

**AS 22****Accounting for Taxes on Income****Question 1**

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 resulting in a tax liability in year 1 and 2 is Rs. 1,000 lakhs and Rs. 2,000 lakhs respectively. From the third year it is expected that the timing difference would reverse each year by Rs. 50 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 and Loss account.

**(MTP Oct 19 5 Marks, RTP Nov'18) (Same concept different figures Old & New SM)**

**Answer 1**

As per para 13 of Accounting Standard (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 Rs. 1,000 lakhs depreciation, timing difference amounting Rs. 400 lakhs (Rs. 50 lakhs x 8 years) will reverse in the tax holiday period and therefore, should not be recognized. However, for Rs. 600 lakhs (Rs. 1,000 lakhs - Rs. 400 lakhs), deferred tax liability will be recognized for Rs. 240 lakhs (40% of Rs. 600 lakhs) in first year. In the second year, the entire amount of timing difference of Rs. 2,000 lakhs will reverse only after-tax holiday period and hence, will be recognized in full. Deferred tax liability amounting Rs. 800 lakhs (40% of Rs. 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 Rs. 1,040 lakhs (240 lakhs + 800 lakhs).

**Question 2**

**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?**

**(RTP Nov '21)**

**Answer 2**

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 3**

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

**(b) Depreciation as per books                      Rs. 2,80,000**

**(c) Depreciation for tax purpose                Rs. 1,90,000**

**The above depreciation does not include depreciation on new additions.**



(d) A new machinery purchased on 1.4.18 costing Rs. 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.

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

(f) 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.

What are the disclosure requirements for deferred tax assets and deferred tax liabilities in the balance sheet as per AS 22?  
**(RTP May 21, PYP 5 Marks Nov '22)**

**Answer 3**

**(a) Statement of Profit and Loss for the year ended 31st March, 2019 (Extract)**

		Rs.
Profit before depreciation and taxes		6,40,000
Less: Depreciation for accounting purposes (2,80,000+30,000)		(3,10,000)
Profit before taxes (A)		3,30,000
Less: Tax expense (B)		
Current tax (W.N.1) (3,30,000 x 40%)	1,32,000	(1,32,000)
Deferred tax (W.N.2)		
Profit after tax(A-B)	NIL	1,98,000

**Working Notes:**

**1. Computation of taxable income**

	Amount (Rs.)
Profit before depreciation and tax	6,40,000
Less: Depreciation for tax purpose (1,90,000 + 1,20,000)	(3,10,000)
Taxable income	3,30,000
Tax on taxable income @ 40%	1,32,000

**2. Impact of various items in terms of deferred tax liability / deferred tax asset**

S.No	Transactions	Analysis	Nature of difference	Effect	Amount (Rs.)
(i)	Difference in depreciation	Generally, written down value method of depreciation is adopted under IT Act which leads to higher depreciation in earlier years of useful life of the asset in comparison to later years.	Responding timing difference	Reversal of DTL	(2,80,000 – 1,90,000) x 40% = (36,000)
(ii)	Depreciation on new machinery	Due to allowance of full amount as expenditure under IT Act, tax payable in the earlier years is less.	Timing difference	Creation of DTL	(1,20,000 – 30,000) x 40% = 36,000
	Net impact				NIL



- B. 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 4

(a) Write short note on Timing differences and Permanent differences as per AS 22

(b) Rama Ltd., has provided the following information:

	Rs.
Depreciation as per accounting records	6,00,000
Depreciation as per income tax records	10,00,000
Unamortized 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%.

*(RTP Nov 20, PYP 5 Marks May'18, Old & New SM, PYP 5 Marks May'19)(Same concept different figures May'18, Old & New SM)*

#### Answer 4

(a) Accounting income and taxable income for a period are seldom the same. Permanent differences are those which arise in one period and do not reverse subsequently. For e.g., an income exempt from tax or an expense that is not allowable as a deduction for tax purposes. Timing differences are those which arise in one period and are capable of reversal in one or more subsequent periods. For e.g., Depreciation, Bonus, etc.

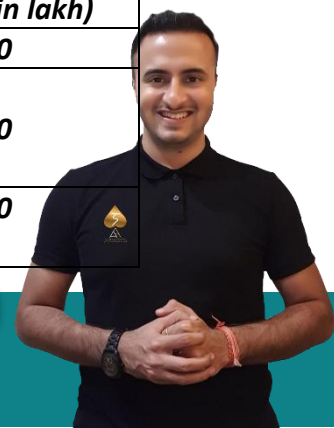
(b) Table showing calculation of deferred tax asset / liability

Particulars	Amount	Timing differences	Deferred tax	Amount @ 30%
	Rs.			Rs.
Excess depreciation as per tax records (Rs. 10,00,000 – Rs. 6,00,000)	4,00,000	Timing	Deferred tax liability	1,20,000
Unamortized preliminary expenses as per tax records	60,000	Timing	Deferred tax asset	(18,000)
Net deferred tax liability				1,02,000

#### Question 5

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

i.	Tax Rate	30%
ii.	Items disallowed in 2019-2020 and allowed for tax purposes in 2020-2021.	(Rs. in lakh) 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.

(RTP May 22)

**Answer 5**

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

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	Rs. 20 lakh X 30% = Rs. 6 lakh
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
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**Question 6**

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

(RTP May 19)

**Answer 6**

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 7**

Define followings as per AS 22:

- Accounting income (loss)
- Taxable income (tax loss)
- Tax expense (tax saving)

**Answer 7**

- Accounting income (loss) is the 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.
- Taxable income (tax loss) is the amount of the income (loss) for a period, determined in accordance with the tax laws, based upon which income-tax payable (recoverable) is determined.
- Taxable expenses is the aggregate of current tax and deferred tax charged or credited to the statement of profit and loss for the period.

**Question 8**

The 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:

- (i) 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. (PYP 5 Marks July 21)

### Answer 8

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, written down value method of depreciation is adopted under IT Act which leads to higher depreciation in earlier years of useful life of the 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 9

The following particulars are stated in the Balance Sheet of HS Ltd. as on 31 -3-2019 :

Particulars	(₹ in lakhs)
Deferred Tax Liability (Cr.)	60.00
Deferred Tax Assets (Dr.)	30.00





<b>The following transactions were reported during the year 2019-20 :</b>	
<b>Depreciation as per accounting records</b>	<b>160.00</b>
<b>Depreciation as per income tax records</b>	<b>140.00</b>
<b>Items disallowed for tax purposes in 2018-19 but allowed in 2019-20</b>	<b>20.00</b>
<b>Donation to Private Trust</b>	<b>20.00</b>
<b>Tax rate</b>	<b>30%</b>

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 31-3-2020 as per AS-22.

(PYP 5 Marks Jan 21, RTP May 20)

### Answer 9

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

- (1) **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 X 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 X 30% = ₹ 6 Lakhs
- (2) **Donations to private trusts** is not an allowable expenditure under IT Act. It is permanent difference. Hence, no reversal of tax is required.

### Question 10

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	7.5%

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.

(PYP 5 Marks, Nov 20) (Same concept different figures RTP Nov'19 & Nov '23, PYP 5 Marks Nov'19, Old & New SM)

### Answer 10

Tax as per accounting profit  $15,00,000 \times 20\% = ₹ 3,00,000$

Tax as per Income–tax Profit  $2,50,000 \times 20\% = ₹ 50,000$

Tax as per MAT  $7,50,000 \times 7.5\% = ₹ 56,250$

Tax expense= Current Tax +Deferred Tax

$₹ 3,00,000 = ₹ 50,000 + \text{Deferred tax}$

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 11**

**Write short note on Timing difference and Permanent Difference as per AS 22. (PYP 5 Marks, May 19)**

**Answer 11**

Matching of taxes against revenue for a period poses special problems arising from the fact that in number of cases, taxable income may be different from the accounting income. The divergence between taxable income may be different from the accounting income arises due to two main reasons: Firstly, there are differences between items of revenue and expenses as appearing in the statement of profit and loss and the items which are considered as revenue, expenses or deductions for tax purposes, known as Permanent Difference. Secondly, there are differences between the amount in respect of a particular item of revenue or expense as recognized in the statement of profit and loss and the corresponding amount which is recognized for the computation of taxable income, known as Timing Difference.

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.

