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DEFERRED INCOME TAX: IMPACT ON FINANCIAL AND TAX REPORTING (THE PRACTICE OF UKRAINE AND GERMANY)

Abstract. Income taxation is typical for most countries with their own peculiarities. In the practice of the Ukrainian enterprises, there is a lack of relationship between accounting and tax accounting to reflect the deferred tax asset and deferred tax liability in the reporting. The purpose of the article is to analyze the income tax in terms of its calculation by the international standards and identify key tax differences. The authors proposed to formulate the definitions of the current income tax which should be understood as the amount of income taxes payable (reimbursed) on taxable profit (tax loss) for the period and expenses (income) from income tax which should be understood as the total amount included in the determination of profit or loss for the period in accordance with current and deferred taxes. This interpretation of the definitions will help better understand the concepts in accounting and taxation. The tax base of assets and the tax base of liabilities are given and substantiated.

The temporary differences were identified by authors. The example of definition of Deferred tax liabilities and Deferred tax assets, the order of their reflection in the report on financial results (about the total income) and disclosure in the Notes to the financial reporting is considered and analyzed. The impact on the indicators of the Income Tax Return is investigated. There is no direct impact of the amount of the Deferred tax assets / Deferred tax liabilities according to the current algorithm for the object of taxation, which is determined by tax legislation.

The conclusions are made about the importance of determining of Deferred tax liabilities and Deferred tax assets, which directly affects the amount of net profit. The result of the study was confirmation of the hypothesis concerning different orientation of norms of the legal documents on the display of information in the forms of the financial and tax reporting. Such differences are related to the different requirement to the reporting by the modern stakeholders.

Keywords: income tax, deferred tax, tax asset, tax liability, reporting.

JEL Classification M40, M41, M48

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ВІДСТРОЧЕНИЙ ПОДАТОК НА ПРИБУТОК: ВПЛИВ НА ФІНАНСОВУ І ПОДАТКОВУ ЗВІТНІСТЬ (ПРАКТИКА УКРАЇНИ І НІМЕЧЧИНИ)

Анотація. Оподаткування прибутку характерне для більшості країн зі своїми особливостями. У практиці українських підприємств спостерігається відсутність взаємозв'язку бухгалтерського і податкового обліку щодо відображення відстроченого податкового активу і відстроченого податкового зобов'язання у звітності. Запропоновано формулювання дефініцій поточний податок на прибуток, під яким слід розуміти суму податків на прибуток, що підлягають сплаті (відшкодуванню) з оподаткованого прибутку (податкового) збитку за період, і витрати (дохід) з податку на прибуток як загальна сума, що включається до визначення прибутку або збитку за період відповідно до поточних і відстрочених податків з метою більш точного розуміння понять в обліку та оподаткуванні. Наведено та обгрунтовано податкову базу активів і податкову базу зобов'язань.

Проведено ідентифікацію тимчасових різниць, які підлягають оподаткуванню або вирахуванню. Розглянуто і проаналізовано приклад визначення відстроченого податкового активу та відстроченого податкового зобов'язання, порядок їх відображення у Звіті про фінансові результати (звіті про сукупний дохід) і розкриття у Примітках до фінансової звітності. Досліджено вплив на показники Податкової декларації з податку на прибуток. Установлено відсутність прямого впливу суми відстрочених податкових активів / відстрочених податкових зобов'язань за чинним алгоритмом на об'єкт оподаткування, що визначається за податковим законодавством. Зроблено висновки про важливість визначення відстроченого податкового активу і відстроченого податкового зобов'язання, що безпосередньо впливає на величину чистого прибутку. У результаті дослідження було підтверджено гіпотезу стосовно різної спрямованості норм нормативних документів щодо відображення інформації у формах фінансової та податкової звітності. Такі розбіжності пов'язані з різними вимогами до звітності сучасних стейкхолдерів.

Ключові слова: податок на прибуток, відстрочений податок, податковий актив, податкове зобов'язання, звітність.

Формул: 0; рис.: 2; табл.: 5; бібл. 16.

Introduction. Income tax is that part of the business income that is transferable to the state. The tax rules in each country are different, but the information about such payments in the financial reporting of different countries is displayed in the following way: in the statement of financial performance (statement of comprehensive income) — in the accrued tax amount in the reporting period, in the statement of cash flows — paid part of taxes and in the balance sheet (statement of condition) — in the amount of prepaid or unpaid at the balance sheet date, but accrued before tax payment or deferred tax payments.

Income tax payers who have applied the International Accounting Standards are governed by IAS 12 Income Taxes [1], disclosing inter alia in the remarks to the financial reporting, the information on the relationship between the amount of tax calculated under tax rules and reflected in the tax return on the one hand, and the profit of the accounting income (loss) before taxation on the fixed income tax rate. Audit practice shows that not all Ukrainian companies disclose this relationship between accounting and tax accounting because of the complexity of calculating of Deferred Tax Assets and Deferred Tax Liabilities.

Literature review. The problematic issues of accounting for current income tax according to the rules of the Tax Code of Ukraine were covered by the authors K. Bezverkhyi, M. Kotsupatryi, T. Kovtun, and O. Malyshkin [2]. The aspects of deferred tax were professionally researched by the authors S. Golovyi, E. Heyer, S. Zubilevych, O. Karpachova, V. Kostyuchenko, and S. Rogoznyi [3; 4].

Among the foreign scientists, Sara R. Boe [5, p. 309—315] researched the debatable issues of discounting of the deferred income taxes. The scientific article provides a brief overview and analysis of the debatable issues regarding discounting according to GAAP standards. It is concluded that discounting is too burdensome to consider its introduction, and FASB should consider discounting in more detail.

Simplification of the deferred taxes under GAAP standards were investigated by Deanna O. Burgess, Jacqueline R. Conrecode, Adrian Valencia and Ara G. Volkan [6]. The authors as a result of the study propose the methods of accounting for the deferred taxes on the adequate assessment of the financial leverage of the economic entities with a significant deferred tax affecting a balance.

Daniel Halperin & Alvin C. Warren [7] using illustrative examples considered the understanding of income tax deferral. The use of data examples can be the basis for the further research.

The German authors J. Bussik [8], H. Ermann [9] emphasize that provisions for deferred taxes should be seen in connection with the impact of the deferred taxes on income (profit) of the company.

Methodology and Research Methods. The research methodology is based on the use of the International Accounting Standard (IAS) 12 «Income taxes». Also the methods of general knowledge, induction and deduction were used in the study and analysis of current and deferred income taxes. The method of the mathematical calculation and graphical representation of calculation results in the form of tables was used for calculation of DTA and DTL.

Results. The accounting rules, including those defined under IFRS, do not always fully comply with a country's tax laws. Tax legislation in Ukraine, as in many other countries, is no exception and also has certain features. In some cases, the differences can be quite significant and there is a need for significant adjustments in accounting income to provide a basis for calculating income taxes. In this case, the concept of temporary and permanent differences arises, which can significantly affect the financial reporting. Against this background, the international financial reporting standards focus on accounting for current and future tax consequences.

Profit before tax can be considered in two aspects: accounting and tax. The accounting approach to income tax, including current and deferred tax issues, is addressed in IAS 12 [1]. The companies that apply national accounting standards continue to be guided by the provisions of Accounting Regulations (Standards) 17 [10], which is a simplified and somewhat outdated analogue to the international one [1].

The complexity of this issue is due to the fact that tax differences often result in different amounts of income tax in the tax return and income tax expense reflected in the statement of financial performance. This is usually due to the fact that:

- 1) not all income (or expenses) can be taken into account for tax purposes;
- 2) income (expenses) are included in accounting profit of one period, and in tax calculations — in another;
- 3) company may have tax benefits;
- 4) there are differences in the formation of reserves depending on accounting and tax approaches;
- 5) different methods of writing off the cost of assets are used; and
- 6) assets are revalued and no adjustment is made for tax purposes.

In view of the above, it is necessary to understand such concepts as current income tax and expenses (income) from income tax (*Fig. 1*).

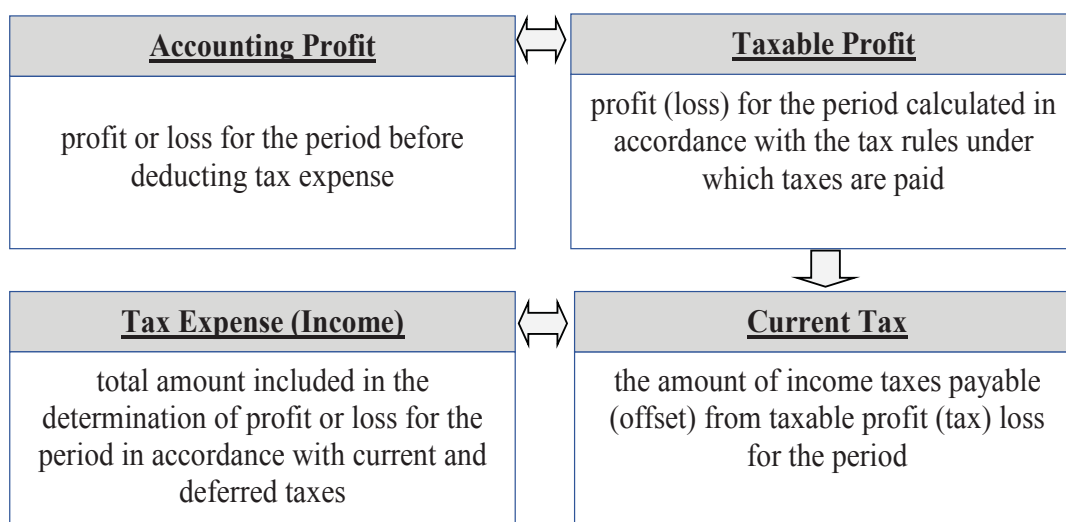


Fig. 1. Definition of Key Concepts

Source. Developed by the authors.

Thus, tax expenses include both current and deferred taxes. In turn, deferred tax allocations allow us to account for temporary differences between the tax and accounting bases of assets and liabilities. The deferred tax mechanism, on the one hand, allows for an even distribution of income and expenses and, on the other, avoids lowering the amounts of the liabilities and expenses and overstating assets and revenues.

It should be noted that in order to calculate income tax, it is important to determine their tax base in addition to the carrying amount of assets and liabilities. It is clear that the carrying amount is the amount at which an asset (liability) is recorded in the statement of condition. And the tax base is the amount used for taxation purposes of the asset or liability (Fig. 2).

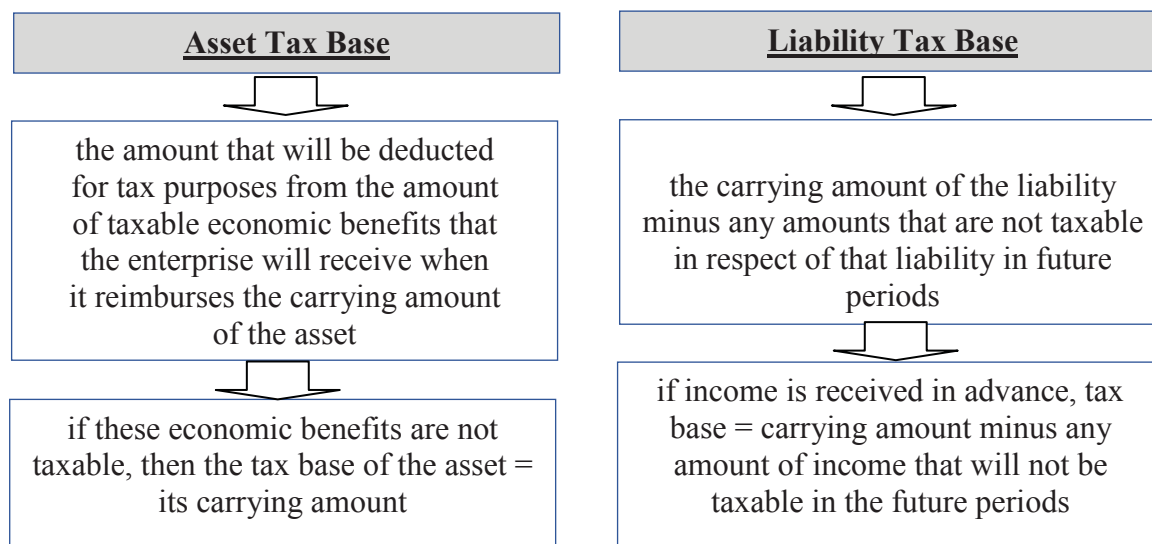


Fig. 2. Assets and Liabilities Tax Base

Source. Developed by the authors based on [1].



Under IFRS, the concept of temporary difference arises as a result of differences in the amount of the tax base and the corresponding carrying amount of an asset or liability. The temporary differences can be of two types:

- 1) Those subject to taxation;
- and 2) Those subject to deduction [2, p. 13].

These differences result in the occurrence of the deferred tax assets or deferred tax liabilities (Table 1).

Table 1

Identification of Temporary Differences

	Difference subject to taxation	Difference subject to deduction
<i>For assets</i>	Carrying Amount of Assets > Tax Base of Assets	Carrying Amount of Assets < Tax Base of Assets
<i>For liabilities</i>	Carrying Amount of Liabilities > Tax Base of Liabilities	Carrying Amount of Liabilities > Tax Base of Liabilities
<i>Taxable profit in the future</i>	Increases	Decreases
		
<i>Occur</i>	<i>Deferred tax liabilities (DTL)</i>	<i>Deferred tax assets (DTA)</i>

Source. Developed by the authors.

When an entity recovers the carrying amount of an asset, the temporary difference that is taxable is reversed. As a result, the company will have taxable profit. This causes loss of economic benefit to the company in the form of tax payments [3, p. 624].

There are several fundamentally important points in this situation:

a) entity recognizes DTL (DTA) if the reimbursement or redemption of the carrying amount of an asset or liability would increase (decrease) future tax payments compared to what they would have been if such reimbursements or redemption had no tax consequences;

b) DTL should not be recognized in situations where taxable differences arise from the initial recognition of goodwill, as well as from the initial recognition of an asset or liability in a transaction that is not a business combination and has no influence on either accounting or on taxable income;

c) current tax for the current and previous periods is recognized at the reporting date as a liability for the amount not paid;

d) if the amount of taxes paid for the current and previous periods exceeds the amount payable for those periods, the excess should be recognized as an asset;

e) receivables and payables on income tax, in accordance with IAS 1 [11], are mentioned in the Statement of Condition as a separate item of current assets or liabilities;

f) benefit associated with the tax loss that can be deducted to offset current tax in the reporting period is also recognized as an asset;

g) if a tax loss is used to offset current tax of a previous period, the company recognizes the benefit as an asset in the period in which the tax loss arose because it is probable to get the benefit and it can be measured reliably;

h) DTL (DTA) related to the investments in subsidiaries, associates, branches, interests in joint ventures are recognized in all situations except where two conditions are met: 1) the parent company or investor is able to control the timing of the reversal of the temporary difference and 2) it is probable that the temporary difference will not be reversed in the foreseeable future;

i) current tax liabilities (assets) should be estimated at the amount that is expected to be paid (or reimbursed) to the tax authorities, using tax rates that remain in force up to the end of the reporting period;

g) DTL and DTA are not discounted;

and k) Company should review the carrying amount of the assets at the end of each reporting period [4].

In domestic practice, the key rules on corporate income taxation are contained in section III of the Tax Code of Ukraine (TCU), which defines the main differences on which companies should adjust their financial performance in order to further calculation of income tax. There are three main groups of time differences:

1) Differences related to the accrual of the depreciation of fixed assets;

2) Differences arising in the formation of reserves (securities);

and 3) Differences related to financial transactions [4].

These differences exist autonomously from tax differences under the accounting standards and do not participate in formation of the financial statements.

An example of the definition of DTL and DTA. Consider the specific features of the definition of DTL and DTA on the example and how they relate to current expenses to pay tax. A simplified statement of condition of the company before taking into account the deferred taxes is given in *Table 2*.

Table 2

Statement of condition as of December 31, 2018

Assets	Amount	Capital and Liabilities	Amount
Fixed assets	450 000	Equity	400 000
Financial investments	50 000	Undivided profit	40 000
Total fixed assets	500 000	Total capital:	440 000
Stocks	100 000		
Receivables	350 000	Bank loans	220 000
Cash and cash equivalents	50 000	Payables	340 000
Total current assets	500 000	Total liabilities	560 000
Total	1 000 000	Total	1 000 000

Source. Compiled by the authors.

Suppose that on January 1, 2019, production equipment was purchased, it was depreciated by a production method economically feasible, given the nature of its use. However, the straight-line method is used for tax purposes. The residual value of fixed assets if the straight-line method were used as of December 31, 2019 would be 480,000 thousand UAH. Receivables are reflected in the statement of condition minus the reserve in the amount of 15,000 thousand UAH. Expenses for the formation of a reserve are not recognized for tax purposes. We define the DTA and DTL provided that the income tax rate is 18%. *Table 3* contains articles related to temporary differences.

Table 3

Calculation of DTA and DTL

Article	Carrying Amount	Tax Base	Temporal Difference	DTA (DTL)
Fixed assets	450 000	448 240	(1 760)	(316)
Financial investments in equity instruments	50 000	41 730	(8 270)	(1 488)
Receivables	350 000	350 140	140	25
Total	X	X	(9 890)	(1 779)

Source. Compiled by the authors.

With respect to the closing-up of DTA and DTL, the company may do so under the following conditions:

- 1) There is a legally guaranteed right to do so;

and

- 2) DTA and DTL refer to income taxes administered by the same tax authority to the same company or to other entities that are subject to tax and intend to repay DTA and DTL on a net basis or realize an asset with a simultaneous redemption of liabilities in each future period, in which the repayment (reimbursement) of significant DTA and DTL is foreseen [6].

The components of DTA and DTL are determined by comparing two contiguous years, which is shown in *Table 4*.

Table 4

Components of Deferred Tax Assets and Liabilities

	Indexes	C2	Recognized	Recognized	CI
		31.12.2019	in revenue (expense)	in OCI	01.01.2019
2019	Deferred tax assets				
	Trade receivables	25	(51)	-	76
	Stocks		(14)	-	14
	Counter enrollment from the DTL	(25)	65	-	(90)
	Total DTA:				
	Deferred tax liabilities		-	-	-
	Fixed assets	(316)	294	-	(610)
	Financial investments in equity instruments	(1488)	-	(239)	(1249)
	Counter enrollment from the DTA	25	(65)	-	=90
	Total DTL	(1779)	229	(239)	=(1769)

	Indexes	31.12.2018	Recognized	Recognized	01.01.2018
			in revenue (expense)	in OCI	
2018	Deferred tax assets				
	Trade receivables	76	19	-	57
	Stocks	14	(46)	-	60
	Counter enrollment from the DTL =	(90)	27	-	(117)
	Deferred tax liabilities	-	-	-	-
	Fixed assets	(610)	3	-	(613)
	Financial investments in equity instruments	(1249)	-	320	(1569)
	Counter enrollment from the DTA	90	(27)	-	117
	Total DTL	(1769)	(24)	320	(2065)

Expense

1

Income tax. Transcript of line 2300 of the Statement of comprehensive income

Income tax-expense components for the year ended on December 31, 2019 are as follows:

Line 2300	Indexes	2019	2018
	Current income tax expense		2823
Deferred income tax expense (revenue)		(229)	+24
Total income tax as a part of expenses for the period		2594	4021
Deferred tax related to the items recognized as a part of comprehensive income during the year		+239	(320)
		=2833	=3701

Source. Compiled by the authors under [3].

In practice, the areas of presentation of the deferred taxation should be divided: if transactions and events are recognized in profit or loss, then related current and deferred taxes are expenses (incomes) and are also recognized in profit/loss. If, however, transactions and events are

recognized outside profit/loss, similarly, tax effects are recognized in other comprehensive income or directly in equity.

Reflection of DTA/DTL in the statement of financial performance (cumulative income).

The result of the DTA/DTL calculations as expenses or income should be reflected in the statement of financial performance (statement of comprehensive income). For this purpose line 2300 is provided in the forms approved by the Ministry of Finance for use in Ukraine [12]. The records under the account 98 Income Tax are used. The positive amount of the calculation of the deferred taxes means expenses, negative one means revenue. In our example for 2018, UAH 24,000 of the expense from deferred tax was recorded. Taking into account the current accruals in the tax return (3997 thousand UAH), the total amount of expenses to be reflected in the statement of financial performance (4021 thousand UAH) was formed. Transactions through other comprehensive income (revaluation of financial investments) resulted in recognition of 320 thousand UAH as part of other comprehensive income. Thus, the cumulative income of 2018 was reduced by 3701 thousand UAH of tax.

The calculation according to the similar rules for 2019 gives the amount of deferred tax income through profit-loss (financial result) 229 thousand UAH and 239 thousand UAH expenses as part of other comprehensive income. Together with current expenses, 2833 thousand UAH of expenses was formed. These results are displayed by year in line 2300 of the report (*Table 5*).

Table 5

Statement of financial performance (statement of comprehensive income)

I. FINANCIAL RESULTS

Indicator	Code	2019	2018
...			
Financial result before tax:			
Profit	2290	16306	19479
Loss	2295	(-)	(-)
Expense (revenue) from income tax	2300	(2594)	(4021)
Profit (loss) from discontinued operations after tax	2305	-	-
Net financial result:			
Profit	2350	13712	15458
Loss	2355	(-)	(-)

II. COMPREHENSIVE INCOME

Article	Line code	2019	2018
...			
Final appraisal (markdown) of financial instruments	2405	1330	(1780)
...		-	-
Other comprehensive income (loss) before tax	2450	-	-
Income tax related to other comprehensive income/loss	2455	(239)	320
Other comprehensive income (loss) after tax	2460	1091	(1460)
Cumulative income (loss) (the sum of lines 2350, 2355 and 2460)	2465	14803	13998

Source. Developed by the authors.

In the domestic report form, this data should be given in full form. However, IFRS encourage the deployment of this parameter on the current period expense (income) and expense (income) from the deferred income tax in the notes. As a result, the analytical nature of the report increases significantly.

Impact of DTA and DTL on the parameters of the tax return. The Ministry of Finance of Ukraine defines the form of the corporate income tax return. Some changes are also made periodically and other forms of tax returns provided by law are used for other categories of payers.

The terms and procedure for filing the tax return to the tax authority are specified in Article 49 of TCU (for example, under the results of 2018 the tax return shall be submitted no later than March 1, 2019, and income tax was to be paid not later than March 11, 2019).

The object of taxation is listed in line 04 of the corporate income tax return. Its sum is formed from the sums of lines 02 Financial Result before Tax (p. 2290 / 2295 f. № 2) and 03 Tax Differences (according to the TCU). Therefore, according to this algorithm, the amounts of the DTA / DTL do not directly affect the object of taxation, which is determined by tax law [16]. We can only speak of indirect impact through the indicator Financial Result Before Tax. From this we conclude that the methodology of calculations and accounting of DTA/DTL is relevant to the financial accounting and, accordingly, the financial reporting and is not provided by the tax legislation of Ukraine.

Reflection in accounting. O. V. Soloviov [13, p. 12—18] proposes to build accounting records in accordance with the Accounting Regulations (Standards) 17 Income Tax in the following sequence:

- 1) Current income tax accrual is shown based on the Income Tax Return.
- 2) Deferred tax liabilities and deferred tax assets for the reporting period in the analytical accounting by their types are accrued.
- 3) DTA and DTL of the previous reporting periods in the analytical accounting by their types based on balances on the accounts 17 Deferred Tax Assets and 54 Deferred Tax Liabilities are repaid or adjusted.
- 4) Balances on the accounts 17 Deferred Tax Assets and 54 Deferred Tax Liabilities, which are not closed-up in the analytical accounting, are displayed.
- 5) Consolidated information on accounts 17 and 54, the turnover of which is recorded in the receipt journal, are compiled; and
- 6) Deferred tax liabilities and deferred tax assets are closed-up in synthetic accounting and at the end of the reporting period there remains: either a debit balance on account 17 Deferred Tax Assets or a credit balance on account 54 Deferred Tax Liabilities, which are reflected in balances [13, p. 16].

At the end of the year, the DTA / DTL in the form of tax differences are to be recorded as income or expense from income tax. Expenses are debited to the subaccount 981 Income Tax on Ordinary Activities.

According to the instructions of the Ministry of Finance of Ukraine dated September 25, 2009, № 1125, income from income tax should be recorded not on credit of account 98, but on credit of account 74 Other Income [10].

In an accounting policy order, it is advisable to mention the allocation of a certain subaccount, for example, 747 Income Tax Revenue and use its data as well as account information 98 to be reported.

Disclosures in the Notes to the Financial Reporting. A company shall disclose separately in the Notes to the financial reporting the following major components of tax expense (or income): a) current tax expenses (income), as well as any adjustments to the previous periods; b) amount of deferred tax expense (income) associated with 1) tax differences reversing; and 2) changing tax rates or introducing new taxes; c) amount of the profit from the unrecognized loss (privilege or temporary difference) of the previous period, which is used in the current period to reduce current tax expenses, and separately — to reduce deferred tax expenses; d) deferred tax expense associated with the write-off or reverse of a prior write-off of a deferred tax asset; and e) amount of tax expense (income) associated with changes in accounting policies and errors included in net income (loss) in accordance with IAS 8 [1; 14].

In addition, the company must disclose the following information:

- 1) Cumulative current and deferred tax related to equity items.
 - 2) Amount of income tax in the context of each component of other comprehensive income;
- and 3) Explanation of the relationship between tax expenses (income) and accounting income, etc. [14; 15].

The practice of creating reserves from deferred income taxes in Germany. The company's income taxes are set on the basis of the German tax law. In practice, the trading result is often different from the tax one. Therefore, one do not need to see any logical relationship between the result of the trade balance and income tax. This discrepancy can be eliminated only when taxes

are also calculated on the basis of the trading results and receive the amount of so-called fictitious tax expense. The difference between it and the taxes paid effectively results in a deferred income tax. This difference can be positive or negative. The difference is positive if the contingent tax expense is higher than the actual tax expense. On the contrary, there is a negative difference if the actual tax costs are higher than the conditional tax costs. Thus, the German term «fictitious tax expenses» corresponds to the concept of income tax expenses in the financial statements.

The German Commercial Code (HCB), as a regulatory legal act on accounting, requires companies to create a reserve and reflect it in the balance sheet under certain conditions. Thus, according to § 274 HCB, a reserve in the amount of the estimated tax burden for the next financial year can be created if the tax expenses for the reporting year are lower than the result in the financial statements. At the same time they are guided § 249 HCB. Such article is specified separately in the balance sheet or in the appendix. The provision should be eliminated as soon as the amount of the tax burden is too high or no longer required.

The German practice provides for the differentiation of the tax expenditures between the reporting and the previous year. If the profit in the financial statements is higher than the profit in the tax return, the amount of the estimated tax burden in subsequent years forms a distinction as an ancillary to the consolidation of the balance sheet on the asset side. The amount of the asset must be cancelled if the opposite situation occurs [8].

The accounting actions for the formation and use of the reserve is as follows:

1. When forming a reserve:

D-t Deferred tax asset / K-t Deferred tax reserve

2. When using the reserve:

D-t Deferred tax reserve / K-t Deferred tax income

Conclusions. Therefore, it is extremely important for the company to correctly and timely identify DTA and DTL as it provides indication of adjusted income tax in a statement of financial performance that directly affects the net income value. However, practice shows that most companies in Ukraine do not burden themselves with such calculations, because their amount does not directly affect the tax return.

From a methodological point of view, the interaction of the tax and accounting legislation is important, which directly affects the relationship between financial and tax reporting indicators. The study confirmed the hypothesis of the different orientations of the norms of these standards, which is explained by the requirements of different users of reporting.

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