## TEMPORARY DIFFERENCES

<table>
<thead>
<tr>
<th>DEDUCTIBLE AMOUNTS</th>
<th>TAXABLE AMOUNTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Product warranty liabilities</td>
<td>1. Difference between book basis and tax basis for prepaid insurance</td>
</tr>
<tr>
<td>2. Subscriptions received in advance</td>
<td>2. Excess tax depreciation over book depreciation</td>
</tr>
<tr>
<td>3. Unearned rent revenue</td>
<td>3. Installment sales contract accounted for on cash basis for tax purposes and on accrual basis for book purposes</td>
</tr>
</tbody>
</table>

## PERMANENT DIFFERENCES

1. Interest received on state municipal obligations

2. Premiums paid on officer's life insurance policy; company is beneficiary

3. 70% or 80% dividends received deduction

4. Fines and expenses resulting from violation of law
Annual Procedures

a. Identify (1) the types and amounts of existing temporary differences and (2) the nature and amount of each type of operating loss and tax credit carryforward and the remaining length of the carryforward period.

b. Measure the total deferred tax liability for taxable temporary differences using the applicable tax rate.

c. Measure the total deferred tax asset for deductible temporary differences and operating loss carryforwards using the applicable tax rate.

d. Measure deferred tax assets for each type of tax credit carryforward.

e. Reduce deferred tax assets by a **valuation allowance** if, based on the weight of available evidence, it is *more likely than not* that some portion or all of the deferred tax assets will not be realized. The valuation allowance should be sufficient to reduce the deferred tax assets to the amount that is more likely than not to be realized.
ILLUSTRATION 20-5
PROCEDURES FOR COMPUTING AND REPORTING DEFERRED INCOME TAXES

Identify types and amounts of existing temporary differences and carryforwards.

Measure deferred tax asset for deductible temporary differences and loss carryforwards (Use enacted tax rate)

Measure deferred tax liability for taxable temporary differences (Use enacted tax rate)

Establish valuation allowance account if more likely than not that some portion or all of the deferred tax asset will not be realized.

On the balance sheet
Classify deferred taxes as current or noncurrent based on asset or liability to which they relate.
Report a net current and a net noncurrent amount.

On the income statement
Report current tax expense (benefit) and deferred tax expense (benefit) and total income tax expense (benefit).