Financial Accounting Recitation 3 (B Term)

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Road Map

- Recap of receivables
- Recap of PP&E
- Recap of tax accounting
- PS 6, PS 7, and class example for tax accounting
- Office hour for specific questions

The Graphical Illustration of Receivables

- Recognition, write-offs, reinstatement
- Please refer to the last two review sessions if you're interested...

Intertemporal Relationship of Bad Debt Allowance

- Ending Balance = Beginning Balance + Bad Debt Expense - Write-offs
- It might be useful to analogize to depreciation expense and PP&E...
- If we work with the B/S approach, *typically*...
  - BB and EB can be inferred from the B/S based on the recognition principles
  - Write-offs are known
  - BDE needs to be backed out by the relationship
- If we work with the I/S approach, *typically*...
  - BB is inherited from the last period
  - Write-offs are known
  - BDE is determined from the credit sales (increase in A/R) in the current period
  - EB will be determined by BB, write-offs, and BDE

Tax Accounting

- The discrepancies between GAAP and IRS tax codes cause accounting issues
- Permanent differences: Different jurisdictions; different items for income/tax purposes
- Temporary differences: Differences between GAAP-basis income and tax-basis income resulting from differences in the time of recognition (decay to zero in the long run)
- Effective tax rate (provisions for income taxes) = tax expense / pre-tax income
- Income tax expense...

$$
\begin{aligned}
&= \text{Tax (current)} \pm \text{Tax (deferred)} \\
&= \text{Statutory Tax Rate} \times (\text{EBT (Tax Rule)} \pm \text{Temporary Difference}) \\
&= \text{Statutory Tax Rate} \times (\text{EBT (GAAP)} \pm \text{Permanent Difference})
\end{aligned}
$$

PP&E

- Ending PP&E = Beginning PP&E + Purchase - Sale/Disposal (All in gross values)
- Ending Acc Dep = Beginning Acc Dep + Dep Exp - Acc Dep Related to Sale/Disposal
- Gain/Loss on Sale of PP&E = Proceeds - (Gross Value of PP&E - Related Acc Dep) (Gain if positive and loss if negative; Note that the red things equal to each other only if there's no disposal)
- Typical roadmap: 1) Use one equation to back out one unknown, x; 2) Use the intermediary result, x, to back out other unknowns in other equations