

Exercise 16-28

Case Development began operations in December 2021. When property is sold on an installment basis, Case recognizes installment income for financial reporting purposes in the year of the sale. For tax purposes, installment income is reported by the installment method. 2021 installment income was \$600,000, and will be collected over the next three years. Scheduled collections and enacted tax rates for 2022-2024 are as follows:

| | | |
|------|-----------|-----|
| 2022 | \$140,000 | 20% |
| 2023 | 260,000 | 25% |
| 2024 | 200,000 | 25% |

Pretax accounting income for 2021 was \$810,000, which includes interest revenue of \$10,000 from municipal bonds. The enacted tax rate for 2021 is 20%.

© Dr. Chula King
All Rights Reserved

Exercise 16-28 (continued)

Part 1: Assuming no differences between accounting income and taxable income other than those described above, prepare the appropriate journal entry to record Case's 2021 income taxes.

| | | |
|---|-----------|------------------|
| Pretax accounting income (given) | | \$810,000 |
| Deduct: Permanent difference – municipal bond interest | (10,000) | |
| Pretax accounting income subject to tax | | \$800,000 |
| Temporary difference: | | |
| Installment income (taxable when collected) | (600,000) | |
| Taxable income | | <u>\$200,000</u> |
| Deferred tax liability: (20% x \$140,000) + (25% x \$260,000) + (25% x \$200,000) = \$143,000 | | |
| Tax expense (plug) | 183,000 | |
| Deferred tax liability (computed above) | | 143,000 |
| Taxes payable (20% x 200,000) | | 40,000 |

© Dr. Chula King
All Rights Reserved

Exercise 16-28 (continued)

Part 2: What is Case's 2021 net income?

| | |
|--------------------------|------------------|
| Pretax accounting income | \$810,000 |
| Less: Tax expense | (183,000) |
| Net income | <u>\$627,000</u> |

© Dr. Chula King
All Rights Reserved
