

Question #1 of 52

Question ID: 1590335

Graphics, Inc. has a deferred tax asset of \$4,000,000 on its books. As of December 31, it became more likely than not that \$2,000,000 of the asset's value may never be realized because of the uncertainty of future income. Graphics, Inc. should:

- A) reduce the asset by establishing a valuation allowance of \$2,000,000 against the asset.
 - B) reverse the asset account permanently by \$2,000,000.
 - C) not make any adjustments until it is certain that the tax benefits will not be realized.
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Question #2 of 52

Question ID: 1590324

Which of the following statements about deferred taxes is *most accurate*? Deferred tax liabilities:

- A) arise primarily due to differences between financial and tax accounting.
 - B) can relate to either permanent or temporary differences.
 - C) should be treated as debt when calculating financial statement ratios.
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Question #3 of 52

Question ID: 1590314

A dance club purchases new sound equipment for \$25,352. It will work for 5 years and has no salvage value. For financial reporting, the straight-line depreciation method is used, but for tax purposes depreciation is 35% of original cost in Years 1 and 2 and the remaining 30% in Year 3. Annual revenues are constant at \$14,384 over these five years. A change in the tax law was enacted in Year 3, reducing the tax rate from 41% to 31% for Years 4 and 5. What is the deferred tax liability as of the end of Year 3?

- A) \$3,144.

B) \$1,039.

C) \$2,948.

Question #4 of 52

Question ID: 1590328

Which of the following factors is *least likely* to cause a difference between a firm's effective tax rate and statutory rate?

A) Non-deductible expenses.

B) Deductible expenses.

C) Tax credits.

Question #5 of 52

Question ID: 1590312

Nespa, Inc., has a deferred tax liability on its balance sheet in the amount of \$25 million. A change in tax laws has increased future tax rates for Nespa. The impact of this increase in tax rate will be:

A) a decrease in deferred tax liability and an increase in tax expense.

B) a decrease in deferred tax liability and a decrease in tax expense.

C) an increase in deferred tax liability and an increase in tax expense.

Question #6 of 52

Question ID: 1590284

Hewie, Inc. purchased equipment for \$300,000. On its financial statements, Hewie depreciates the equipment over six years using the straight-line method with no residual value. For tax purposes, Hewie uses double-declining balance depreciation over five years. What is the tax base of the asset at the end of Year 1?

A) \$250,000.

B) \$180,000.

C) \$120,000.

Question #7 of 52

Question ID: 1590321

Firm 1 has a deferred tax liability and Firm 2 has a deferred tax asset. If the tax rate decreases, the balance sheet values of these deferred tax items will:

- | <u>Firm 1</u> | <u>Firm 2</u> |
|---------------|---------------|
| A) decrease. | decrease. |
| B) increase. | decrease. |
| C) increase. | increase. |
-

Question #8 of 52

Question ID: 1590322

A firm has deferred tax assets of \$315,000 and deferred tax liabilities of \$190,000. If the tax rate increases, adjusting the value of the firm's deferred tax items will:

- A) decrease income tax expense.
 - B) have no effect on income tax expense.
 - C) increase income tax expense.
-

Question #9 of 52

Question ID: 1590330

Deferred tax items should be measured based on the:

- A) firm's effective tax rate at the time when the temporary difference reverses.
- B) statutory tax rate at the time when the temporary difference is recognized.
- C) tax rate that will apply when the temporary difference reverses.

Question #10 of 52

Question ID: 1590289

Alter Inc. determines that it has \$35,000 of accounts receivable outstanding at the end of 20X8. Based on past experience, it recognizes an provision for doubtful debt equal to 10% of its credit sales outstanding. For tax purposes, the doubtful debts cannot be deducted until written off. The tax base of Alter's accounts receivable at the end of 20X8 is *closest* to:

- A) \$3,500.
 - B) \$31,500.
 - C) \$35,000.
-

Question #11 of 52

Question ID: 1590315

A firm needs to adjust its financial statements for a change in the tax rate. Taxable income is \$80,000 and pretax income is \$120,000. The current tax rate is 50%, and the new tax rate is 40%. The effect on taxes payable of adjusting the tax rate is *closest* to:

- A) \$4,000.
 - B) \$8,000.
 - C) \$16,000.
-

Question #12 of 52

Question ID: 1590316

A health care company purchased a new MRI machine on 1/1/X3. At year-end the company recorded straight-line depreciation expense of \$75,000 for book purposes and accelerated depreciation expense of \$94,000 for tax purposes. Management estimates warranty expense related to corrective eye surgeries performed in 20X3 to be \$250,000. Actual warranty expenses of \$100,000 were incurred in 20X3 related to surgeries performed in 20X2. The company's tax rate for the current year was 35%, but a tax rate of 37% has been enacted into law and will apply in future periods. Assuming these are the only relevant entries for deferred taxes, the company's recorded changes in deferred tax assets and liabilities on 12/31/X3 are *closest to*:

	<u>DTA</u>	<u>DTL</u>
A)	\$55,500	\$7,030
B)	\$55,500	\$6,650
C)	\$52,500	\$6,650

Question #13 of 52

Question ID: 1590313

An analyst has gathered the following tax information:

	Year 1	Year 2
Pretax Income	\$60,000	\$60,000
Taxable Income	\$50,000	\$65,000

Assume all the differences between pretax income and taxable income are expected to reverse in the future.

The current tax rate is 40%. The tax rate is reduced to 30% and the change is enacted at the beginning of Year 2.

In year 1, what are the taxes payable and what is the deferred tax liability (DTL)?

	<u>Taxes payable</u>	<u>DTL</u>
A)	\$24,000	\$1,500

B) \$20,000 \$1,500

C) \$20,000 \$3,000

Question #14 of 52

Question ID: 1590331

In the context of deferred tax items, what is the impact on net income of an increase in the valuation allowance?

- A)** Decrease net income.
 - B)** No effect on net income.
 - C)** Increase net income.
-

Question #15 of 52

Question ID: 1590311

A company purchases a new pizza oven for \$12,675. It will work for 5 years and have no salvage value. The company will depreciate the oven over 5 years using the straight-line method for financial reporting, and over 3 years for tax reporting. If the tax rate for years 4 and 5 changes from 41% to 31%, the deferred tax liability as of the end of year 3 is *closest* to:

- A)** \$1,570.
 - B)** \$2,080.
 - C)** \$1,040.
-

Question #16 of 52

Question ID: 1590327

Deferred tax liabilities may result from:

- A)** pretax income greater than taxable income due to permanent differences.
- B)** pretax income greater than taxable income due to temporary differences.

C) pretax income less than taxable income due to temporary differences.

Question #17 of 52

Question ID: 1590320

Habel Inc. owns equipment with a tax base of \$400,000 and a carrying value of \$600,000. Habel also has a tax loss carryforward of \$200,000 that is expected to be utilized in the foreseeable future. Deferred tax items on the balance sheet are based on a tax rate of 30%. Based only on this information, an increase in future tax rates to 35% will cause Habel's total equity to:

- A) decrease.
 - B) remain unchanged.
 - C) increase.
-

Question #18 of 52

Question ID: 1590303

An analyst gathered the following information about a company:

- Taxable income = \$100,000.
- Pretax income = \$120,000.
- Current tax rate = 20%.

Assuming the difference between taxable income and pretax income will reverse in the future, the effect these events on the company's financial statements will be to report income tax expense of:

- A) \$24,000 and an addition to deferred tax liabilities of \$4,000.
 - B) \$24,000 and a decrease in deferred tax assets of \$4,000.
 - C) \$22,000 with no change in deferred tax items.
-

Question #19 of 52

Question ID: 1590300

Year ending

31

2002

2003

2004

December:

Income Statement:

Revenues

after all

expenses

\$200

\$300

\$400

other than

depreciation

Depreciation

50

50

50

expense

Income

before

\$150

\$250

\$350

income

taxes

Tax return:

Taxable

income

before

\$200

\$300

\$400

depreciation

expense

Depreciation

75

50

25

expense

Taxable

income

\$125

\$250

\$375

Assume an income tax rate of 40% and zero deferred tax liability on 31 December 2001.

The deferred tax liability to be shown in the 31 December 2003, balance sheet and the 31 December 2004 balance sheet, is:

2003

2004

- A) \$0 \$10
- B) \$10 \$0
- C) \$25 \$20
-

Question #20 of 52

Question ID: 1590292

Xanos Corporation faced a 50% marginal tax rate last year and showed the following financial and tax reporting information:

- Deferred tax asset of 1,000.
- Deferred tax liability of 5,000.

Based only on this information and the news that the tax rate will decline to 40%, Xanos Corporation's deferred tax:

- A) asset will be reduced by 200 and income tax expense will be reduced by 1,000.
- B) liability will be reduced by 1,000 and income tax expense will be reduced by 800.
- C) asset will be reduced by 400 and deferred tax liability will be reduced by 2,000.
-

Question #21 of 52

Question ID: 1590309

Fred Company has a deferred tax liability of \$1,200,000. If Fred's tax rate increases from 30% to 40%, the impact of this tax rate change will:

- A) increase Fred's income tax expense by \$120,000.
- B) increase Fred's income tax expense by \$400,000.
- C) decrease Fred's income tax expense by \$120,000.
-

Question #22 of 52

Question ID: 1590333

Which of the following statements *best* justifies analyst scrutiny of valuation allowances?

- A)** Changes in valuation allowances can be used to manage reported net income.
 - B)** Increases in valuation allowances may be a signal that management expects earnings to improve in the future.
 - C)** If differences in taxable and pretax incomes are never expected to reverse, a company's equity may be understated.
-

Question #23 of 52

Question ID: 1590298

Camphor Associates uses accrual basis for financial reporting purposes and cash basis for tax purposes. Cash collections from customers is \$238,000, and accrued revenue is only \$188,000. Assume expenses at 50% in both cases (i.e., \$119,000 on cash basis and \$94,000 on accrual basis), and a tax rate of 34%. What is the deferred tax asset/liability in this case? A deferred tax:

- A)** asset of \$48,960.
 - B)** liability of \$8,500.
 - C)** asset of \$8,500.
-

Question #24 of 52

Question ID: 1590308

A company purchased a new pizza oven for \$12,676. It will work for 5 years and has no salvage value. The tax rate is 41%, and annual revenues are constant at \$7,192. For financial reporting, the straight-line depreciation method is used, but for tax purposes depreciation is 35% of original cost in years 1 and 2 and the remaining 30% in Year 3. For this question ignore all expenses other than depreciation.

What is the deferred tax liability as of the end of year three?

- A)** \$2,079.
- B)** \$780.
- C)** \$1,029.

Question #25 of 52

Question ID: 1590302

The Puchalski Company reported the following:

	Year 1	Year 2	Year 3	Year 4
Income before taxes	\$1,000	\$1,000	\$900	\$800
Taxable income	\$800	\$900	\$900	\$1,000

Puchalski has no deferred tax asset or liability prior to Year 1. If the tax rate is 40%, what is the amount of the deferred tax asset or liability reported at the end of Year 3?

- A) Asset of \$120.
 - B) Asset of \$80.
 - C) Liability of \$120.
-

Question #26 of 52

Question ID: 1590326

Permanent differences between taxable and pretax income:

- A) can be deferred in some cases.
 - B) are not addressed specifically in the financial statements.
 - C) are considered as changes in the effective tax rate.
-

Question #27 of 52

Question ID: 1590323

Which of the following statements regarding deferred taxes is *least* accurate?

- A) A deferred tax asset is created when a temporary difference results in taxable income that exceeds pretax income.
- B) A permanent difference is a difference between taxable income and pretax income that will not reverse.

C) Deferred tax assets and liabilities are not adjusted for changes in tax rates.

Question #28 of 52

Question ID: 1590285

Which of the following is the *most accurate* definition of a liability's tax base?

- A) Carrying amount of the liability minus the amount that will not be deductible in the future.
 - B) Amount of tax payable by the company at year-end.
 - C) Carrying amount of the liability minus the amount that will be deductible in the future.
-

Question #29 of 52

Question ID: 1590288

In 20X8, Oliver Ltd. received \$80,000 cash from a customer for goods that it could not deliver until the next year and established a liability for unearned revenue. Oliver reports under U.S. GAAP, faces a 40% tax rate, and is located in a tax jurisdiction where unearned revenue is taxed as received. On their balance sheet for 20X8, what change in deferred tax should Oliver record as a result of this transaction?

- A) A deferred tax asset of \$32,000.
 - B) A deferred tax liability of \$32,000.
 - C) There is no effect on deferred tax items from this transaction.
-

Question #30 of 52

Question ID: 1590305

Given the following data regarding two firms under different scenarios, determine the amount of any deferred tax liability or asset.

Firm 1:

<i>Tax Reporting</i>		<i>Financial Reporting</i>	
Revenue	\$500,000	Revenue	\$500,000
Depreciation	<u>\$100,000</u>	Depreciation	<u>\$50,000</u>
Taxable income	\$400,000	Pretax income	\$450,000
Taxes payable	<u>\$160,000</u>	Tax expense	<u>\$180,000</u>
Net income	\$240,000	Net income	\$270,000

Firm 2:

<i>Tax Reporting</i>		<i>Financial Reporting</i>	
Revenue	\$500,000	Revenue	\$500,000
Warranty expense	<u>\$0</u>	Warranty expense	<u>\$10,000</u>
Taxable income	\$500,000	Pretax income	\$490,000
Taxes payable	<u>\$200,000</u>	Tax expense	<u>\$196,000</u>
Net income	\$300,000	Net income	\$294,000

Firm 1 Deferred Tax

Firm 2 Deferred Tax

- A) \$20,000 Liability \$4,000 Asset
- B) \$20,000 Asset \$6,000 Liability
- C) \$30,000 Asset \$6,000 Asset

A firm buys an asset with an estimated useful life of five years for \$100,000 at the beginning of the year. The firm will depreciate the asset on a straight-line basis with no salvage value on its financial statements and will use double declining balance depreciation for tax. The tax base for this asset at the end of the first year is *closest* to:

- A) \$80,000.
 - B) \$60,000.
 - C) \$40,000.
-

Question #32 of 52

Question ID: 1590318

Inka Corporation has deferred tax assets of \$20 million and deferred tax liabilities of \$50 million. The corporate tax rate decreases from 40% to 35%. What effect will the tax rate change have on net income?

- A) No effect on net income.
 - B) Increase net income.
 - C) Decrease net income.
-

Question #33 of 52

Question ID: 1590286

Noonan, Ltd. estimates that a warranty provision of \$20,000 will be required on goods already sold. On the tax return, warranties are not deductible until the warranty work has been performed. What is the tax base of the warranty liability?

- A) \$20,000.
 - B) \$0.
 - C) \$10,000.
-

Question #34 of 52

Question ID: 1590332

Which of the following situations will *most likely* require a company to record a valuation allowance on its balance sheet?

- A) A firm has differences between taxable and pretax income that are never expected to reverse.
 - B) To report depreciation, a firm uses the double-declining balance method for tax purposes and the straight-line method for financial reporting purposes.
 - C) A firm is unlikely to have future taxable income that would enable it to take advantage of deferred tax assets.
-

Question #35 of 52

Question ID: 1590334

Which of the following statements *best* describes the impact of a valuation allowance on the financial statements? A valuation allowance:

- A) increases reported income, reduces assets, and reduces equity.
 - B) reduces reported income, increases liabilities, and reduces equity.
 - C) reduces reported income, reduces assets, and reduces equity.
-

Question #36 of 52

Question ID: 1590304

The Puchalski Company reported the following:

	<i>Year 1</i>	<i>Year 2</i>	<i>Year 3</i>	<i>Year 4</i>
Income before taxes	\$1,000	\$1,000	\$900	\$800
Taxable income	\$800	\$900	\$900	\$1,000

The differences between income before taxes and taxable income are the result of using accelerated depreciation for tax purposes on an asset purchased in Year 1. Puchalski had no deferred tax liability prior to Year 1. If the tax rate is 40%, what is the amount of the deferred tax liability reported at the end of Year 4?

- A) \$40.

- B) \$80.
 - C) \$120.
-

Question #37 of 52

Question ID: 1590325

Which of the following statements regarding differences between taxable and pretax income is *most* accurate? Differences between taxable and pretax income that:

- A) result in deferred tax assets or liabilities are called temporary differences.
 - B) are not reversed for five or more years are called permanent differences.
 - C) increase or decrease the effective tax rate are called temporary differences.
-

Question #38 of 52

Question ID: 1590293

Corcoran Corp acquired an asset on 1 January 2004, for \$500,000. For financial reporting, Corcoran will depreciate the asset using the straight-line method over a 10-year period with no salvage value. For tax purposes the asset will be depreciated straight line for five years and Corcoran's effective tax rate is 30%. Corcoran's deferred tax liability for 2004 will:

- A) decrease by \$15,000.
 - B) decrease by \$50,000.
 - C) increase by \$15,000.
-

Question #39 of 52

Question ID: 1590287

At the end of 20X8, Martin Inc. estimates that \$26,000 of warranty repairs will be required in the future on goods already sold. For tax purposes, warranty expense is not deductible until the work is actually performed. The firm believes that the warranty work will be required over the next two years. The tax base of the warranty liability at the end of 20X8 is:

A) \$26,000.

B) \$13,000.

C) zero.

Question #40 of 52

Question ID: 1590307

A company purchased a new pizza oven for \$12,676. It will work for 5 years and has no salvage value. The tax rate is 41%, and annual revenues are constant at \$7,192. For financial reporting, the straight-line depreciation method is used, but for tax purposes depreciation is 35% of original cost in years 1 and 2 and the remaining 30% in Year 3. For this question ignore all expenses other than depreciation.

What is the deferred tax liability as of the end of year one?

A) \$780.

B) \$1,129.

C) \$1,909.

Question #41 of 52

Question ID: 1590329

For the year ended 31 December 2004, Pick Co's pretax financial statement income was \$400,000 and its taxable income was \$300,000. The difference is due to the following:

Interest on tax-exempt municipal bonds	\$140,000
Premium expense on key person life insurance	\$(40,000)
Total	\$100,000

Pick's statutory income tax rate is 30 percent. In its 2004 income statement, what amount should Pick report as current provision for tax payable?

A) \$102,000.

B) \$90,000.

C) \$120,000.

Question #42 of 52

Question ID: 1590297

This year, Blue Horizon has recorded \$390,000 in revenue for financial reporting purposes, but, on a cash basis, revenue was only \$262,000. Assume expenses at 50% in both cases (i.e., \$195,000 on accrual basis and \$131,000 on cash basis), and a tax rate of 34%. What is the deferred tax liability or asset? A deferred tax:

- A) liability of \$21,760.
- B) asset of \$21,760.
- C) liability of \$16,320.

Question #43 of 52

Question ID: 1590299

A firm purchased a piece of equipment for \$6,000 with the following information provided:

- Revenue will increase by \$15,000 per year.
- The equipment has a 3-year life expectancy and no salvage value.
- The firm's tax rate is 30%.
- Straight-line depreciation is used for financial reporting and double declining is used for tax purposes.

What will the firm report for deferred taxes on the balance sheet for years 1 and 2?

- | | <u>Year 1</u> | <u>Year 2</u> |
|----|---------------|---------------|
| A) | \$3,900 | \$3,900 |
| B) | \$3,300 | \$4,100 |
| C) | \$600 | \$400 |

Question #44 of 52

Question ID: 1590295

Kruger Associates uses an accrual basis for financial reporting purposes and cash basis for tax purposes. Cash collections from customers are \$476,000, and accrued revenue is only \$376,000. Assume expenses at 50% in both cases (i.e., \$238,000 on cash basis and \$188,000 on accrual basis), and a tax rate of 34%. What is the deferred tax asset or liability? A deferred tax:

- A)** liability of \$17,000.
 - B)** asset of \$17,000.
 - C)** asset of \$48,960.
-

Question #45 of 52

Question ID: 1590301

All-Star Enterprises purchased a machine on January 1. The company uses straight-line depreciation for financial reporting and accelerated depreciation for tax purposes. Depreciation for tax purposes during the year was \$36,000 greater than depreciation for financial reporting. Assuming a 30% tax rate will apply in the future, how much will be recorded as a deferred tax liability during the year?

- A)** \$10,800.
 - B)** \$25,200.
 - C)** \$36,000.
-

Question #46 of 52

Question ID: 1590291

In the period when a deferred tax liability reverses, tax expense on the income statement is:

- A)** less than taxes payable on the tax return.
 - B)** greater than taxes payable on the tax return.
 - C)** equal to taxes payable on the tax return.
-

Question #47 of 52

Question ID: 1590306

A company purchased a new pizza oven for \$12,676. It will work for 5 years and has no salvage value. The tax rate is 41%, and annual revenues are constant at \$7,192. For financial reporting, the straight-line depreciation method is used, but for tax purposes depreciation is 35% of original cost in years 1 and 2 and the remaining 30% in Year 3. For this question ignore all expenses other than depreciation.

What is the tax payable for year one?

- A) \$1,130.
 - B) \$779.
 - C) \$1,909.
-

Question #48 of 52

Question ID: 1590296

Unit Technologies uses accrual basis for financial reporting purposes and cash accounting for tax purposes. So far this year, Unit Technologies has recorded \$195,000 in revenue for financial reporting purposes, but, on a cash basis, revenue was only \$131,000. Assume expenses at 50 percent in both cases (i.e., \$ 97,500 on accrual basis and \$ 65,500 on cash basis), and a tax rate of 34%. What is the deferred tax liability or asset? A deferred tax:

- A) liability of \$16,320.
 - B) liability of \$10,880.
 - C) asset of \$10,880.
-

Question #49 of 52

Question ID: 1590310

Laser Tech has net temporary differences between tax and book income resulting in a deferred tax liability of \$30.6 million. According to U.S. GAAP, an increase in the tax rate would have what impact on deferred taxes and net income, respectively:

Deferred Taxes

Net Income

- A) Increase Decrease
- B) Increase No effect
- C) No effect Decrease
-

Question #50 of 52

Question ID: 1590319

A firm with an effective tax rate of 35% uses straight-line depreciation on its financial statements and accelerated depreciation for tax reporting. This results in the following differences:

	Year 1	Year 2	Year 3
Accounting depreciation	4,000	4,000	4,000
Tax depreciation	8,000	2,667	1,333
Timing difference	(4,000)	1,333	2,667

At the end of Year 2, what deferred tax item is the result of these differences?

- A) \$467 deferred tax liability.
- B) \$933 deferred tax liability.
- C) \$467 deferred tax asset.
-

Question #51 of 52

Question ID: 1590317

When an increase in the tax rate is enacted, deferred tax:

- A) liability and asset accounts are maintained at historical tax rates until they reverse.
- B) assets decrease in value and deferred tax liabilities increase in value.
- C) assets and liabilities both increase in value.
-

Question #52 of 52

Question ID: 1590294

A company purchased a new pizza oven directly from Italy for \$12,676. It will work for 5 years and has no salvage value. The tax rate is 41%, and annual revenues are constant at \$7,192. For financial reporting, the straight-line depreciation method is used, but for tax purposes depreciation is accelerated to 35% in years 1 and 2, and 30% in year 3. For purposes of this exercise ignore all expenses other than depreciation.

What is the net income and depreciation expense for year one for financial reporting purposes?

	<u>Net Income</u>	<u>Depreciation Expense</u>
A)	\$2,748	\$2,535
B)	\$4,657	\$2,748
C)	\$2,535	\$3,169