investments in subsidiaries and associates to the extent it is probable the temporary difference will reverse in the foreseeable future and there will be available tax profit to be utilised.

A deferred tax asset is recognised for the carry forward of unused tax losses and unused tax credits to the extent that it is probable that future taxable profits will be available (i.e. the entity has sufficient taxable temporary differences or there is convincing other evidence that sufficient taxable profits will be available against which the unused tax losses or unused tax credits can be utilised).

Disclose that the entity has applied the exception to recognising and disclosing information about deferred tax assets and liabilities related to Pillar Two income taxes.

DEFERRED TAX - MEASUREMENT

- Measure the balance at tax rates that are expected to apply in the period in which the asset is realised or liability settled based on tax rates that have been enacted or substantively enacted by the end of the reporting period
- Deferred tax assets and liabilities are not discounted
- The applicable tax rate depends on how the carrying amount of an asset or liability is recovered or settled
- Current and deferred tax shall be recognised as income or an expense and included in profit or loss for the period, except to the extent that the tax arises from a transaction or event which is recognised, in the same or a different period, directly in equity or other comprehensive income, or a business combination
- Current tax and deferred tax are charged or credited directly to equity or other comprehensive income if the tax relates to items that are credited or charged, in the same or a different period, directly to equity or other comprehensive income.

Effective Date
Periods beginning on or after 1 July 2000

SIC-25 *Income Taxes: Changes in the Tax Status of an Entity or its Shareholders*

ISSUE

- The issue is how an entity accounts for the tax consequences of a change in its tax status or that of its shareholders
- A change in the tax status of an entity or of its shareholders may have consequences for an entity by increasing or decreasing its tax liabilities or assets. This may, for example, occur upon the public listing of an entity's equity instruments or upon the restructuring of an entity's equity. It may also occur upon a controlling shareholder's move to a foreign country. As a result of such an event, an entity may be taxed differently; it may for example gain or lose tax incentives or become subject to a different rate of tax in the future
- A change in the tax status of an entity or its shareholders may have an immediate effect on the entity's current tax liabilities or assets. The change may also increase or decrease the deferred tax liabilities and assets recognised by the entity, depending on the effect the change in tax status has on the tax consequences that will arise from recovering or settling the carrying amount of the entity's assets and liabilities.

CONSENSUS

- A change in the tax status of an entity or its shareholders does not give rise to increases or decreases in amounts recognised outside profit or loss
- The current and deferred tax consequences of a change in tax status are included in net profit or loss for the period, unless those consequences relate to transactions and events that result, in the same or a different period, in a direct credit or charge to the recognised amount of equity or in amounts recognised in other comprehensive income
- Those tax consequences that relate to changes in the recognised amount of equity, in the same or a different period (not included in net profit or loss), are charged or credited directly to equity
- Those tax consequences that relate to amounts recognised in other comprehensive income are recognised in other comprehensive income.

Effective Date
Periods beginning on or after 1 January 2019
(earlier application permitted)

IFRIC 23 *Uncertainty over Income Tax Treatments*

MEASUREMENT

IFRIC 23 addresses the following issues:

- Whether an entity should consider uncertain tax treatments separately;
- The assumptions an entity should make about the examination of tax treatments by taxation authorities;
- How an entity determines taxable profit or loss, tax bases, unused tax losses, unused tax credits and tax rates; and
- How an entity considers changes in facts and circumstances

SCOPE

IFRIC 23 clarifies how to apply the recognition and measurement requirements in IAS 12 Income Taxes when there is uncertainty over income tax treatments.

DEFINITIONS

- 'Tax treatments' refers to the treatments used by an entity that it plans to use in its income tax filings
- 'Taxation authority' refers to the body or bodies that decide whether tax treatments are acceptable under tax law. This might include a court
- An 'uncertain tax treatment is a tax treatment for which there is uncertainty over whether the relevant taxation authority will accept the tax treatment under tax law

CONSENSUS

1.UNIT OF ACCOUNT

IFRIC 23 requires an entity to treat uncertain tax treatments separately or together depending on which method better predicts the resolution of the uncertainty.

2.EXAMINATION BY TAX AUTHORITIES

When measuring current and deferred income tax assets and liabilities IFRIC 23 requires an entity to assume that a taxation authority will examine amounts that it has a right to examine and have full knowledge of all related information when making those examinations.

3.DETERMINATION OF TAX ITEMS

IFRIC 23 requires an entity to make an assessment of whether it is probable a taxation authority will accept an uncertain tax treatment. If it is probable the treatment will be accepted then taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rate should be consistent with the treatment used or planned to be used in its income tax filings. If it is not probable the position will be accepted, then an entity reflects that uncertainty in one of two ways depending on which method better predicts the resolution of the uncertainty:

- An expected value approach; or
- The most likely approach

4.CHANGES IN FACTS AND CIRCUMSTANCES

The accounting for uncertain tax treatments requires an entity to make estimates and judgements about whether the relevant taxation authority will accept the position taken by the entity in its tax filings. IFRIC 23 requires those estimates and judgements to be reassessed if the facts and circumstances on which those estimates and judgements are based change, or as a result of new information that affects the estimates and judgements. The effects of such changes should be reflected by applying IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors and treated as a change in accounting estimate. In addition IAS 10 Events after the Reporting Date should be applied to determine whether such a change that occurs after the reporting period is an adjusting or non-adjusting event.

EXAMPLES

In applying consensus 3:

- Assume an entity has claimed deductions in its taxation filing related to transfer pricing and concluded it is not probable the taxation authority will accept the deductions claimed. If the entity expects the taxations authority's decision on one transfer pricing matter would affect, or be affected by, the other transfer pricing matters, then it would calculate a probability-weighted average of the possible outcomes arising from an investigation by the tax authorities in measuring income tax assets and liabilities (i.e. an expected value approach).
- Assume an entity may has claimed a current tax deduction of 100% of the cost of an intangible asset, but expects the taxation authority to accept only a 10% deduction in each of the next 10 years, the entity would measures its current tax position in the year of purchase based on a current tax deduction equal to only 10% of cost and its deferred tax position would assume a tax base of the asset equal to 90% of cost and not 0% (i.e. the most likely approach).

DISCLOSURE

- Judgements made in determining taxable profit or loss (paragraph 122 of IAS 1 Presentation of Financial Statements;
- Information about the assumptions and estimates made (paragraphs 125-129 of IAS 1)
- Potential effect of an uncertainty tax treatment as a tax-related contingency (paragraph 88 of IAS 12)

TRANSITION

An entity may use either

- retrospectively by restating comparatives if possible without hind sight; or
- retrospectively with the cumulative effect recognised by adjusting the opening balance of retained earnings on the date of initial application (i.e. the start of the accounting period in which IFRIC 23 is fist applied). In this case comparatives would not be restated.

STRAIGHT PROBLEMS

1. a. A machine cost 100. For tax purposes, depreciation of 30 has already been deducted in the current and prior periods and the remaining cost will be deductible in future periods, either as depreciation or through a deduction on disposal. Revenue generated by using the machine is taxable, any gain on disposal of the machine will be taxable and any loss on disposal will be deductible for tax purposes. *The tax base of the machine is 70.*

   b. Interest receivable has a carrying amount of 100. The related interest revenue will be taxed on a cash basis. *The tax base of the interest receivable is nil.*

   c. Trade receivables have a carrying amount of 100. The related revenue has already been included in taxable profit (tax loss). *The tax base of the trade receivables is 100.*

   d. Dividends receivable from a subsidiary have a carrying amount of 100. The dividends are not taxable. *In substance, the entire carrying amount of the asset is deductible against the economic benefits. Consequently, the tax base of the dividends receivable is 100. Under this analysis, there is no taxable temporary difference. An alternative analysis is that the accrued dividends receivable have a tax base of nil and that a tax rate of nil is applied to the resulting taxable temporary difference of 100. Under both analyses, there is no deferred tax liability.*

   e. A loan receivable has a carrying amount of 100. The repayment of the loan will have no tax consequences. *The tax base of the loan is 100.*

2. a. Current liabilities include accrued expenses with a carrying amount of 100. The related expense will be deducted for tax purposes on a cash basis. *The tax base of the accrued expenses is nil.*

   b. Current liabilities include interest revenue received in advance, with a carrying amount of 100. The related interest revenue was taxed on a cash basis. *The tax base of the interest received in advance is nil.*

   c. Current liabilities include accrued expenses with a carrying amount of 100. The related expense has already been deducted for tax purposes. *The tax base of the accrued expenses is 100.*

   d. Current liabilities include accrued fines and penalties with a carrying amount of 100. Fines and penalties are not deductible for tax purposes. *The tax base of the accrued fines and penalties is 100. Under this analysis, there is no deductible temporary difference. An alternative analysis is that the accrued fines and penalties payable have a tax base of nil and that a tax rate of nil is applied to the resulting deductible temporary difference of nil. Under both analyses, there is no deferred tax asset.*

   e. A loan payable has a carrying amount of 100. The repayment of the loan will have no tax consequences. *The tax base of the loan is 100.*

3. An asset which cost 150 has a carrying amount of 100. Cumulative depreciation for tax purposes is 90 and the tax rate is 25%.

   The tax base of the asset is 60 (cost of 150 less cumulative tax depreciation of 90). To recover the carrying amount of 100, the entity must earn taxable income of 100, but will only be able to deduct tax depreciation of 60. Consequently, the entity will pay income taxes of 10 (40 at 25%) when it recovers the carrying amount of the asset. The difference between the carrying amount of 100 and the tax base of 60 is a taxable temporary difference of 40. Therefore, the entity recognizes a deferred tax liability of 10 (40 at 25%) representing the income taxes that it will pay when it recovers the carrying amount of the asset.

4. An entity intends to use an asset which cost 1,000 throughout its useful life of five years and then dispose of it for a residual value of nil. The tax rate is 40%. Depreciation of the asset is not deductible for tax purposes. On disposal, any capital gain would not be taxable and any capital loss would not be deductible.

   As it recovers the carrying amount of the asset, the entity will earn taxable income of 1,000 and pay tax of 400. The entity does not recognize the resulting deferred tax liability of 400 because it results from the initial recognition of the asset.

   In the following year, the carrying amount of the asset is 800. In earning taxable income of 800, the entity will pay tax of 320. The entity does not recognize the deferred tax liability of 320 because it results from the initial recognition of the asset.

5. An entity recognizes a liability of 100 for accrued product warranty costs. For tax purposes, the product warranty costs will not be deductible until the entity pays claims. The tax rate is 25%.

   The tax base of the liability is nil (carrying amount of 100, less the amount that will be deductible for tax purposes in respect of that liability in future periods). In settling the liability for its carrying amount, the entity will reduce its future taxable profit by an amount of 100 and, consequently, reduce its future tax payments by 25 (100 at 25%). The difference between the carrying amount of 100 and the tax base of nil is a deductible temporary difference of 100. Therefore, the entity recognizes a deferred tax asset of 25 (100 at 25%), provided that it is probable that the entity will earn sufficient taxable profit in future periods to benefit from a reduction in tax payments.

6. Identification of a deductible temporary difference at the end of Year 2:

   Entity A purchases for P1,000, at the beginning of Year 1, a debt instrument with a nominal value of P1,000 payable on maturity in 5 years with an interest rate of 2% payable at the end of each year. The effective interest rate is 2%. The debt instrument is measured at fair value.

   At the end of Year 2, the fair value of the debt instrument has decreased to P918 as a result of an increase in market interest rates to 5%. It is probable that Entity A will collect all the contractual cash flows if it continues to hold the debt instrument.

   Any gains (losses) on the debt instrument are taxable (deductible) only when realized. The gains (losses) arising on the sale or maturity of the debt instrument are calculated for tax purposes as the difference between the amount collected and the original cost of the debt instrument.

   Accordingly, the tax base of the debt instrument is its original cost.

   The difference between the carrying amount of the debt instrument in Entity A's statement of financial position of P918 and its tax base of P1,000 gives rise to a deductible temporary difference of P82 at the end of Year 2, irrespective of whether Entity A expects to recover the carrying amount of the debt instrument by sale or by use, ie by holding it and collecting contractual cash flows, or a combination of both.

This is because deductible temporary differences are differences between the carrying amount of an asset or liability in the statement of financial position and its tax base that will result in amounts that are deductible in determining taxable profit (tax loss) of future periods, when the carrying amount of the asset or liability is recovered or settled. Entity A obtains a deduction equivalent to the tax base of the asset of P1,000 in determining taxable profit (tax loss) either on sale or on maturity.

7. a. An item of property, plant and equipment has a carrying amount of 100 and a tax base of 60. A tax rate of 20% would apply if the item were sold and a tax rate of 30% would apply to other income.

   The entity recognizes a deferred tax liability of 8 (40 at 20%) if it expects to sell the item without further use and a deferred tax liability of 12 (40 at 30%) if it expects to retain the item and recover its carrying amount through use.

   b. An item or property, plant and equipment with a cost of 100 and a carrying amount of 80 is revalued to 150. No equivalent adjustment is made for tax purposes. Cumulative depreciation for tax purposes is 30 and the tax rate is 30%. If the item is sold for more than cost, the cumulative tax depreciation of 30 will be included in taxable income but sale proceeds in excess of cost will not be taxable.

   The tax base of the item is 70 and there is a taxable temporary difference of 80. If the entity expects to recover the carrying amount by using the item, it must generate taxable income of 150, but will only be able to deduct depreciation of 70. On this basis, there is a deferred tax liability of 24 (80 at 30%). If the entity expects to recover the carrying amount by selling the item immediately for proceeds of 150, the deferred tax liability is computed as follows:

	Taxable Temporary Difference	*Tax Rate*	*Deferred Tax Liability*
Cumulative tax depreciation	*30*	*30%*	*9*
Proceeds in excess of cost	*50*	*nil*	*–*
Total	*80*		*9*

   (note: in accordance with PAS12, the additional deferred tax that arises on the revaluation is recognized in other comprehensive income)

   c. The facts are as in **B**, except that if the item is sold for more than cost, the cumulative tax depreciation will be included in taxable income (taxed at 30%) and the sale proceeds will be taxed at 40%, after deducting an inflation-adjusted cost of 110.

   *If the entity expects to recover the carrying amount by using the item, it must generate taxable income of 150, but will only be able to deduct depreciation of 70. On this basis, the tax base is 70, there is a taxable temporary difference of 80 and there is a deferred tax liability of 24 (80 at 30%), as in **B**.*

   If the entity expects to recover the carrying amount by selling the item immediately for proceeds of 150, the entity will be able to deduct the indexed cost of 110. The net proceeds of 40 will be taxed at 40%. In addition, the cumulative tax depreciation of 30 will be included in taxable income and taxed at 30%. On this basis, the tax base is 80 (110 less 30), there is a taxable temporary difference of 70 and there is a deferred tax liability of 25 (40 at 40% plus 30 at 30%). If the tax base is not immediately apparent in this example, it may be helpful to consider the fundamental principle set out in PAS12.

   (note: in accordance with PAS12, the additional deferred tax that arises on the revaluation is recognized in other comprehensive income)

8. An investment property has a cost of 100 and fair value of 150. It is measured using the fair value model in PAS 40. It comprises land with a cost of 40 and fair value of 60 and a building with a cost of 60 and fair value of 90. The land has an unlimited useful life.

   Cumulative depreciation of the building for tax purposes is 30. Unrealized changes in the fair value of the investment property do not affect taxable profit. If the investment property is sold for more than cost, the reversal of the cumulative tax depreciation of 30 will be included in taxable profit and taxed at an ordinary tax rate of 30%. For sales proceeds in excess of cost, tax law specifies tax rates of 25% for assets held for less than two years and 20% for assets held for two years or more.

   Because the investment property is measured using the fair value model in PAS 40, there is a rebuttable presumption that the entity will recover the carrying amount of the investment property entirely through sale. If that presumption is not rebutted, the deferred tax reflects the tax consequences of recovering the carrying amount entirely through sale, even if the entity expects to earn rental income from the property before sale.

   The tax base of the land if it is sold is 40 and there is a taxable temporary difference of 20 (60 – 40). The tax base of the building if it is sold is 30 (60 – 30) and there is a taxable temporary difference of 60 (90 – 30). As a result, the total taxable temporary difference relating to the investment property is 80 (20 + 60).

   In accordance with PAS 12, the tax rate is the rate expected to apply to the period when the investment property is realized. Thus, the resulting deferred tax liability is computed as follows, if the entity expects to sell the property after holding it for more than two years:

	Taxable Temporary Difference	*Tax Rate*	*Deferred Tax Liability*
Cumulative tax depreciation	*30*	*30%*	*9*
Proceeds in excess of cost	*50*	*20%*	*10*
Total	*80*		*19*

   If the entity expects to sell the property after holding it for less than two years, the above computation would be amended to apply a tax rate of 25%, rather than 20%, to the proceeds in excess of cost.

   If, instead, the entity holds the building within a business model whose objective is to consume substantially all of the economic benefits embodied in the building over time, rather than through sale, this presumption would be rebutted for the building. However, the land is not depreciable. Therefore the presumption of recovery through sale would not be rebutted for the land. It follows that the deferred tax liability would reflect the tax consequences of recovering the carrying amount of the building through use and the carrying amount of the land through sale.

   The tax base of the building if it is used is 30 (60 – 30) and there is a taxable temporary difference of 60 (90 – 30), resulting in a deferred tax liability of 18 (60 at 30%).

The tax base of the land if it is sold is 40 and there is a taxable temporary difference of 20 (60 – 40), resulting in a deferred tax liability of 4 (20 at 20%).

As a result, if the presumption of recovery through sale is rebutted for the building, the deferred tax liability relating to the investment property is 22 (18 + 4).

9. Measurement of current and deferred tax assets and liabilities for an entity in a jurisdiction where income taxes are payable at a higher rate on undistributed profits (50%) with an amount being refundable when profits are distributed. The tax rate on distributed profits is 35%. At the end of the reporting period, 31 December 2022, the entity does not recognize a liability for dividends proposed or declared after the reporting period. As a result, no dividends are recognized in the year 2022. Taxable income for 2022 is 100,000. The net taxable temporary difference for the year 2022 is 40,000.

   The entity recognizes a current tax liability and a current income tax expense of 50,000. No asset is recognized for the amount potentially recoverable as a result of future dividends. The entity also recognizes a deferred tax liability and deferred tax expense of 20,000 (40,000 at 50%) representing the income taxes that the entity will pay when it recovers or settles the carrying amounts of its assets and liabilities based on the tax rate applicable to undistributed profits.

   Subsequently, on 15 March 2023 the entity recognizes dividends of 10,000 from previous operating profits as a liability.

   On 15 March 2023, the entity recognizes the recovery of income taxes of 1,500 (15% of the dividends recognized as a liability) as a current tax asset and as a reduction of current income tax expense for 2023.

10. In 2022, an entity has accounting profit in its own jurisdiction (country A) of 1,500 (2021: 2,000) and in country B of 1,500 (2021: 500). The tax rate is 30% in country A and 20% in country B. In country A, expenses of 100 (2021: 200) are not deductible for tax purposes.

    The following is an example of a reconciliation to the domestic tax rate.

	2021	*2022*
Accounting Profit		
2,000 (A) + 500 (B)	*2,500*	
1,500 (A) + 1,500 (B)		*3,000*
Tax at the domestic rate of 30%	*750*	*900*
Tax effect of expenses that are not deductible for tax purposes	*60*	*30*
Effect of lower tax rates in country B	*(50)*	*(150)*
Tax expense	*760*	*780*

The following is an example of a reconciliation prepared by aggregating separate reconciliations for each national jurisdiction. Under this method, the effect of differences between the reporting entity's own domestic tax rate and the domestic tax rate in other jurisdictions does not appear as a separate item in the reconciliation. An entity may need to discuss the effect of significant changes in either tax rates, or the mix of profits earned in different jurisdictions, in order to explain changes in the applicable tax rate(s), as required by PAS 12.

Accounting Profit	*2,500*	*3,000*
Tax at the domestic rates applicable to profits in the country concerned	*700*	*750*
Tax effect of expenses that are not deductible for tax purposes	*60*	*30*
Tax expense	*760*	*780*

MULTIPLE CHOICE –Theory

1. Which of the following statements is correct regarding the provisions for income taxes in the financial statements of a sole proprietorship?
   a. The provision for income taxes should be based on business income using individual tax rates.
   b. The provisions for income taxes should be based on business income using corporate tax rates.
   c. The provision for income taxes should be based on the proprietor's total taxable income.
   d. No provision for income taxes is required.

2. The purpose of an interperiod income tax allocation is to
   a. allow reporting entities to fully utilize tax losses carried forward from a previous year.
   b. allow reporting entities whose tax liabilities vary significantly from year to year to smooth payments to taxing agencies.
   c. recognize an asset or liability for the tax consequences of temporary difference that exist at the balance sheet date.
   d. amortize the deferred tax liability shown on the balance sheet

3. Which is not subject to the application of intraperiod income tax allocation?
   a. Discontinued operations c. Prior period errors
   b. Income from continuing operations d. Operating income

4. When accounting for income taxes, a temporary difference occurs when
   a. An item is included in the calculation of net income in one year and taxable income in a different year.
   b. An item is included in the calculation of net income but is neither taxable nor deductible.
   c. The accrual method of accounting is used.
   d. An item is no longer taxable due to a change in the tax law.

5. When temporary difference will result in taxable amounts in future years
   a. A deferred tax liability is recognized in the current year.
   b. A deferred tax asset is recognized in the current year.
   c. A deferred tax asset may be recognized in the current year if certain conditions are met.
   d. A deferred tax liability may be recognized in the current year if certain conditions are met.

6. Which is correct about the presentation of deferred tax assets and liabilities?
   a. Current deferred tax assets are netted against current deferred tax liabilities
   b. All noncurrent deferred tax assets are netted against noncurrent deferred tax liabilities
   c. Deferred tax assets are never netted against deferred tax liabilities
   d. Deferred tax assets are netted against deferred tax liabilities if they relate to the same taxing authority.

7. Which of the following is true regarding reporting deferred taxes in financial statements prepared in accordance with IFRS?
   a. Deferred tax assets and liabilities are classified as current and noncurrent based on expiration date.
   b. Deferred tax assets and liabilities may only be classified as noncurrent.
   c. Deferred tax assets are always netted against deferred tax liabilities.
   d. Deferred taxes of one jurisdiction are offset against another jurisdiction in the netting process.

8. At the most recent year-end, a noncurrent deferred income tax asset exceeded a current deferred income tax liability. Which of the following should be reported at the most recent year-end?
   a. The excess of the deferred tax asset over the deferred tax liability as a current asset.
   b. The excess of the deferred tax asset over the deferred tax liability as a noncurrent asset
   c. The deferred tax asset as a noncurrent asset
   d. The deferred income tax asset as a current asset.

9. Unless a company has a legal right of set-off, PAS 12 Income Taxes, requires disclosure of all of the following information for deferred tax balance sheet items:
   i. The amount of deferred tax assets recognized.
   ii. The amount of the deferred tax liabilities recognized.
   iii. The net amount of the deferred tax assets and liabilities recognized.
   iv. The amount of the deferred tax asset relating to tax losses
   a. I, II and IV only c. III and IV only
   b. I, II and III only d. IV only

10. All of the following can result in a temporary difference between pretax financial income and taxable income except for
    a. Impairment loss on goodwill c. Contingent liabilities
    b. Depreciation expense d. Product warranty costs

MULTIPLE CHOICE – Problems

PROBLEM 1

The following differences between financial and taxable income were reported by Dider, for the current year, 2023:

(a) Excess of tax depreciation over book depreciation P60,000
(b) Interest revenue on municipal bonds 9,000
(c) Excess of estimated warranty expense over actual expenditures 54,000
(d) Unearned rent received 12,000
(e) Fines paid 30,000
(f) Prepaid expenses.. 45,000
(g) Interest on indebtedness incurred to purchase tax-exempt securities... 3,000
(h) Unrealized losses on marketable securities recognized for financial reporting 18,000

Assume that Dider Corporation had pretax accounting income [before considering items (a) through (h)] of P900,000 for the current year.

The temporary differences of items a to d are expected to reverse by the end of 2024 while the temporary differences relating to items e to h are expected to be reversed by the end of 2025.

The enacted tax rates are: 2023 - 35%, 2024 - 40% and 2025 - 32%.

1. How much is the taxable income for 2023?
   a. 903,000 b. 924,000 c. 945,000 d. 1,023,000

2. How much is the total income tax expense for 2023?
   a. 316,050 b. 328,050 c. 323,400 d. 322,290

PROBLEM 2

The following differences enter into the reconciliation of accounting profit and taxable profit of Mulanay Company for the year ended December 31, 2023, its first year of operations

Life insurance expense	P100,000
Excess tax depreciation	2,000,000
Warranty Expense	200,000
Litigation accrual	500,000
Unamortized computer software	3,000,000
Unearned rent income deferred on the books but appropriately recognized in taxable profit	400,000
Interest income from long-term certificate of deposit	200,000

Additional information:

a. On July 1, 2023, Mulanay paid insurance premium of P200,000 on the life of an officer with Mulanay Company as beneficiary.

b. Excess tax depreciation will reverse equally over a four-year period, 2024-2027.

c. The warranty liability is the estimated warranty cost that was recognized as expense in 2023 but deductible for tax purposes when actually paid.

d. It is estimated that the litigation liability will be paid in 2027.

e. In January 2023, Mulanay Company incurred P4,000,000 of computer software cost. Considering the technical feasibility of the project, this cost was capitalized and amortized over 4 years for accounting purposes. However, the total amount was expensed in 2023 for tax purposes.

f. Rent income will be recognized during the last year of the lease, 2027.

g. Interest income from the long-term certificate of deposit is expected to be P200,000 each year until their maturity at the end of 2024.

h. Accounting profit for 2023 is P10,000,000. Tax rate is 35%.

3. Deferred tax liability
   a. 1,050,000 b. 2,100,000 c. 1,750,000 d. 1,890,000

4. Deferred tax asset
   a. 385,000 b. 245,000 c. 210,000 d. 1,085,000

5. Current tax expense
   a. 2,100,000 b. 2,800,000 c. 1,750,000 d. 1,820,000

6. Tax expense
   a. 3,535,000 b. 3,465,000 c. 3,500,000 d. 4,830,000