

ACCOUNTANCY 422
SUPPLEMENTAL PROBLEM
DEFERRED TAXES

Farmer Inc. began business on January 1, 2010. Its pretax financial income for the first 2 years was as follows:

2010	\$240,000
2011	560,000

The following items caused the only differences between pretax financial income and taxable income.

1. In 2010, the company collected \$180,000 of rent; of this amount, \$60,000 was earned in 2010; the other \$120,000 will be earned equally over the 2011–2012 period. The full \$180,000 was included in taxable income in 2010.
2. The company pays \$10,000 a year for life insurance on officers.
3. In 2010, the company terminated a top executive and agreed to \$90,000 of severance pay. The amount will be paid \$30,000 per year for 2010–2012. The first two payments were paid during 2010. The \$90,000 will be properly expensed in 2012. For tax purposes, the severance pay is deductible as it is paid.

The enacted tax rates existing at December 31, 2010 are:

2010	30%	2012	40%
2011	35%	2013	45%

Required:

1. Prepare a deferred tax worksheet for 2010 in good form.
2. Record the year-end tax journal entry.

THE SOLUTION IS ON THE NEXT PAGE

Farmer, Inc.
 Deferred Taxes
 For the Year Ended December 31, 2010

Enacted tax rate (2011)= 35%
 Enacted Tax Rate (2012) = 40%

<u>Accounting Event</u>	<u>Future Taxable Amount</u>	<u>Future Deductible Amount</u>	<u>Deferred Tax Liability</u>	<u>Deferred Tax Asset</u>	<u>Taxable Income</u>
Pretax income					\$ 240,000
<u>Noncurrent</u>					
Unearned rent		\$ 60,000	\$ -	\$ 24,000	\$ 60,000
Severance Pay	\$ 30,000		\$ 12,000		\$ (30,000)
Total Noncurrent			<u>\$ 12,000</u>	<u>\$ 24,000</u>	
<u>Current</u>					
Unearned rent		\$ 60,000	\$ -	\$ 21,000	\$ 60,000
Severance Pay	\$ 30,000		\$ 10,500		\$ (30,000)
Total Current			<u>\$ 10,500</u>	<u>\$ 21,000</u>	
<u>Permanent Items</u>					
Life insurance premiums					\$ 10,000
Taxable income					\$ 310,000
Current tax rate					30%
Tax payable					<u>\$ 93,000</u>

Journal Entry

Noncurrent deferred tax asset	\$ 24,000		
Current deferred tax asset	\$ 21,000		
Provision for income taxes	\$ 70,500		
Noncurrent deferred tax liability		\$ 12,000	
Current deferred tax liability		\$ 10,500	
Income tax payable		\$ 93,000	