Discussion of Teaching Reform about Income Tax on Basis of the Convergence of Accounting Standards

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ABSTRACT

For Chinese companies that are playing an increasingly global role, the acceptance of the new standards should also reduce the cost of complying with the accounting regimes of different jurisdictions in which they operate. For advanced course of accounting education, the benefits of these accounting reforms for China are clear. [1] The objective of this Standard teaching is to prescribe the accounting treatment for income taxes. Teaching reform is designed to meet the needs of those students who work in the accounting field or who are presently employed and want to complete additional accounting courses beyond the diploma level.

Key Words: income taxes; new accounting standards; teaching Reform; Convergence

INTRODUCTION

World economy globalization highlighted with deregulation of trade, capital movement and financing has been the dominant trend under the push of rapid growing of modern information technology, creating an urgent demand for internationalized accounting standards.[2]

The Ministry of Finance People's Republic of China ("MoF") issued on 15 February 2006 new accounting standards for Business Enterprises - Chinese Accounting Standards ("CAS"). The MoF has now brought 39 Chinese accounting standards closer in-line with international practice. The revised standards will be first applied to listed companies starting from 1 January 2007 and then gradually to other types of entities. The revised standards for Chinese enterprises have now largely converged with International Financial Reporting Standards ("IFRS"). China's central-level State-Owned Enterprises (SOEs) and large to mid-scale companies will all adopt China's new accounting standards that comply with the International Financial Reporting Standards (IFRS) by the end of 2009. The MOF will also speed up the construction of an internal control system on accounting to ensure the credibility of accounting information released by the enterprises.

For advanced course of accounting education, the benefits of these accounting reforms for China are clear. The new Chinese standards that incorporate accounting principles familiar to investors worldwide will encourage investor confidence in China's capital market and financial reporting, and will be an additional spur for investment from both domestic and foreign sources of capital. [3]

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[1] As reported by the Embassy of the People's Republic of China in the United States of America, http://www.china-embassy.org/eng/gyzg/t340049.htm

[2] Internationalization of Accounting Standards – L Shuyun

[3] China's new accounting standards to be adopted, www.chinaview.cn,

As technology continues to evolve, accounting professionals will be expected to keep pace. Theory and applications of accounting for business combinations, income tax, branches and segments, partnerships, and foreign currency transactions and translations topics are covered in. the course of advanced accounting. So this course will cover accounting for a view to regulating the recognition and measurement of enterprise income taxes and the presentation of relevant information.

CHAPTER OF INCOME TAX TEACHING IN THE COURSE OF ADVANCED ACCOUNTING

The course of advanced accounting is designed for undergraduate students majoring in accounting and auditing. It is arranged in the fourth or fifth semester. It is aimed to enhance students' ability both in western accounting knowledge and professional English, and to improve their competition for their job in all kinds of companies.

For Chinese companies that are playing an increasingly global role, the acceptance of the new standards should also reduce the cost of complying with the accounting regimes of different jurisdictions in which they operate.[4]

China's listed companies adopted the new Chinese accounting standards at the beginning of 2007. The standards, including 39 specific principles for corporate accounting, are much closer to international practices.[5] Accounting Standards for Enterprises No.18 - Income Taxes are converged with IFES.

FOCUS ON THE CHANGES OF INCOME TAX ACCOUNTING STANDARDS

The original accounting system required an enterprise to account for deferred tax using either the deferral method or a liability method which is sometimes known as the income statement liability method. The Accounting Standards for Enterprises No.18 - Income Taxes prohibits the deferral method and requires another liability method which is sometimes known as the balance sheet liability method.

The income statement liability method focuses on timing differences, whereas the balance sheet liability method focuses on temporary differences. Timing differences are differences between taxable profit and accounting profit that originate in one period and reverse in one or more subsequent periods. Temporary differences are differences between the tax base of an asset or liability and its carrying amount in the balance sheet. The tax base of an asset or liability is the amount attributed to that asset or liability for tax purposes.

The original accounting system permitted an enterprise not to recognise deferred tax assets and liabilities where there was reasonable evidence that timing differences would not reverse for some considerable period ahead. Income Taxes Accounting Standards requires an enterprise to recognise a deferred tax liability or (subject to certain conditions) asset for all temporary differences, with certain exceptions noted below.

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[4] Ibid

[5] Ibid

The original accounting system required that:

- Deferred tax assets arising from timing differences should be recognised when there was a reasonable expectation of realisation

- Deferred tax assets arising from tax losses should be recognised as an asset only where there was assurance beyond any reasonable doubt that future taxable income would be sufficient to allow the benefit of the loss to be realised. The original accounting system permitted (but did not require) an enterprise to defer recognition of the benefit of tax losses until the period of realisation.

Income Taxes Accounting Standards requires that deferred tax assets should be recognised when it is probable that taxable profits will be available against which the deferred tax asset can be utilised. Where an enterprise has a history of tax losses, the enterprise recognises a deferred tax asset only to the extent that the enterprise has sufficient taxable temporary differences or there is convincing other evidence that sufficient taxable profit will be available.

The original accounting system required that taxes payable on undistributed profits of subsidiaries and associates should be recognised unless it was reasonable to assume that those profits will not be distributed or that a distribution would not give rise to a tax liability. However, Income Taxes Accounting Standards prohibits the recognition of such deferred tax liabilities (and those arising from any related cumulative translation adjustment) to the extent that:

- The parent, investor or venturer is able to control the timing of the reversal of the temporary difference

- It is probable that the temporary difference will not reverse in the foreseeable future. Where this prohibition has the result that no deferred tax liabilities have been recognised, Income Taxes Accounting Standards requires an enterprise to disclose the aggregate amount of the temporary differences concerned.

- The original accounting system did not refer explicitly to fair value adjustments made on a business combination. Such adjustments give rise to temporary differences and Income Taxes Accounting Standards requires an entity to recognise the resulting deferred tax liability or (subject to the probability criterion for recognition) deferred tax asset with a corresponding effect on the determination of the amount of goodwill or any excess of the acquirer's interest in the net fair value of the acquirer's identifiable assets, liabilities and contingent liabilities over the cost of the combination. However, Income Taxes Accounting Standards prohibits the recognition of deferred tax liabilities arising from the initial recognition of goodwill.

So the income statement liability method focuses on timing differences, whereas the balance sheet liability method focuses on temporary differences. Timing differences are differences between taxable profit and accounting profit that originate in one period and reverse in one or more subsequent periods. Temporary differences are differences between the tax base of an asset or liability and its carrying amount in the balance sheet. The tax base of an asset or liability is the amount attributed to that asset or liability for tax purposes.

- **Objective of Income Tax Accounting Standards Teaching**

The objective of this Standard teaching is to prescribe the accounting treatment for income taxes. The principal issue in accounting for income taxes is how to account for the current and future tax consequences of:

- Transactions and other events of the current period that are recognised in an enterprise's financial statements; and

- The future recovery (settlement) of the carrying amount of assets (liabilities) that are recognised in an enterprise's balance sheet.

It is inherent in the recognition of an asset or liability that the reporting enterprise expects to recover or settle the carrying amount of that asset or liability. If it is probable that recovery or settlement of that carrying amount will make future tax payments larger (smaller) than they would be if such recovery or settlement were to have no tax consequences, this Standard requires an enterprise to recognise a deferred tax liability (deferred tax asset), with certain limited exceptions.

This Standard requires an entity to account for the tax consequences of transactions and other events in the same way that it accounts for the transactions and other events themselves. Thus, for transactions and other events recognised in profit or loss, any related tax effects are also recognised in profit or loss. For transactions and other events recognised directly in equity, any related tax effects are also recognised directly in equity. Similarly, the recognition of deferred tax assets and liabilities in a business combination affects the amount of goodwill arising in that business combination or the amount of any excess of the acquirer's interest in the net fair value of the acquirer’s identifiable assets, liabilities and contingent liabilities over the cost of the combination.

This Standard also deals with the recognition of deferred tax assets arising from unused tax losses or unused tax credits, the presentation of income taxes in the financial statements and the disclosure of information relating to income taxes.

TEACHING REFORM ENVIRONMENT: THE CONVERGENCE OF ACCOUNTING STANDARDS

The environment for accounting education has totally changed and certain new challenges have emerged in this regard. The WTO reforms call for restructuring of the service sector including the accounting services. Therefore accounting education needs to be given due attention in this emerging scenario. The Information technology and the Globalization of Markets are the two other major governing factors impacting various changes in the accounting education. It is also important to mention here that world regions and countries vary in terms of the stage of the development of the accounting education in tune with their economic systems. Hence a great deal of attention needs to be given to customizing the broad educational needs of the accountancy profession keeping in view this factor.

Teaching reform is designed to meet the needs of those students who work in the accounting field or who are presently employed and want to complete additional accounting courses beyond the diploma level. If a company does not recognize a tax liability, then the accountant

should disclose the temporary differences, at a summary level, for which no tax liability is recorded, as well as those circumstances under which a liability would be recorded. The accountant should also list any permanent unrecognized tax liabilities related to investments in foreign entities.

The accountant should itemize the amount of any net operating loss carry forwards and related credits, as well as the dates on which they expire. In addition, one should present a reconciliation of the statutory tax rate to the actual rate experienced by the organization during the reporting period, though privately held entities can restrict this reporting to a description of the general types of reconciling items.

The amounts of the following items related to income taxes must be attached to the income statement or reported within it:

- Any investment tax credit.
- Changes in tax assets or liabilities caused by changes in valuation estimates.
- Changes in tax assets or liabilities caused by regulatory changes.
- Net operating loss carry forwards.
- Tax-reducing government grants.
- The current tax expense.
- The deferred tax expense.

There are some innovation in the new Accounting Standards, such as some new standards which provide guidance for some special transactions and industries, some new accounting principles and measurement requirements. Because the new Accounting Standards for Business Enterprises ("ASBEs") cover nearly all of the topics under the current International Financial Reporting Standards ("IFRSs") literature , the issuance and implementation of new ASBEs realizes the substantial convergence of Chinese Accounting Standards for Business Enterprises with the IFRSs, making the beginning of a new era. It makes huge differences between the accounting regulations and practices before 2007 and the new ASBEs, and in some areas, it can be called as a great Innovation in China.

TEACHING REFORM METHODS

This course mainly adopts lecture in class, with the help of multimedia. We also allocate some presentations after group discussion out of classroom. It is taught either in English or in the combination of both English and Chinese.

- **The Case of Teaching**

    For example, current tax liabilities (assets) for the current and prior periods should be measured at the amount expected to be paid to (recovered from) the taxation authorities, using the tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date.

    Deferred tax assets and liabilities should be measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date.

    An asset with a cost of 100 and a carrying amount of 80 is revalued to 150. No

equivalent adjustment is made for tax purposes. Cumulative depreciation for tax purposes is 30 and the tax rate is 30%. If the asset is sold for more than cost, the cumulative tax depreciation of 30 will be included in taxable income but sale proceeds in excess of cost will not be taxable.

The tax base of the asset is 70 and there is a taxable temporary difference of 80. If the enterprise expects to recover the carrying amount by using the asset, it must generate taxable income of 150, but will only be able to deduct depreciation of 70. On this basis, there is a deferred tax liability of 24 (80 at 30%). If the enterprise expects to recover the carrying amount by selling the asset immediately for proceeds of 150, the deferred tax liability is computed as follows in (Figure 1)

	Taxable Temporary Difference	Tax Rate	Deferred Tax Liability
Cumulative tax depreciation	30	30%	9
Proceeds in excess of cost	50	nil	-
Total	80		9

Figure 1: Outlines the bases and resulting rules upon which one should account for income taxes, focusing on an asset and liability approach to the presentation of income tax information.

- **The Comparison of Teaching**

  All timing differences are temporary differences. Temporary differences also arise in the following circumstances, which do not give rise to timing differences, although the original accounting system treated them in the same way as transactions that do give rise to timing differences:

- Subsidiaries, associates or joint ventures have not distributed their entire profits to the parent or investor;
- Assets are revalued and no equivalent adjustment is made for tax purposes; and
- The cost of a business combination is allocated to the identifiable assets acquired and liabilities assumed by reference to their fair values, but no equivalent adjustment is made for tax purposes.

Furthermore, there are some temporary differences which are not timing differences, for example those temporary differences that arise when:

- The non-monetary assets and liabilities of an entity are measured in its functional currency but the taxable profit or tax loss (and, hence, the tax base of its non-monetary assets and liabilities) is determined in a different currency;
- Non-monetary assets and liabilities are restated under IAS 29, Financial Reporting in Hyperinflationary Economies; or
- The carrying amount of an asset or liability on initial recognition differs from its initial tax base.

- **Exam Form and Requirements**

  After finishing the course, the exam will be tested in English, no matter that the course is taught in English or in combination with both English and Chinese. Normally, the exam adopts the close book test, if applied and allowed by the officers, it could be tested in another form according to the situation.

  The formats of the final exam paper include multiple choice, translation both from English to Chinese and from Chinese to English , identification of true or false, case analysis writing, making journal entries, calculation, preparation of the worksheet for the financial statements, preparation of balance sheet, income statement and cash flow statements, and the analysis of the financial statements, etc.

  It adopts a 100% scoring system. The final score consists of two parts, one is the score of the final exam, the other is the score of daily performance, which includes assignment/s, attendance and discussion performance etc. The proportion of the two parts depends on the requirement of the university.

CONCLUSION

Income Tax accounting education in certain developed countries has undergone a paradigm shift in tune with the changing global economic environment. The environment of accounting in the various developing economies has also changed and certain new challenges have emerged. Hence the accounting education and profession should not be neglected in this scenario.

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