Do the Deferred Tax Liabilities Have Substance? Perception of Australian Practicing Auditors

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Abstract

This study examines whether the provision for deferred income tax (PDIT) is perceived by the auditors as a liability of substance. To this end a survey of Australian auditors was undertaken based on the concept of liabilities as stated in the Statement of Accounting Concepts (SAC) 4. The results based on a sample of one hundred and seventy-six auditors showed that a majority of them do not consider PDIT as a liability of substance. But a majority is in favour of recognising and disclosing it in the balance sheet as a deferred credit. The findings have implications in the context of the current review of the standard in the area of tax effect accounting in Australia and overseas.

Introduction

The present study examines the auditors' perception of provision for deferred income tax (PDIT) as a liability. The major aim of the study is to ascertain whether auditors consider the PDIT as a liability as per the definition and recognition criteria outlined in Statement of Accounting Concepts (SAC) 4 Definition and recognition of the Elements of Financial Statements (AARF 1995).

This study is important for the following reasons. Firstly, to our knowledge this is the first attempt at empirically ascertaining the attitude of auditors toward PDIT. Secondly, it sheds further light on the debate on the issue of tax effect accounting (TEA) and more particularly on the status of PDIT. Finally, the empirical findings of the study will be of relevance to reviewing the Accounting standard on tax allocations in Australia and overseas.

The remainder of the paper is organised along the following lines. We review prior research on TEA both at a priori and empirical levels. This is followed by an examination of the role of auditors in relation to TEA. The next section outlines the data sources and sample selection and discusses the questionnaire used for this study. Then the results of the survey are reported followed by an analysis of those results. The final section provides conclusions of the study.

II. Prior Research

The debate over TEA has been going on since the 1940s defying any permanent resolution. at an *a priori* level arguments for TEA have been advanced by among others. Moonitz (1957). Baylis (1971). Morley (1973). Van Hoepen (1981) and Defliese (1983). Arguments against TEA have been advanced by among others. Hill (1957). Chambers (1968). Barton (1970). Clarke (1976). Rosenfield and Dent (1983). Ernst & Whinney (FASB 1983) and Henderson (1992).

At an empirical level there have been specific studies on the eventual crystallization of the PDIT as a liability. Davidson (1958) demonstrated with a simulation study that the deferred tax liabilities would require actual payment only in the case of a declining firm when those declining years are also profitable years. Other studies examined the extent to which PDIT becomes a liability requiring the sacrifice of an economic resource. Price Waterhouse (1967) examined 100 companies over a thirteen year period and found that additions to the PDIT exceeded reductions by a factor of 48 to 1. A number of studies since then have confirmed the Price Waterhouse results (Cawsey et. al., 1973. Herring and Jacobs. 1976; Bartholemew. 1987; Wise. 1986).

While there have been a large number of studies concerning conceptual as well as empirical aspects (for details of the studies see Keys. 1995) of TEA to our knowledge there has been no published work on the user perception of the various aspects of tax allocation. The current study is a step toward filling this gap by examining the perception of auditors of PDIT.

III. PDIT and the Auditors

To satisfactorily audit general purpose financial reports, auditors are required to have an extensive knowledge of accounting standards and the conceptual framework (CF). On this basis, it is reasonable to assume that auditors will be knowledgeable on issues relating to TEA and the treatment of deferred tax liabilities. Auditors' familiarity with TEA issues, together with their importance as a group involved in the verification and quality control of public company accounts, make an examination of their perception of the treatment of the PDIT of interest.

Any survey of auditors, which is directed at ascertaining their opinion on some aspects of an accounting standard, must allow for their role in ensuring that reporting entities adopt, and correctly apply accounting standards. The role of auditors in applying approved accounting standards raises questions about their willingness to question the integrity of those standards. An auditor who publicly questions the integrity of an accounting standard may find herself in the dubious position of being engaged in ensuring that a client fully complies with an approved accounting standard while simultaneously being on record as not approving of it. In such circumstances, their clients might be excused for questioning the purpose, reason and benefit of complying with the controversial accounting standard. Auditors will have a tendency to avoid such potential problems by refraining from publicly questioning the integrity of an accounting standard.

For the above reason, the study is designed to avoid asking auditors directly their agreement/disagreement with AASB 1020 accounting for Income Tax (Tax-Effect Accounting). The approach was to ascertain the auditors' perception of PDIT with reference to the criteria outlined in SAC 4.

IV. Methodology

Data Sources and Sample Selection

Preliminary discussions with the Institute of Chartered Accountants in Australia (ICAA) and the Australian Society of Certified Practicing Accountants (ASCPA) indicated the population frame of auditors in Australia to be in the region of five to seven thousand. It was considered impractical to send a questionnaire to a population of that size. Instead, two representative groups out of the total population were selected for a questionnaire survey.

The first group consisted of all auditors engaged in the audit of companies listed on the Australian Associated Stock Exchange (ASX). As the purpose of the questionnaire was to examine the perceived status of the PDIT within the provisions of the CF, this subgroup of public company auditors was considered particularly appropriate. Firstly, listed companies are required to adopt TEA and hence are likely to disclose some information about the PDIT requiring consideration by an auditor. Secondly, the financial statements of listed companies enjoy a high profile. Accordingly, one might expect auditors to be particularly sensitive about the nature of what is disclosed in listed company accounts. Auditors in this subgroup were identified by using the ASX's CD-ROM "Datadisc" (Australian Stock Exchange [ASX], 1993). The Datadisc holds, among other things, the corporate details of every listed company in Australia. The examination of this source led to the identification of one hundred and seventy-six audit firms. A questionnaire was posted to an audit partner of each audit (accounting) firm.

The second group of auditors included in the survey is a cluster sample. As there is no evidence to suggest that the opinion of auditors, on accounting issues, is determined by geographical location, it was decided to include all the Western Australian auditors in the survey. Western Australian branches of ICAA and the ASCPA were approached for a mailing list of their members involved in audit work.

The ASCPA supplied a list of one hundred and twenty-two names. The ICAA provided a similar list which contained a total of four hundred and seventy names. An aggregate of five hundred and ninety-two questionnaires were posted to the members identified above.[1]

Questionnaire

The questionnaire consisted of six questions (Appendix 1) and a section for demographic details including job function, audit experience, and specific accounting designation.[2] The questions centre on critical conceptual statements about the status of the PDIT. Each question was accompanied by a five-point Likert scale, asking the respondents to indicate whether they strongly agree, agree, neither nor disagree disagree (i.e., neutral) or strongly disagree with the relevant conceptual statement.

The questions were drafted to reflect the essential characteristics of liabilities as contained in SAC 4.[3] Specifically, the questions concerned the following issues.

1) Does the reduction of a PDIT due to a loss involve sacrifice of an economic resource?
2) Is the PDIT a present obligation?
3) Can a present obligation depend on the occurrence of a future event?
4) Should the PDIT be treated as an aggregate account?
5) Should recurring timing differences be recognised as a liability?
6) Should the PDIT be disclosed if its measurement is possibly unreliable?

Each question is considered to stand on its own. Accordingly, the analysis will focus on ascertaining the prevailing attitude to these issues.

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[1] In order to minimise duplication known audit partners names appearing in the second sample were removed prior to mailing of the questionnaire. In any event we do not believe that an auditor would be so naive as to complete the same questionnaire twice.
[2] A pilot test using a random sample of 20 auditors indicated the questionnaire was satisfactory. Consequently, no changes were made to the questionnaire.

[3] A liability has been defined in SAC 4 as follows:
The future sacrifice of service potential or future economic benefits that the entity is presently obliged to make to other entities as a result of past transactions or other past events (AARF, PSASB &AASB, 1995, para. 48). For a formal recognition of a liability two additions must be met (SAC 4 para 65):

1. The settlement of the liability is probable
2. The liability is reliably measurable.

Although the questions in the questionnaire focus on differing conceptual issues, and are considered relatively independent, if a respondent has a preconceived notion of whether a PDIT is a meaningful liability, some questions can be expected to be answered in a particular way. For example, if a respondent believes that the PDIT is a meaningful liability, then he/she is likely to agree with question six, which generally states that the PDIT is useful information. It is possible that a respondent will regard the PDIT as useful information, even though he/she does not consider it to be a meaningful liability. In these circumstances, the PDIT may be seen as useful because it reflects the current total of deferred tax arising from the tax allocation process. Accordingly, a respondent who is of the opinion that the PDIT is not a meaningful liability, is less likely to treat it as an important piece of information than a respondent who considers the PDIT to be a liability an unavoidable future sacrifice of economic resources.

The reasons outlined above also suggest that a respondent, who is of the opinion that the PDIT is useful information, is more likely to indicate in question two that the PDIT is a present obligation, and take the view in question five, that the apparent non-reversal of a PDIT, in aggregate over time, is a valid reason for not recognising the PDIT (or part of the PDIT) in the books of account.[4] If an analysis of the responses to the questionnaire indicates that the answers to questions 2, 5 and 6 are internally consistent, the presumption will be that the questionnaire has generally been understood and carefully considered.

V. Results

From a total of seven hundred and sixty-eight distributed questionnaires, one hundred and seventy-six (23%) usable replies were received, forty-five (a 25% response rate) from the Australia wide survey of audit firms[5] and one hundred and thirty-one (a 22% response rate) from the survey of auditors residing in Western Australia.[6]

[4] A respondent who is of the opinion that a PDIT is merely a deferred credit that should be reported in the balance sheet, will not be troubled by the non-reversal over time of a PDIT. However, a respondent who believes that the PDIT is a meaningful liability will be more concerned if that liability does not appear to settle (reverse) over time.

[5] Those auditors, irrespective of their location in Australia, who are engaged in the audit of public companies.

[6] Due to time and cost constraints a mail follow-up was not undertaken.

Demographic Information

Demographic information was obtained on each respondent's primary job function, whether audit partner, audit manager or other; years of experience in audit; and which professional accounting body they belonged to and their professional designation[*] within that body. These appear in Table 1 below.

Table 1
Survey of Auditors, Demographic Information

Primary Job Function	Number
Partner	79
Manager	42
Other	55
Total	176
Experience in Audit (yrs)	**Number**
Under 5	22
5-9	43
10-19	57
Over 19	54
Total	176
Professional Designation	**Number**
ACA	97
ACACPA	24
CPA	19
FCA	24
FCACPA	7
FCPA	3
OTHER	2
Total	176

Demographic information was sought for several reasons. Firstly, in forwarding the questionnaire to various accounting firms there was some concern as to whether the questionnaire would be completed by the audit partner/manager as

[*] The ASCPA has two designations for its members, namely CPA (Certified Practising Accountant) and FCPA (Fellow). The ICAA designates its members either as an ACA (Associate) or as an FCA (Fellow). Some professional accountants are members of both bodies (ACACPA or FCACPA).

requested, or by an audit junior staff. Only five respondents[8] gave their primary job function as "other" (ie., not a partner or manager) and only 31% of this group had less than five years experience. This means that a very high proportion of the respondents were senior auditors. A second reason for acquiring demographic information was to allow some assessment to be made of the standing of those auditors who responded. In total, 45% of respondents were audit partners, 24% were managers, and a full 86% of all respondents had five or more years of audit experience. These figures suggest that the replies represent the views of experienced auditors. The final reason for seeking demographic information was to ascertain whether auditors' views on the PDIT can be associated with their work experience or the accounting body they belong to.

Internal Validity

For the purpose of testing internal validity auditors were divided into two groups. Those that indicate, in question six, that PDIT may not be useful information, and those that indicate that it is. The responses of each group, to question two and five, were then compared to ascertain whether auditors who regard PDIT as useful information are more likely to treat the PDIT as a meaningful liability. Of the one hundred and seventy-six responses received, one hundred and eighteen gave a reply to question six indicating that PDIT was useful information, while forty-eight indicated that it was not. Ten respondents neither agreed nor disagreed with question six. The group of ten was excluded from the sample as they have not provided on opinion.

The wording of questions two and five were designed so that a consistent response to both questions required selecting opposite end of the Likert scale. Respondents indicating that PDIT may not be useful information in question six would need to select either "strongly agree" or "agree," in question two, but "disagree" or "strongly disagree" in question five. Accordingly, for a statistical test to be valid, not only must the mean of the responses for both groups statistically differ, but the mean response of the group of forty eight to question two must be lower than the group of one hundred and eighteen, while their mean response to question five must be higher.

The results of the *t*-tests (Table 2), with a 95% confidence level, confirm that the two groups identified from question six, have answered questions two and five consistently. Accordingly, it is concluded that the respondents have reasonably considered and consequently understood the questionnaire.

Analysis of the demographic information, including job designation: audit partners, managers or others; years of experience, those with less than five and those

[8] Five from the forty-five replies received from the Australia wide survey of audit firms.

with more than nineteen; and membership of the ICAA and ASCPA, failed to show any significant statistical difference in the responses to any of the questions in the questionnaire (tested by way of independent *t*-test). Based on the results of the test of internal validity (table 2), the relative seniority of the auditors who responded to the survey, the fact that all respondents, irrespective of job function, experience and accounting designation appear to have answered the questionnaire in similar manner[9], the research design is considered internally consistent.

Table 2

Auditors t-test of internal validity questions 2 & 5

Group A:

Respondents answering either disagree or strongly disagree to question 6, forty eight (48).

Group B:

Respondents answering either agree or strongly agree to question 6, one hundred and eighteen (118).

Independent t-test on question 2

Group	N	Mean	SD	T	DF	PROB
A	48	2.354	1.263	2.882	86	0.005
B	118	2.975	1.244	2.882	86	0.005

Independent t-test on question 5

Group	N	Mean	SD	T	DF	PROB
A	48	2.854	1.330	4.981	66.2	0.000
B	118	1.966	0.784	4.981	66.2	0.000

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[9] If a senior (experienced) group of auditors, say audit partners, responded to the questionnaire in a different way from another less senior group ie., those auditors with a job function of "other" and having less then ten years experience, a question might arise as to the reliability of responses, This is so because, TEA and the CF are complex accounting issues.

A finding that senior auditors have differing opinions that the less experienced groups, might imply that the less experienced group did not fully understand or appreciate the issues.

Main Results

As the questionnaire was primarily designed to ascertain opinion on several specific conceptual issues, the analysis of the data will focus on reviewing the response to individual questions. The extent to which responses to the questions overall, indicate an underlying perception auditors have of the PDIT, will be discussed in the analysis section.

Question 1. As shown in Table 3 seventy-three (41.5%) of the respondents agreed with this statement. 15.9% were neutral and seventy-five (42.6%) disagreed.

Table 3
Responses to Question 2

Likert Scale	Number	Cumulative Number	Percent	Cumulative percent
. Strongly Agree	7	7	4.0	4.0
Agree	66	73	37.5	41.5
Neutral	28	101	15.9	57.4
Disagree	56	157	32.9	90.3
Strongly Disagree	17	176	9.7	100.0

The results indicate that the respondents were almost equally divided on the use of losses to settle a PDIT as a settlement requiring sacrifice of economic resources. Only a slight majority of auditors perceive the PDIT as not satisfying an important criterion of the definition of a liability in SAC 4 namely, the necessity to sacrifice an economic resource for the settlement of a liability.

It was noted that in ten of the responses to question one, the term "accounting losses" was crossed out and "taxation losses" substituted in its place. It is hypothesised that because TEA specifically provides for the offsetting of taxation losses against the PDIT[10] (ASRB 1020, para. 14), and only allows the offset of accounting losses against the PDIT by indirectly applying a more unusual TEA provision[11] (ASRB 1020, para. 18), auditors probably treated question four as referring to taxation losses. If this is the

[10] Clause 14 states: "(Where a provision for deferred income tax exits and a company incurs a tax loss, the future income tax benefit attributable to the tax loss shall be brought to account as a reduction in the provision for deferred income tax...)".
[11] Clause 18 states: "...a provision for deferred income tax shall be offset against future income tax benefit brought to account, to the extent that income tax covered by the provision is likely to become payable in the same financial periods as the future income tax benefits is expected to become realisable".

case 42.6% of auditors believe that the allocation of taxation losses against a PDIT does not involve the sacrifice of resources, despite taxation losses specifically recognised at way as available to reduce future income tax payable (Income Tax Assessment Act, 1936, Section, 80G).

Question 2. As shown in Table 4 ninety-nine (56.3%) respondents agreed with this statement, 4% were neutral and seventy (39.8%) disagreed. In particular twenty-six (14.8%) respondents strongly agreed with the above statement, while only fifteen (8.5%) strongly disagreed.

Table 4

Responses to Question 2

Likert Scale	Number	Cumulative Number	Percent	Cumulative Percent
Strongly Agree	26	26	14.8	14.8
Agree	73	99	41.5	56.3
Neutral	7	106	4.0	60.2
Disagree	55	161	31.3	91.5
Strongly Disagree	15	176	8.5	100.0

This result indicates that an absolute majority of auditors are of the opinion that the PDIT is not a present obligation. This is consistent with the conclusion that the PDIT does not readily satisfy the present obligation requirement of SAC 4.

> ...future income tax payable from current timing differences may fail to be re recognised as a liability because...it does not satisfy the recognition criteria of probable future sacrifice of service potential or economic benefits (AARF 1995, para. 65).

Question 3. As shown in Table 5 one hundred and eleven (63.1%) of respondents agreed with this statement, 10.2% were neutral and forty-seven (26.7%) disagreed. In particular twenty-two (12.5%) respondents strongly disagreed.

Table 5
Responses to Question 3

Likert Scale	Number	Cumulative Number	Percent	Cumulative Percent
Strongly Agree	22	22	12.5	12.5
Agree	89	111	50.6	63.1
Neutral	18	129	10.2	73.3
Disagree	37	166	21.0	94.3
Strongly Disagree	10	176	5.7	100.0

The results indicate that a clear majority of auditors consider a present obligation cannot exist if it is dependent on the occurrence of a future event. This is not altogether surprising as it is consistent with the definition of a present obligation. The question that arises is whether the response to question three indicates that the auditors are supportive of the conclusion that there is no effective past transaction or event which can be said to create present obligation to pay deferred taxes.

It would appear that auditors who indicated in question two that the PDIT is not a present obligation. because the taxation office is unaware of it. or even if the tax office were aware. it would not be in position to claim payment. have effectively taken a view that the PDIT is dependent on a future event. the earning of future taxable income. Moreover. the response to question three seems to confirm that a majority of auditors appreciate the need for a present obligation to arise solely from a past transaction or event. Accordingly. it appears that a majority of the auditors do not perceive the PDIT as a present obligation.

Question 4. As shown in Table 6 seventy-eight (44.6%) respondent agreed with this statement. 16% were neutral and sixty-nine (39.4%) disagreed.

Table 6
Responses to question 4

Likert Scale	Number	Cumulative Number	Percent	Cumulative Percent
Strongly Agree	8	8	4.6	4.6
Agree	70	78	40.0	44.6
Neutral	28	106	16.0	60.6
Disagree	58	164	33.1	93.7
Strongly Disagree	11	175	6.3	100.0

The purpose of this question was to ascertain whether the auditors preferred the aggregate or singular view of timing differences. The aggregate view implies that the PDIT should be taken as one single item of liability and therefore the probability of the future economic sacrifice will be considered for the aggregate amount of PDIT. To the extent a timing difference is not considered ultimately to be payable it will not be included in the measure of PDIT. The singular view, on the other hand, would imply that every timing difference is treated as an independent item. Since most of the timing differences would reverse the probability criterion would seem to be satisfied with almost certainty. Thus the aggregate view is consistent with the partial or no allocation approach whereas the singular view would support the comprehensive allocation of taxes.

The results indicate that most auditors would be supportive of the aggregate approach. The implication is that the proposition that the PDIT is a meaningful liability since each individual timing difference must reverse and hence be paid, does not have majority support of auditors.

Question 5. As shown in Table 7 one hundred and thirty-eight (78.4%) respondents agreed with this statement, 5.1% were neutral and twenty-nine (16.5%) disagreed. In particular thirty (17%) respondents strongly agreed with the above statement, while only four (2.3%) strongly disagreed.

Table 7

Responses to Question 5

Likert Scale	Number	Cumulative Number	Percent	Cumulative percent
Strongly Agree	30	30	17.0	17.0
Agree	108	138	61.4	78.4
Neutral	9	147	5.1	83.5
Disagree	25	172	14.2	97.7
Strongly Disagree	4	176	2.3	100.00

The purpose of question five was to ascertain the degree of support among auditors for the recognition of PDIT in the light of the empirical evidence suggesting that the PDIT account for most companies increases over time. The results demonstrate that auditors do not believe this evidence forms a basis for the non recognition of the PDIT.

Question 6. As shown in Table 8 one hundred and eighteen (67%) respondents agreed with this statement, 57% were neutral and forty-eight (27.3%) disagreed.

The primary purpose of question six was to determine whether auditors thought that, the PDIT should be recognised as a liability. Although it could not be reliably measured the results indicate that most auditors do not consider problems of reliable measurement as a basis for non-recognition of a PDIT. By agreeing with question six the respondent is in effect stating, that inspite of the uncertainty about the timing and amounts concerning the settlement of the PDIT, it should be stated in the financial statements. This is an interesting finding because it appears to conflict with the CF.

Table 8

Responses to Question 6

Likert Scale	Number	Cumulative Number	percent	Cumulative percent
Strongly Agree	23	23	13.1	13.1
Agree	95	118	54.0	67.0
Neutral	10	128	5.7	72.7
Disagree	33	161	18.8	91.5
Trongly Disagree	15	176	8.5	100.0

VI. Analysis

An essential characteristic of a liability is that a sacrifice of service potential or future economic benefit must be required to settle the obligation. Responses to question one show that a majority of auditors believe that reductions in PDIT may happen in ways other than involving the sacrifice of an economic resource. This weakens the case for PDIT to be considered as a liability. The responses to question two is indicative that a clear majority of auditors does not view PDIT as a present obligation.

The responses to question three show that a majority of auditors do not consider that the condition of 'past transaction or other past event' is satisfied since the PDIT will be payable only if the company makes profits in the future. Thus it appears that the auditors do not perceive the PDIT as a genuine liability. It is important to note here that the criteria of (1) sacrifice of economic resource, (2) present obligation and (3) evidenced by past transaction or event are all essential characteristics of a liability as per SAC4. Failure to meet any one of these criteria disqualifies the item to be considered for recognition as a liability. We hasten to reiterate that the auditors surveyed were not unanimous in their opinion rather only a majority thought that the

PDIT was lacking the three essential characteristics of a liability. Responses to question four also serve to indicate the divided nature of the auditing profession on the issue of PDIT. While a majority was in favour of considering PDIT as an aggregate item, a large minority would consider each timing difference individually. As explained earlier, those who prefer the aggregate approach would be more inclined to treat PDIT as non-liability than those who prefer the singular approach. Thus on the definitional attributes a majority of auditors would view PDIT as a non-liability.

For question five the majority of responses were in favour of recognising PDIT as a liability although experience may show that PDIT hardly ever needs settlement with an external party. Consistent with the responses to question five, the responses to question six indicate that a clear majority of the auditors considered PDIT in the balance sheet a useful piece of information even though there may be reliability problems in their measurement.

Two observations seem to be in order. Firstly, auditors are divided on whether PDIT satisfies the definition and recognition criteria in SAC 4. Secondly, even when a majority considers PDIT not to satisfy the definition of a liability most auditors would still like it to be reported in the balance sheet. The two positions are inconsistent.

Alternative explanations are available to reconcile this apparent inconsistency. It is possible that auditors have a different view of liabilities than what is contained in SAC 4. They answered questions one to three based on SAC 4 ideas but in questions five and six they gave answers based on their own conception(s) of a liability. Alternatively, auditors do not believe that PDIT is genuine liability but would like to allocate taxes for "better matching" in the income statement and condone the appearance of the PDIT on the balance sheet as a deferred credit-a dubious liability.

VII. Conclusions

The result of our study reflects the state of confusion prevailing with regard to issues concerning TEA and more particularly PDIT. While a majority of auditors do not believe that PDIT satisfies the definitional attributes of a liability they at the at the same time believe that the PDIT should be reported on the balance sheet. In a way, it may be indicative of a divided loyalty on the part of the auditors between the income statement and the balance sheet views of accounting. It also indicates that auditors may not have completely internalised the SAC 4 view of a liability.

Overall, our research shows that the auditors do not unequivocally treat PDIT as a liability. Such a finding is consistent with SAC 4 and with the conclusions of other researchers (Goodwin, 1989; Picker, 1992; Sims, 1993).

Further research is needed at both analytical and empirical levels to clarify the status of PDIT and the propriety of interperiod tax allocations. In particular, studies are needed to clarify the status of the so called future income tax benefits. Empirical surveys could be done of other interest groups such as financial analysts, shareholders and trade creditors to see how they perceived the PDIT.

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Appendix 1

QUESTIONNAIRE (Extract)

Q1. The elimination of a Provision for Deferred income Tax, due to the recognition of accounting losses, amounts to settlement of that liability involving sacrifice of economic resources.

Q2. A Present obligation to settle (pay) a Provision for Deferred Income Tax Liability does not exist at balance date because the Taxation Office (Federal Government) is not in a position to claim payment of that liability and, in addition, does not consider it self entitled to, and hence is not expecting , any future receipt from the entity in respect of that liability.

Q3. A Present obligation cannot exist at the balance sheet date if it is dependent on the occurrence of a future event. Future events must only be ancillary to the obligation. Accordingly, a present obligation must result solely from past transactions or events.

Q4. It is incorrect to think of the Provision for Deferred Income Tax as an account consisting of a collection of unique timing differences. The account should always be viewed and treated as a single liability because all the timing differences are about the same thing, the deferral of payment to one external party, the federal government.

Q5. There is substantial amount of evidence proving that, for many companies, the balance of the Provision for Deferred Income Tax Liability never falls due because new timing differences always replace older, reversing, timing differences. This does not constitute a reason for not recognising the Provision for Deferred Income Tax as a liability since many other liabilities, creditors in particular, tend to "roll-over" resulting in the net creditors balance remaining constant or even increasing over time.

Q6. Accruing income tax expence, and the consequential recognition of a Deferred Income tax Liability, convey useful information to the users of general purpose financial reports, even though the actual payment of income tax eventually paid is often materially different from the originally accrued income tax expense.