

ACCOUNTING FOR TAXES ON INCOME

AS
22

<p>Scope</p>	<p>This standard prescribes the accounting treatment of taxes on income and follows the concept of matching expenses against revenue for the period.</p> <p>This includes determination of the amount of the expense or saving related to taxes on income in respect of an accounting period & disclosure of such an amount in the financial statements.</p> <p>The differences between taxable income and accounting income can be classified into permanent differences and timing differences</p>	
<p>Definitions</p>	<p>Accounting income (loss)</p>	<p>Net profit or loss for a period, as reported in the statement of profit and loss, before deducting income-tax expense or adding income tax saving.</p>
	<p>Taxable income (tax loss)</p>	<p>Amount of the income (loss) for a period, determined in accordance with the tax laws, based upon which income-tax payable (recoverable) is determined.</p>
	<p>Tax expense (tax saving)</p>	<p>Aggregate of current tax and deferred tax charged or credited to the statement of profit and loss for the period</p>
	<p>Current tax</p>	<p>Amount of income tax determined to be payable (recoverable) in respect of the taxable income (tax loss) for a period.</p>
	<p>Deferred tax</p>	<p>Tax effect of timing differences.</p>
	<p>Timing differences</p>	<p>Differences between taxable income and accounting income for a period that originate in one period and are capable of reversal in one or more subsequent periods.</p>
	<p>Permanent differences</p>	<p>Differences between taxable income and accounting income for a period that originate in one period and do not reverse subsequently</p>
<p>Recognition</p>	<ul style="list-style-type: none"> ❖ Tax expense for the period, comprising current tax and deferred tax, should be included in the determination of net profit or loss for the period. ❖ Permanent differences do not result in deferred tax assets or deferred tax liabilities. ❖ Taxes on income are considered to be an expense incurred by the enterprise in earning income and are accrued in the same period as the revenue and expenses to which they relate. Such matching may result into timing differences. ❖ The tax effects of timing differences are included in the tax expense in the statement of profit and loss and as deferred tax assets or as deferred tax liabilities, in the balance sheet. 	
<p>Deferred Tax Assets</p>	<ul style="list-style-type: none"> ❖ While recognizing the tax effect of timing differences, consideration of prudence cannot be ignored. Therefore, deferred tax assets are recognised and carried forward only to the extent that there is a reasonable certainty of their realisation. 	

	<ul style="list-style-type: none"> ❖ This reasonable level of certainty would normally be achieved by examining the past record of the enterprise and by making realistic estimates of profits for the future. ❖ Where an enterprise has unabsorbed depreciation or carry forward of losses under tax laws, <i>deferred tax assets should be recognised</i> only to the extent that there is <i>virtual certainty supported by convincing evidence</i> that sufficient future taxable income will be available against which such deferred tax assets can be realised. 	
Re-Assessment of Unrecognized Deferred Tax Assets	At each balance sheet date, an enterprise re-assesses unrecognized deferred tax assets. The enterprise recognizes previously unrecognized deferred tax assets to the extent that it has become reasonably certain or virtually certain, as the case may be, that sufficient future taxable income will be available against which such deferred tax assets can be realized	
Measurement	<ul style="list-style-type: none"> ➤ Current tax should be measured at the amount expected to be paid to (recovered from) the taxation authorities, using the applicable tax rates and tax laws. ➤ Deferred tax assets and liabilities are usually measured using the tax rates and tax laws that have been enacted by the balance sheet date. ➤ However, certain announcements of tax rates and tax laws by the government may have the substantive effect of actual enactment. In these circumstances, deferred tax assets and liabilities are measured using such announced tax rate and tax laws. ➤ Deferred tax assets and liabilities should not be discounted to their present value. 	
Disclosure	Statement of profit & loss	Under AS 22, there is no specific requirement to disclose current tax and deferred tax in the statement of profit and loss. However, considering the requirements under the Companies Act, 2013, the amount of income tax and other taxes on profits should be disclosed.
	Balance sheet	Deferred tax assets and liabilities should be disclosed under a separate heading in the balance sheet of the enterprise, separately from current assets and current liabilities.
Accounting for Taxes on Income in the situations of Tax Holiday	<ul style="list-style-type: none"> ❖ The deferred tax in respect of timing differences which reverse during the tax holiday period should not be recognised to the extent the enterprise's gross total income is subject to the deduction during the tax holiday period as per the requirements of the Act. ❖ Deferred tax in respect of timing differences which reverse after the tax holiday period should be recognised in the year in which the timing differences originate. ❖ However, recognition of deferred tax assets should be subject to the consideration of prudence as laid down in AS 22. For the above purposes, the timing differences which originate first should be considered to reverse first 	

ASSIGNMENT QUESTIONS

Question 1 ***(RTP Jan 2025)*** _____ Pg no. _____

ABC Ltd. prepares its accounts annually on 31st March. On 1st April, 2022, it purchases a machine at a cost of ₹ 1,50,000. The machine has a useful life of three years and an expected scrap value of zero. Although it is eligible for a 100% first year depreciation allowance for tax purposes, the straight line method is considered appropriate for accounting purposes. ABC Ltd. has profits before depreciation and taxes of ₹ 2,00,000 each year and corporate tax rate is 40% each year.

The purchase of machine at a cost of ₹ 1,50,000 in 2022 gives rise to a tax saving of ₹ 60,000. The corporate tax rate has been assumed to be same in each of the three years.

Calculate deferred tax and pass necessary journal entries.

What will be the amount of deferred tax, if the substantively enacted tax rates for 2022, 2023 and 2024 are 40%, 35% and 38% respectively.

Question 2 ***(ICAI Study Material)*** _____ Pg no. _____

Omega Limited is working on different projects which are likely to be completed within 3 years period. It recognizes revenue from these contracts on percentage of completion method for financial statements during 2017-2018, 2018-2019 and 2019-2020 for ₹ 11,00,000, ₹ 16,00,000 and ₹ 21,00,000 respectively. However, for Income-tax purpose, it has adopted the completed contract method under which it has recognised revenue of ₹ 7,00,000, ₹ 18,00,000, and ₹ 23,00,000 for years 2017-2018, 2018-2019 and 2019-2020 respectively. Income-tax rate 35%. Compute the amount of deferred tax asset/ liability for the years 2017-2018, 2018-2019 and 2019-2020.

Question 3 ***(RTP May 2018) / (ICAI Study Material)*** _____ Pg no. _____

Rama Ltd., has provided the following information:

Depreciation as per accounting records	2,00,000
Depreciation as per income tax records	5,00,000
Unamortised preliminary expenses as per tax record	30,000

There is adequate evidence of future profit sufficiency. How much deferred tax asset/ liability should be recognised as transition adjustment? Tax rate 50%

Question 4 ***(RTP May 2020)*** _____ Pg no. _____

The following particulars are stated in the Balance Sheet of PQR Ltd. as on 31.03.2019

	(₹ In Lakhs)
Deferred Tax Liability (Cr.)	30.00
Deferred Tax Assets (Dr.)	15.00

The following transactions were reported during the year 2019-20

(i)	Tax Rate	30%
		(₹ In Lakhs)
(ii)	Depreciation as per Books	80.00
	Depreciation for tax purposes	70.00
(iii)	Items disallowed in 2018-19 & allowed for tax purposes in 2019-20	10.00
(iv)	Donations to Private Trusts made in 2019-20	10.00

There were no additions to Fixed Assets during the year. You are required to show the impact of various items on Deferred Tax Assets and Deferred Tax Liability as on 31.03.2020.

Question 5 - **(Inter Nov 2023) (5 Marks)** Pg no. _____

The following particulars are stated in Balance Sheet of Siddhi Limited as on 31st March, 2022:

Particulars	(₹ In lakhs)
Deferred Tax Liabilities (Cr.)	2.50
Deferred Tax Assets (Dr.)	1.35

The following transactions were reported during the year 2022-23:

	(₹ in Lakhs)
(i) Depreciation as per accounting records	15.00
(ii) Depreciation as per income tax records	20.00
(iii) Interest paid to NBFC accounted in books on accrual basis but paid on 30-06-2023	6.00
(iv) Items disallowed for tax purposes in 2021-22 but allowed in 2022-23	1.05
(v) Donation to Private Trust	40.00
(vi) Tax rate	15%
(vii) There were no additions to fixed assets during the year	

You are required to calculate the Deferred Tax Asset and Deferred Tax Liability as on 31st March 2023 as per AS-22.

Solution

Balances of Deferred tax assets and Deferred tax liability as on 31st March, 2023

	₹ (in lakhs)
Deferred tax liability (Cr.) (2.5 +.75)	3.25
Deferred tax asset (Dr.) (1.35 - .158*)	1.192

Working Note:

Impact of various items in terms of deferred tax liability / deferred tax asset

S. No.	Transactions	Nature of difference	Effect	Amount (₹)
(i), (ii)	Difference in depreciation	Timing difference	Creation of DTL	(20 - 15) x 15% = .75 lakh
(iii)	Interest to financial institutions	No timing difference	Not applicable	Not applicable
(iv)	Disallowances, as per IT Act, of earlier years	Timing difference	Reversal of DTA	₹ 1.05 lakh x 15% = ₹ .158* lakh
(v)	Donation to private trusts	Permanent difference	Not applicable	Not applicable

*Alternatively, may be rounded off as ₹ 0.157 lakh or 0.1575 lakh

Question 6 **(RTP May 2021)** Pg no. _____

The following information is furnished in respect of Slate Ltd. for the year ending 31-3-2019:

(i) Depreciation as per books ₹ 2,80,000

Depreciation for tax purpose ₹ 1,90,000

The above depreciation does not include depreciation on new additions.

(ii) A new machinery purchased on 1.4.18 costing ₹ 1,20,000 on which 100% depreciation is allowed in the 1st year for tax purpose whereas Straight-line method is considered appropriate for accounting purpose with a life estimation of 4 years.

(iii) The company has made a profit of ₹ 6,40,000 before depreciation and taxes.

(iv) Corporate tax rate of 40%.

Prepare relevant extract of statement of Profit and Loss for the year ending 31-3-2019 and also show the effect of above items on deferred tax liability/asset as per AS 22

Question 7 - *(ICAI Study Material)* Pg no. _____

ABC Company Ltd. had an investment in Venture Capital amounting 10 Crores. Venture capital in turn had invested in the below portfolio companies (New Start-ups) on behalf of ABC Ltd:

Portfolio Companies	Amount of investment (₹ in Crores)
Oscar Limited	2
Zee Limited	3
Star Limited	4
Sony Limited	1
Total	10

During the FY 2019-2020, Venture Capital had sold their investment in Star Limited and realised an amount of ₹ 8 Crores on sale of shares of star Limited and entire proceeds of ₹ 8 Crores have been transferred by Venture Capital to ABC Company Limited.

The accounts manager has received the following additional information from venture capital on 31.03.2020:

- ₹8 Crores has been deducted from the cost of investment and carrying amount of investment as at year end is ₹ 2 Crores.
- Company had to pay a capital gain tax @ 20% on the net sale consideration of ₹ 4 Crores.
- Due to COVID-19, the remaining start-ups (i.e. Oscar Limited, Zee Limited, and Sony Limited) are not performing well and will soon wind up their operations. Venture capital is monitoring the situation and if required they will provide an impairment loss in June 2020 Quarter.

You need to suggest the accounts manager what should be the correct accounting treatment as per AS 22 "Accounting for Taxes on Income"

Solution

As company had to pay capital gain tax @ 20% on the net sale consideration as per income tax laws, the company has to recognise a current tax liability of 0.8 Crores computed as under:

Particulars	Amount (crores)
Sales Consideration	8
Cost of Investment	4
Net gain on Sale	4
Tax @ 20%	0.8

Timing differences are those differences between taxable income & accounting income for a period that originate in one period & are capable of reversal in one or more subsequent period

Particulars	Amount (crores)	Rationale
Taxable Income	4	As per income tax laws
Accounting Income	Nil	As the same is deducted from the cost of investment
Timing Difference	4	

As per AS 22, deferred tax assets should be recognised and carried forward only to the extent that there is a reasonable certainty that sufficient future taxable income will be available against which such deferred tax assets can be realised.

Since in current scenario, due to Covid 19 the portfolio companies are not performing well, thus the company may not have sufficient future taxable income which will reverse deferred tax assets. Therefore, the company should not recognise DTA of ₹ 0.8 Crores and company should recognise only current tax liability of ₹ 0.8 Crores.

Question 8 ***(ICAI Study Material)*** Pg no. _____

PQR Ltd.'s accounting year ends on 31st March. The company made a loss of ₹ 2,00,000 for the year ending 31.3.2018. For the years ending 31.3.2019 and 31.3.2020, it made profits of ₹ 1,00,000 and ₹ 1,20,000 respectively. It is assumed that the loss of a year can be carried forward for eight years and tax rate is 40%. By the end of 31.3.2018, the company feels that there will be sufficient taxable income in the future years against which carry forward loss can be set off. There is no difference between taxable income and accounting income except that the carry forward loss is allowed in the years ending 2019 and 2020 for tax purposes. Prepare a statement of Profit and Loss for the years ending 2018, 2019 and 2020

Question 9 ***(RTP Nov 2018)*** Pg no. _____

Beta Ltd. is a full tax-free enterprise for the first ten years of its existence and is in the second year of its operation. Depreciation timing difference is ₹ 1,000 lakhs and ₹ 2,000 lakhs respectively which will result in a tax liability in year 1 and 2. From the third year it is expected that the timing difference would reverse each year by ₹ 50 lakhs. Assuming tax rate of 40%, you are required to compute the deferred tax liability at the end of the second year and any charge to the Profit and Loss account

Solution

As per AS 22, Accounting for Taxes on Income", deferred tax in respect of timing differences which originate during the tax holiday period and reverse during the tax holiday period, should not be recognized to the extent deduction from the total income of an enterprise is allowed during the tax holiday period as per the provisions of sections 10A and 10B of the Income-tax Act. Deferred tax in respect of timing differences which originate during the tax holiday period but reverse after the tax holiday period should be recognized in the year in which the timing differences originate. However, recognition of deferred tax assets should be subject to the consideration of prudence. For this purpose, the timing differences which originate first should be considered to reverse first.

Out of ₹ 1,000 lakhs depreciation, timing difference amounting ₹ 400 lakhs (₹ 50 lakhs x 8 years) will reverse in the tax holiday period and therefore, should not be recognized. However, for ₹ 600 lakhs (₹ 1,000 lakhs – ₹ 400 lakhs), deferred tax liability will be recognized for ₹ 240 lakhs (40% of ₹ 600 lakhs) in first year. In the second year, the entire amount of timing difference of ₹ 2,000 lakhs will reverse only after-tax holiday period and hence, will be recognized in full. Deferred tax liability amounting ₹ 800 lakhs (40% of ₹ 2,000 lakhs) will be created by charging it to profit and loss account and the total balance of deferred tax liability account at the end of second year will be ₹ 1,040 lakhs (240 lakhs + 800 lakhs).

Question 10 - ***(ICAI Study Material)*** Pg no. _____

From the following details of A Ltd. for the year ended 31-03-2020, calculate the deferred tax asset/ liability as per AS 22 and amount of tax to be debited to the Profit and Loss Account for the year.

Particulars	₹
Accounting Profit	6,00,000
Book Profit as per MAT	3,50,000
Profit as per Income Tax Act	60,000
Tax Rate	20%
MAT Rate	7.50%

PRACTICE QUESTIONS

Question 1 *(Inter May 2019) (5 Marks) / (RTP Nov 2020) / (ICAI Study Material)* Pg no. _____

Write short note on Timing differences and Permanent differences as per AS 22.

Solution

In current practices, companies, in general, prepare books of accounts as per Companies Act, 2013 generating Accounting Profit/Loss and Income-tax Act, 1961 generating Taxable Profit/Loss. Accounting income and taxable income for a period are seldom the same.

Permanent differences are the differences between taxable income and accounting income which arise in one accounting period and do not reverse subsequently. For example, an income exempt from tax or an expense that is not allowable as a deduction for tax purposes.

Timing differences are those differences between taxable income and accounting income which arise in one accounting period and are capable of reversal in one or more subsequent periods. For e.g., Depreciation, Bonus, etc.

Question 2 *(Inter May 2018) (5 Marks)* Pg no. _____

Rohit Ltd. has provided the following information:

Particulars	Amount
Depreciation as per accounting records	2,50,000
Depreciation as per tax records	5,50,000
Unamortised preliminary expenses as per tax record	40,000

There is adequate evidence of future profit sufficiency. How much deferred tax assets/liability should be recognized as transition adjustment when the tax rate is 50%?

Solution

Table showing calculation of deferred tax asset / liability

Particulars	Amount	Timing Difference	Deferred Tax	Amount @ 50%
Excess depreciation as per tax records (5,50,000 – 2,50,000)	3,00,000	Timing	Deferred Tax Liability	1,50,000
Unamortised preliminary expenses as per tax records	40,000	Timing	Deferred Tax Asset	20,000
Net deferred tax liability				1,30,000

Net deferred tax liability amounting ₹ 1,30,000 should be recognized as transition adjustment.

Question 3 *(RTP Nov 2020)* Pg no. _____

Rama Ltd. has provided the following information:

Particulars	Amount
Depreciation as per accounting records	6,00,000
Depreciation as per tax records	10,00,000
Unamortised preliminary expenses as per tax record	60,000

There is adequate evidence of future profit sufficiency.

You are required to calculate the amount of deferred tax asset/liability to be recognized as transition adjustment assuming tax rate as 30%?

Solution

Table showing calculation of deferred tax asset / liability

Particulars	Amount	Timing Difference	Deferred Tax	Amount @ 30%
Excess depreciation as per tax records (₹ 10,00,000 - ₹ 6,00,000)	4,00,000	Timing	Deferred Tax Liability	1,20,000
Unamortised preliminary expenses as per tax records	60,000	Timing	Deferred Tax Asset	18,000
Net deferred tax liability				1,02,000

Net deferred tax liability amounting 1,02,000 should be recognized as transition adjustment.

Question 4 **(Inter Jan 2021) (5 Marks)**

Pg no. _____

The following particulars are stated in the Balance Sheet of HS Ltd. as on 31.03.2019

	(₹ In Lakhs)
Deferred Tax Liability (Cr.)	60.00
Deferred Tax Assets (Dr.)	30.00

The following transactions were reported during the year 2019-20

(i)	Tax Rate	30%
		(₹ In Lakhs)
(ii)	Depreciation as per accounting records	160.00
	Depreciation as per income tax records	140.00
(iii)	Items disallowed in 2018-19 & allowed for tax purposes in 2019-20	20.00
(iv)	Donations to Private Trusts	20.00

There were no additions to Fixed Assets during the year. You are required to show the impact of various items on Deferred Tax Assets & Deferred Tax Liability as on 31.03.20 as per AS 22.

Solution

Impact of various items in terms of AS 22 deferred tax liability/deferred tax asset

- Difference in Depreciation-** Generally, written down value method of depreciation is adopted under income Tax Act which leads to higher depreciation in earlier years of useful life of the asset in comparison to later years. It is timing difference for which reversal of Deferred tax liability is required.
Reversal of DTL = $(160 - 140)$ Lakhs $\times 30\% = 6$ Lakhs
- Disallowances, as per IT Act of earlier years-** Due to disallowance tax payable for the earlier years was higher on this account. It is responding timing difference which required Reversal of Deferred tax assets.
Reversal of Deferred tax assets = 20 Lakhs $\times 30\% = 6$ Lakhs
- Donations to private trusts** is not an allowable expenditure under IT Act. It is permanent difference. Hence, no reversal of tax is required

Question 5 **(Inter July 2021) (5 Marks)**

Pg no. _____

Following particulars are stated in the Balance Sheet of Deep Limited as on 31st March, 2020:

	(₹ In Lakhs)
Deferred Tax Liability (Cr.)	28.00
Deferred Tax Assets (Dr.)	14.00

The following transactions were reported during the year 2020 -2021:

- Depreciation as per books was ₹ 70 Lakhs whereas Depreciation for Tax purposes was ₹ 42 Lakhs. There were no additions to Fixed Assets during the year.

- (ii) Expenses disallowed in 2019-20 and allowed for tax purposes in 2020-21 were ₹ 14 Lakhs.
- (iii) Share issue expenses allowed under section 35(D) of the Income Tax Act, 1961 for the year 2020-21 (1/10th of ₹ 70.00 lakhs incurred in 2019-20).
- (iv) Repairs to Plant and Machinery were made during the year for ₹ 140.00 Lakhs and was spread over the period 2020-21 and 2021-22 equally in the books. However, the entire expenditure was allowed for income-tax purposes in the year 2020-21.

Tax Rate to be taken at 40%.

You are required to show the impact of above items on Deferred Tax Assets and Deferred Tax Liability as on 31st March, 2021.

Solution

Impact of various items in terms of deferred tax liability/deferred tax asset on 31.3.21

Transactions	Analysis	Nature of difference	Effect	Amount (₹)
Difference in depreciation	Generally, WDV method of dep. is adopted under IT Act which leads to higher dep. in earlier years of useful life of asset in comparison to later years.	Responding timing difference	Reversal of DTL	28 lakhs x 40% = ₹ 11.20 lakhs
Disallowances, as per IT Act, of earlier years	Tax payable for the earlier year was higher on this account.	Responding timing difference	Reversal of DTA	14 lakhs x 40% = 5.6 lakhs
Share issue expenses	Due to disallowance of full expenditure under IT Act, tax payable in the earlier years was higher.	Responding timing difference	Reversal of DTA	7 lakhs x 40% = ₹ 2.8 lakhs
Repairs to plant and machinery	Due to allowance of full expenditure under IT Act, tax payable of the current year will be less.	Originating timing difference	Increase in DTL	70 lakhs x 40% =28 lakhs

Question 6 (RTP May 2022)

Pg no. _____

The following transactions were reported by PQR Ltd. during the year 2020-2021:

(i)	Tax Rate	30%
		(₹ In Lakhs)
(ii)	Items disallowed in 2019-20 & allowed for tax purposes in 2020-21	20.00
(iii)	Interest to Financial Institutions accounted in the books on accrual basis, but actual payment was made before the due date of filing return and allowed for tax purpose also.	20.00
(iv)	Donations to Private Trust made in 2020-2021 (not allowed under Income Tax Laws)	10.00

You are required to show impact of the above items in terms of Deferred Tax Assets/Deferred Tax Liability for the year ended 31.03.2021.

Solution

Impact of various items in terms of deferred tax liability/deferred tax asset on 31.3.21

Transactions	Analysis	Nature of difference	Effect	Amount (₹)
Disallowances, as per IT Act, of earlier years	Tax payable for the earlier year was higher on this account.	Timing difference	Reversal of DTA	20 lakhs x 30% = ₹ 6 lakhs
Interest to financial institutions	It is allowed as deduction under IT Act, if the payment is made before the due date of filing the return of income	No Timing difference	Not Applicable	Not Applicable
Donation to private trusts	Not an allowable expenditure under IT Act.	Permanent difference	Not Applicable	Not Applicable

Question 7 *(ICAI Study Material)*

Pg no. _____

Saras Ltd. closes its books as on 31st March 2022. They have accrued ₹ 5,00,000 towards GST Liability for the month of March 2022 by debiting their Profit and loss statement which is expected to be paid off by 21st April 2022. As per the provisions of Section 43B of the Income Tax Act, 1961 – Any expenditure of the nature mentioned in section 43B (e.g. taxes, duty, cess, fees, etc.) accrued in the statement of profit and loss on mercantile basis will be allowed for tax purposes in subsequent years on payment basis only. Assuming a Tax rate of 30% determine the Deferred Tax Asset/Liability as at 31st March 2022.

Solution**Calculation of difference between taxable income and accounting income**

Particulars	Amount
GST Liability debited in books	5,00,000
Less: GST Liability allowed under Income Tax Act (Section 43B)	Nil
Timing difference	5,00,000

Tax expense is less than the current tax due to timing difference.

Therefore, deferred tax Asset = 30% x 5,00,000 = 1,50,000

Question 8 *(Inter Nov 2022) (5 Marks)*

Pg no. _____

The following information is furnished in respect of Mohit Limited for the year ending 31st March, 2022.

- Depreciation as per accounting records ₹ 56,000
Depreciation for income tax records ₹ 38,000.
The above depreciation does not include depreciation on new addition.
- A new machinery purchased on 1st April, 2021 costing ₹ 24,000 on which 100% depreciation is allowed in the 1st Year for income tax purpose, whereas straight line method of depreciation is considered appropriate for accounting purpose with a life estimation of 4 years.
- The company has made a profit of ₹ 1,28,000 before depreciation and taxes.
- Donation to private trust during the year is ₹ 15,000 (not allowed under Income tax laws.)
- Corporate tax is 40%.

Prepare relevant extract of statement of Profit & Loss for the year ending 31 st March, 2022. Also show the effect of the above items on Deferred Tax Liability/Assets as per AS 22.

Solution**Statement of profit and Loss for the year ended 31st March, 2022 (An Extract)**

	₹
Profit before taxes and depreciation	1,28,000
Less: Depreciation (56,000+ 6,000)	(62,000)
Profit before tax	66,000
Less: Current tax (W.N)	(32,400)
Deferred Tax	Nil
Profit after tax	33,600

Working Note:**Computation of taxable income**

	₹
Profit before taxes and depreciation	1,28,000
Less: Depreciation (38,000+ 24,000)	(62,000)
	66,000
Add: Donation*	15,000
	81,000
Current tax (40%)	32,400

Note: The profit of ₹ 1,28,000 given in question is before depreciation and taxes. It has been considered that this amount is after making adjustment of donation amounting ₹ 15,000.

Impact of various items in terms of deferred tax liability/deferred tax asset

	Transactions	Nature of difference	Effect	Amount
1.	Difference in depreciation (old machinery)	Timing difference	Reversal of DTL	₹ 18,000 (56,000 – 38,000) *40% = (+) ₹ 7,200
2.	Depreciation on new machinery	Timing difference	Creation of DTL	₹ 18,000 (24,000 – 6,000) *40%= (-) ₹ 7,200
3.	Donation to private trusts	Permanent difference	Not applicable	--
	Net Effect of Deferred Tax			Nil

Question 9

Pg no. _____

A company, ABC Ltd., prepares its accounts annually on 31st March. The company has incurred a loss of ₹ 1,00,000 in the year 2018 and made profits of ₹ 50,000 and 60,000 in year 2019 and year 2020 respectively. Under the tax laws, loss can be carried forward for 8 years and tax rate is 40% and at the end of year 2018, it was virtually certain, supported by convincing evidence, that the company would have sufficient taxable income in the future years against which unabsorbed depreciation and carry forward of losses can be set-off. Also there is no difference between taxable income and accounting income except that set-off of loss is allowed in years 2019 and 2020 for tax purposes. Current tax in the year 2020 is ₹ 4,000. Show the effect of above transactions by preparing the Statement of Profit and Loss

Solution**Statement of Profit & Loss**

	2018	2019	2020
Profit / (Loss)	(1,00,000)	50,000	60,000
Less: Current Tax	-	-	(4,000) [10,000*40%]

Deferred Tax:			
Tax effect of timing differences originating during the year (1,00,000 x 40%)	40,000		
Tax effect of timing differences reversed/ adjusted during the year (50,000 x 40%)		(20,000)	(20,000)
Profit / (Loss) after tax	(60,000)	30,000	36,000

Question 10 – **(ICAI Study Material)** Pg no. _____

Y Ltd. is a full tax free enterprise for the first ten years of its existence and is in the second year of its operation. Depreciation timing difference is ₹ 200 lakhs and ₹ 400 lakhs respectively which will result in a tax liability in year 1 and 2. From the third year it is expected that the timing difference would reverse each year by ₹ 10 lakhs. Assuming tax rate of 40%, find out the deferred tax liability at the end of the second year and any charge to the Profit & Loss account.

Solution

As per AS 22, 'Accounting for Taxes on Income', deferred tax in respect of timing differences which originate during the tax holiday period and reverse during the tax holiday period, should not be recognised to the extent deduction from the total income of an enterprise is allowed during the tax holiday period as per the provisions of sections 10A and 10B of the Income-tax Act. Deferred tax in respect of timing differences which originate during the tax holiday period but reverse after the tax holiday period should be recognised in the year in which the timing differences originate. However, recognition of deferred tax assets should be subject to the consideration of prudence. For this purpose, timing differences which originate first should be considered to reverse first.

Out of ₹ 200 lakhs timing difference due to depreciation, difference amounting ₹ 80 lakhs (₹ 10 lakhs x 8 years) will reverse in the tax holiday period and therefore, should not be recognised. However, for ₹ 120 lakhs (₹ 200 lakhs – ₹ 80 lakhs), deferred tax liability will be recognised for ₹ 48 lakhs (40% of ₹ 120 lakhs) in first year.

In the 2nd year, entire amount of timing difference of ₹ 400 lakhs will reverse only after tax holiday period & hence, will be recognised in full. Deferred tax liability amounting ₹ 160 lakhs (40% of ₹ 400 lakhs) will be created by charging it to profit & loss account and total balance of deferred tax liability account at end of 2nd year will be ₹ 208 lakhs (48 lakhs + 160 lakhs).

Question 11 **(Inter Nov 2019) (5 Marks)** Pg no. _____

Sheetal Ltd. has provided the following information for the year ended 31-03-2020:

Particulars	₹
Accounting Profit	9,00,000
Book Profit as per MAT	5,25,000
Profit as per Income Tax Act	95,000
Tax Rate	30%
MAT Rate	7.50%

You are required to calculate the deferred tax asset/ liability as per AS 22 and amount of tax to be debited to the Profit and Loss Account for the year.

Solution

Tax as per accounting profit $9,00,000 \times 30\% = ₹ 2,70,000$
 Tax as per Income-tax Profit $95,000 \times 30\% = ₹ 28,500$
 Tax as per MAT $5,25,000 \times 7.50\% = ₹ 39,375$

Tax expense= Current Tax + Deferred Tax

₹ 2,70,000 = ₹ 28,500+ Deferred tax

Therefore, Deferred Tax liability as on 31-03-2020 = ₹ 2,70,000 – ₹ 28,500 = ₹ 2,41,500

Amount of tax to be debited in Profit and Loss account for the year 31-03-2020

Current Tax + Deferred Tax liability + Excess of MAT over current tax

= ₹ 28,500 + ₹ 2,41,500 + ₹ 10,875 (39,375 – 28,500) = ₹ 2,80,875

Question 12 *(Inter Nov 2020) (5 Marks) / (RTP Nov 2023)*

Pg no. _____

From the following details of Aditya Limited for accounting year ended on 31st March, 2020

Particulars	₹
Accounting Profit	15,00,000
Book Profit as per MAT	7,50,000
Profit as per Income Tax Act	2,50,000
Tax Rate	20%
MAT Rate	7.50%

You are required to calculate the deferred tax asset/ liability as per AS 22 and amount of tax to be debited to the Profit and Loss Account for the year.

Solution

Tax as per accounting profit 15,00,000 x 20% = ₹ 3,00,000

Tax as per Income-tax Profit 2,50,000 x 20% = ₹ 50,000

Tax as per MAT 7,50,000 x 7.50% = ₹ 56,250

Tax expense= Current Tax + Deferred Tax

₹ 3,00,000 = ₹ 50,000+ Deferred tax

Therefore, Deferred Tax liability as on 31-03-2020 = ₹ 3,00,000 – ₹ 50,000 = ₹ 2,50,000

Amount of tax to be debited in Profit and Loss account for the year 31-03-2020

Current Tax + Deferred Tax liability + Excess of MAT over current tax

= ₹ 50,000 + ₹ 2,50,000 + ₹ 6,250 (56,250 – 50,000) = ₹ 3,06,250

Question 13 *(RTP May 2021)*

Pg no. _____

What are the disclosure requirements for deferred tax assets and deferred tax liabilities in the balance sheet as per AS 22?

Solution

The break-up of deferred tax assets and deferred tax liabilities into major components of the respective balance should be disclosed in the notes to accounts. Deferred tax assets and liabilities should be distinguished from assets and liabilities representing current tax for the period.

Deferred tax assets and liabilities should be disclosed under a separate heading in the balance sheet of the enterprise, separately from current assets and current liabilities. The nature of the evidence supporting the recognition of deferred tax assets should be disclosed, if an enterprise has unabsorbed depreciation or carry forward of losses under tax laws.

Question 14 *(RTP Nov 2021)*

Pg no. _____

Can an enterprise offset deferred tax assets and deferred tax liabilities? If yes, prescribe the conditions required for such offset as per provisions of AS 22.

Solution

Yes. It can offset deferred tax assets and deferred tax liabilities.

As per AS 22, an enterprise should offset deferred tax assets and deferred tax liabilities if:

- (i) the enterprise has a legally enforceable right to set off assets against liabilities representing current tax; and
- (ii) the deferred tax assets and the deferred tax liabilities relate to taxes on income levied by the same governing taxation laws.

Question 15 **(RTP May 2019)** Pg no. _____

Is it permissible not to recognize deferred tax liability on the ground that Company expects that there will be losses both for accounting & tax purposes in near future? You are required to give advice to company.

Solution

The Company should provide for deferred tax liability on the timing differences irrespective for the fact that these timing differences will reverse in the period in which the Company expects to be in loss both from the accounting as well as tax point of view. It may, however, be added that the deferred tax liability recognized at the balance sheet date will give rise to future taxable income at the time of reversal thereof.

Question 16 **(Inter Sep 2024) (5 Marks)** Pg no. _____

Delta Ltd. is working on different projects those are likely to be completed within 3 years period. It recognizes revenue from these contracts on Percentage of Completion Method for Financial Statements for the years ending 2021, 2022 and 2023 for ₹ 34 Lakhs, ₹ 50 Lakhs and ₹ 65 Lakhs respectively.

However, for Income Tax purpose, it has adopted the Completed Contract Method under which it has recognized revenue of ₹ 30 Lakhs, ₹ 52 Lakhs and ₹ 67 Lakhs for the years ending 2021, 2022 and 2023 respectively. Income Tax rate is 30%.

Compute the amount of Deferred Tax Asset / Liability and Total Tax Expenses for the years ending 31st March 2021, 2022 and 2023.

Solution

Calculation of Deferred Tax Asset/Liability in Delta Limited

Year	Accounting Income	Taxable Income	Timing Difference	Timing Difference (balance)	Deferred Tax	Deferred Tax Liability (balance)
2021	34,00,000	30,00,000	4,00,000	4,00,000	1,20,000	1,20,000
2022	50,00,000	52,00,000	(2,00,000)	2,00,000	(60,000)	60,000
2023	65,00,000	67,00,000	(2,00,000)	NIL	(60,000)	NIL
	1,49,00,000	1,49,00,000				

Calculation of total tax

Year	Deferred Tax	Current tax expense	Total tax
2021	1,20,000	9,00,000 (30,00,000 x 30%)	10,20,000
2022	(60,000)	15,60,000 (52,00,000 x 30%)	15,00,000
2023	(60,000)	20,10,000 (67,00,000 x 30%)	19,50,000

Note: It is assumed that the revenue and the taxable profit is same.