**ASC Topic 740 Case Study**

COMPANY NAME Inc. sells stick puppets and marionettes, as well as theater curtains, fancifully painted stage backgrounds, and related props. The corporation held its grand opening on April 16, 2007, and is an accrual-method, calendar-year taxpayer. The business operates retail locations in Florida, which does not have a state income tax. A partial income statement prepared under GAAP appears below:

|  |  |  |
| --- | --- | --- |
| **Income statement** | | |
| Income |  |  |
| Sales |  | $1,900,500 |
| Cost of goods sold |  | 550,000 |
| Gross profit |  | $1,350,500 |
| Dividends |  | 8,200 |
| Interest income |  |  |
| Savings and checking account, King Friday Bank | $4,500 |  |
| US Treasury bonds | 3,000 |  |
| City of Make-believe bonds | 7,200 | 14,700 |
| Income (loss) from financial investments |  | (8,000) |
| Total income |  | $1,365,400 |
|  |  |  |
| Expenses |  |  |
| Salaries |  |  |
| Company officers | $270,000 |  |
| Sales and administrative | 102,000 | $372,000 |
| Advertising |  | 23,700 |
| Bad debt expense |  | 4,280 |
| Depreciation |  | 28,750 |
| Interest expense |  | 16,610 |
| Life insurance premiums |  | 13,300 |
| Meals and entertainment |  | 9,200 |
| Repairs and maintenance |  | 4,220 |
| Taxes (property and payroll) |  | 56,600 |
| Total expenses |  | $528,660 |

The company also provided the following additional information for the 2016 tax year:

* MACRS depreciation for the year totaled $20,000. There were no new acquisitions this year.
* Actual bad debt write-offs were $1,000.
* Life insurance premiums were paid on policies covering the lives of the two owners. The corporation is the beneficiary of the policies.
* All of the interest expense was incurred for general business purposes.
* Dividends received were from stock investment in less-than-20%-owned U.S. corporations.
* This year, the company had a $5,000 capital gain and a $13,000 capital loss. It has not reported any capital income or loss in previous tax years. In management’s judgment, it is more likely than not that it will only be able to generate $3,500 in capital gains over the next five years.
* In 2007, COMPANY NAME Inc. incurred startup costs of $7,000, organizational costs of $3,000, and syndication costs of $2,000.
* The company disposed of a portion of its business in 2016 that related to selling men’s cardigan sweaters and leather loafers. The disposal qualifies as a discontinued operation. It generated a loss of $72,000, which it has not yet accounted for on its partial income statement.
* COMPANY NAME is entitled to a $9,000 nonrefundable credit that related to continuing operations.
* Please assume the applicable statutory rate is 30%.

Required:

1. Utilize the partial income statement and additional information provided to identify the company’s book-tax differences for the year. Enter the amount of each difference in the first worksheet of the accompanying Excel template, and then use the drop-down menu in the “deferred effect” column to note whether the difference increases/decreases a deferred tax asset, increases/decreases a deferred tax liability, or neither (n/a). At the bottom of the worksheet, calculate the annual change to the cumulative taxable differences and cumulative deductible differences and enter the effects in the associated drop-down boxes.
2. Based on the information provided and your calculations in Task 1, calculate the year’s total income tax provision on the second worksheet and prepare the journal entry (or entries) required to record the total income tax provision. Complete the income statement in proper form. The company will disclose the required current/deferred breakout on the face of the income statement in lieu of disclosing it in the footnotes.
3. Use your total income tax provision journal entry/(entries) from Task 2 and the additional information provided to complete the income statement in proper form on the third worksheet. The company will disclose the required current/deferred income tax break-out on the face of the income statement in lieu of disclosing it in the footnotes.
4. Prepare the year-end rate reconciliation for the company’s income tax footnote. Assume all items are significant.

General Instructions: Please prepare the required elements of this case study in the appropriate worksheet tabs of Excel. While completing each sheet, please do so neatly. Specifically, please make sure your font and alignment are consistent, cell border underlines are consistent, etc. You may also turn in any supplemental work you did or explanations.