The Income Tax Accounting Controversy: A Matter of Perspective

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Abstract

The study examines SFAS No. 96 and SFAS No. 109 in the context of the unit problem. The unit problem involves the selection of the appropriate perspective for applying measurement and recognition conventions to the phenomenon of interest. From an individual event perspective, the FASB's conclusions regarding liability recognition are inconsistent with their definition of a liability found in Statement of Finance Accounting Concepts No. 6. In addition, the use of inconsistent perspectives by the SFAS No. 96 and SFAS No. 109 create disagreements with the Board's positions. The simultaneous use of both the individual and aggregate perspectives as the basis of the Board's decisions is the source of these disagreements. The study argues that the income tax accounting issue should be viewed from an aggregate perspective and concludes that the flow through method of accounting for income taxes should be adopted.

Introduction

After much debate and a considerable amount of compromise, the Financial Accounting Standards Board (FASB) issued *Statement of Financial Accounting Standards No.96* (*SFAS No.* 96) "Accounting for Income Taxes" (FASB, 1987). The statement was to take effect after December 15, 1988. However, due to the complexities of implementing *SFAS No. 96*, the Board delayed the effective date of the Pronouncement three times (FASB, 1991). Finally, in 1992 the Board issued *Statement of Financial Accounting Standard No. 109* (*SFAS No. 109*) which superseded the requirements of *SFAS No. 96* completely (FASB, 1992). The *SFAS No. 109* reverts back in a large extent to the requirements of *APB No. 11*. Thus for more than five years, the Board struggled with the controversy of changi ng the reporting requirements for deferred taxes. The large number of responses received by the Board throughout the standard formulation process, the continuing controversies regarding the final pronouncement, and the delays in implementing the standards attest to the complexity and controversy of the issues confronting the FASB.

Since the release of *SFAS No. 96* and *SFAS No. 109*, critics have raised several concerns about accounting for deferred taxes. They have criticized (1) the inconsistent treatment of the deferred tax asset and liability (Wolk, Martin, and Nichols, 1989; Parks, 1988), (2) the FASB's failure to allow for discounting of the

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deferred tax liability (Rayburn, 1987), (3) the method's complexity and potential lack of usefulness (Burton and Sack, 1989; Gregory, Petree, and Vitray, 1992) and (4) the FASB's failure to deal with temporary differences that are "permanently deferred" (Jeter and Chaney, 1988). Many of these concerns are not fully addressed in either statement.

The controversy over the accounting for income taxes will not subside until the Board completely reconsiders its position and adequately addresses what is referred to as the "unit problem" (Devine, 1985). The unit problem involves the selection of the appropriate perspective for applying measurement and recognition conventions to the phenomenon of interest. The perspective ranges from accounting for individual events or transactions to accounting for aggregate events or transactions. The positions taken by both proponents and opponents of *SFAS No. 96* and *SFAS No. 109* are affected by whether one views income tax accounting as an issue of accounting for individual events or as an issue of accounting for aggregate activity. The positions one takes regarding the income tax accounting issue are directly related to one's view of the unit.

This paper examines *SFAS No. 96* and *SFAS No. 109* in the context of the unit problem. It is shown that the FASB generally adopted the individual event perspective regarding the income tax accounting issue, except for a few instances where conclusions were based on the aggregate view. However, from an individual event perspective, the FASB's conclusions regarding liability recognition are inconsistent with the definition of a liability found in *Statement of Financial Accounting Concepts No. 6* (FASB, 1985, par. 35). This study argues that the income tax accounting issue should be viewed from an aggregate perspective and concludes that the flow through method of accounting for income taxes should be adopted. In light of these conclusions and the conclusions of many other flow through proponents, the FASB should reconsider the entire income tax accounting issue.

The Unit Problem

Carl Devine discusses the "unit problem" and how it affects several accounting policy issues. The unit problem revolves around the selection of the scope or perspective from which to apply measurement and recognition conventions. This choice is critical and will affect the outcome of the application. Devine states:

We begin with the old, but important, procedural problem: whether to select small units and aggregate them so long as they prove to be useful or to select a large unit and use imputation devices until interest wanes ... Many of the arguments and controversies in accounting result from undisclosed differences in points of view with regard to the accountability units selected (Devine, 1985, p.2).

The problem is one of selecting appropriate attributes for characterizing the event for which one wishes to account. The accounting process involves the identification, grouping and measurement of what are believed to be relatively homogeneous events. If events are not strictly homogeneous, however, a problem can arise in selecting attributes of the group or class portrayed by the accounting process. Some may take a specific or individual perspective which examines the attributes of one member of the group and assumes that those attributes may be generalized to the other members. Others may take an aggregate perspective which attempts to identify attributes relevant to the accounting process by examining the behavior of the group taken as a whole rather than focusing on individual members. Given some nontrivial degree of heterogeneity within the group, an observer adopting the individual perspective will most likely identify a different set of accounting attributes for the class of events than someone who takes an aggregate perspective. Thus, supportable alternative perspectives (individual versus aggregate) can emerge which will lead to different positions on the relevant attributes of an accounting phenomenon and to different conclusions concerning its accounting disposition.

SFAS No. 96 & SFAS No. 109 - An Individual Event Perspective

The FASB's view of the income tax accounting issue generally requires that an individual event perspective be taken. The Board's position is that tax consequences of an individual event are separable from aggregate taxable income (FASB, 1987, par.174). *SFAS* No.96 requires that:

A liability or asset shall be recognized for the deferred tax consequences of all temporary differences, that is, of taxes payable or refundable in future years as a result of the deferred tax consequences of events recognized in the financial statements of current or preceding years (FASB, 1987, par. 14).

Further *SFAS No. 109* indicates:

Temporary differences ordinarily become taxable or deductible when the related asset is recovered or the related liability is settled (FASB, 1992, Summary)

While the procedures outlined for implementing the Standard require the analysis of individual temporary differences and scheduling their reversals in future years, an aggregate calculation is required for each future year in order to determine the net taxable amounts upon which the liability calculation is based.

The Board's discussion of the basis for their conclusions also clearly indicates the individual event perspective that they take. For example, in response to advocates of partial allocation (an aggregate perspective), the Board states:

Nevertheless, the deferred tax consequences of a depreciation difference for a particular depreciable asset ordinarily will result in a sacrifice in future years. There will be a future sacrifice because an individual difference results in a taxable amount when revenue that recovers the reported amount of the depreciable asset exceeds its remaining tax basis (FASB, 1987, par. 179).

Based upon this individual event perspective, *SFAS No. 96* and *SFAS No.* 109 require the adoption of the "liability method" of accounting for interperiod income tax allocation. The liability method is built upon the premises that deferred tax assets and liabilities will result in future tax obligations or benefits irrespective of assumptions concerning future taxable income or loss and that the objective of accounting for income taxes is to recognize both current and deferred taxes payable or refundable at the date of financial statements as a result of all events recognized in the financial statements and by provisions of existing tax laws. Implicit in their assumption is that the tax consequences of earning income or incurring losses or expenses in future years are not anticipated for purposes of recognition and measurement of a deferred tax liability or asset. Since this view is not defensible in many situations, *SFAS No. 109* modifies this requirement by considering future events to assess the likelihood that future tax consequences have been affected by events recognized in the current financial statements (FASB, 1992, par. 6).

The Question of Liability Recognition

In the Board's view a deferred tax liability meets the *SFAC No. 6* definition of a liability:

Probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events (FASB, 1985, par. 35).

In support of its conclusions in *SFAS No.109*, the Board argues that:

(1.) Temporary differences will become taxable amounts in future years as a result of events whose occurrence is already inherently assumed in an enterprise's statement of financial position for the current year; (2.) No other future events need occur; (3.) The enterprise might be able to delay settlement of a tax obligation by delaying the events that give rise to taxable amounts ... However, a contention that those events will

never occur would contradict assumptions inherent in the statement of financial position; and (4.) Tax obligations are incurred when temporary differences originate (FASB, 1985, pars. 85-89).

It can be demonstrated that this conclusion is not supported at the individual event perspective. If one takes an individual event perspective, the characteristics of a liability are present if the temporary differences between taxable income and financial statement income result in future net taxable amounts and if there is sufficient future taxable income (an aggregate concept). Without future income, the deferred tax liability may disappear. Consider the example of a machine costing $1,000,000 with an $80,000 residual value and a five year useful life. Double declining balance depreciation is used for tax purposes and straight line is used for financial reporting. Table 1 reflects depreciation expense for the financial statements and the tax return. It shows the deferred tax liability for each of the five years under the liability approach.

As long as future income is sufficient, the deferred liability will follow the pattern illustrated in Table 1. However, if income is not sufficient or if losses occur, the liability disappears. Table 2 illustrates one example in which a loss in year two significantly alters the presentation of the deferred liability. In this example, taxes are not paid on the depreciation difference until the fifth year. The actual obligation at year 1 was only $25,840 as opposed to the $73,440 accrued in accordance with the standard. It is easy to present several scenarios where no taxes will be paid due to a one year loss situation.

A counter-argument made by proponents of deferral method is that the liability should still be recognized in year one because inherent in the financial statement is the assumption that assets will be recovered. However, this assumption does not assume that an enterprise will never incur losses. A one year loss, in all probability, does not affect the going concern assumption of accounting. Clearly, without sufficient future income, the liability does not cause a future economic sacrifice. From an individual event perspective, the resource transfer is dependent upon future events, namely future income. Further, the "sacrifices of economic benefits arising from present obligations" of an entity disappear or are significantly reduced if a depreciable asset is sold during its useful life for an amount less than its book value. Again, liability recognition is warranted only if the asset is held to the end of its useful life. Liability recognition depends upon future events, that is, future operational decisions regarding asset disposition. *SFAS No. 109* accepts this argument since it states:...attribution of taxes to

Table 1
The Typical Pattern of Individual Deferred Tax Liabilities

Machine Costs:	$1,000,000
Salvage:	80,000
Depreciation Base:	920,000
Tax Rate:	34%
Useful Life:	5 years

Year	Double Declining Balance	Straight Line	Deferred Difference	Deferred Tax	Deferred Tax Liability
1	$400,000	$184,000	($216,000)	$73,440	$73,440
2	240,000	184,000	(56,000)	19,040	92,480
3	144,000	184,000	40,000	(13,600)	78,880
4	86,000	184,000	98,000	(33,320)	45,560
5	50,000	184,000	134,000	(45,560)	---

Table 2
Illustration of the Effects of Loss on Deferred Tax Liability

Basic Assumptions:

Year	Income (Loss) (Before Depreciation and Income Taxes)	Depreciation and Temporary Differences: Taxes	Books	Difference
1	$500,000	$400,000	$184,000	($216,000)
2	(400,000)	240,000	184,000	(56,000)
3	284,000	144,000	184,000	40,000
4	484,000	86,000	184,000	98,000
5	984,000	50,000	184,000	134,000

Year 1 Tax Provisional/Liability Computation

				Reversal Years	
	Year 1	Year 2	Year 3	Year 4	Year 5
Pre-Tax Book Income	$316,000				
Temporary Difference	(216,000)		$40,000	$98,000	$78,000
Taxable Income/Amounts	100,000		40,000	98,000	78,000
Taxes Payable/Deferred	34,000		13,600	33,320	26,520

Tax Provision for Year 1:

Current	$34,000
Deferred	73,440
Total	$107,440

Deferred Tax Liability: $73,440

Year 2 Tax Provision/Liability Computation

			Reversal Years	
	Year 2	Year 3	Year 4	Year 5
Pre-Tax Book Loss	($584,000)			
Temporary Differences	(56,000)	$40,000	$98,000	$78,000
Taxable Income/Amounts	(640,000)	40,000	98,000	134,000
Loss Carryback	100,000			
Tax Loss	(540,000)			
Loss Carryforward	272,000	(40,000)	(98,000)	(134,000)
Remaining Carryforward	(268,000)			
Taxable Amounts		0	0	0

Tax Provision for Year 2:

Current Refund	($34,000)
Deferred	(73,440)
Total	(107,440)

Deferred Tax Liability: 0

Year 3 Tax Provision/Liability Computation

		Reversal Years	
	Year 3	Year 4	Year 5
Pre-Tax Book Income	$100,000		
Temporary Difference	40,000	$98,000	$134,000
Taxable Income/Amounts	140,000	98,000	134,000
Loss Carryforward	140,000		
Tax Income (Loss)	0		
Loss Carry forward	232,000	(98,000)	(134,000)
Taxable Amounts	0	0	0

Tax Provision for Year 3:

Current Refund	0
Deferred	0
Total	0

Deferred Tax Liability: 0

individual items and events is arbitrary and, except in the simplest situations, requires estimates and approximations (FASB, 1992, par. 6). Yet, the pronouncement requires the recognition of deferred tax assets or liabilities for estimated future tax effects attributed to "temporary" differences and carryforwards.

Another question is whether a present obligation exists. Unlike all other liabilities recognized for financial reporting purposes, there is no explicit or implicit contract between the reporting entity and the creditor. At any point in time in the life of the entity, the government does not have a claim to the entity's assets for the deferred tax liability. The only time the claim arises is in the future when sufficient taxable income is reported. While the recovery of the asset through use or sale has a high probability of occurrence in a going concern (an individual event), the incidence of tax depends on the occurrence of aggregate future events that together determine whether taxable income exists.

The third aspect of the *SFAC No. 6* definition is that future sacrifices are "...a result of past transactions or events." While *SFAC No. 6* describes depreciation as an internal event (FASB, 1992, par. 138), temporary differences between taxable income and financial statement income are not caused by the event of depreciation. The differences occur because of the use of alternative methods of depreciation. Since alternative allocation schemes are allowed by law, the resulting taxable income and accounting income are caused by different allocation methods and estimates of residual value. They are not the result of "past transaction or events" since estimates of useful life and residual values must reflect future usefulness.

The Asset/Liability Inconsistency

The Board's dissenters and several commentators have criticized the inconsistencies regarding the treatment of deferred tax assets versus deferred tax liabilities in *SFAS 96*. In justifying their conclusions regarding asset recognition, the Board took an individual event perspective concluding that:

Earning financial income in future years (a) has not occurred and (b) is not inherently assumed in financial statements for the current year. The Board concluded that a deferred tax asset should not be recognized for temporary differences that result in net deductible amounts that cannot result in a refund of taxes paid in the current or preceding years (FASB, 1987, par. 100).

Adopting the same perspective, some critics of *SFAS No. 96* arrived at the opposite conclusion and have called for asset recognition on the same basis as liability recognition (Wolk, Martin, and Nichols, 1989). While adopting an individual event perspective, the Board selected a conservative approach in recognizing deferred tax assets. Deferred tax assets were only recognized to the extent that net tax operating losses can be carried back to offset taxable income (Bierman, 1990). To arrive at a political compromise, the FASB later relaxed its conservative approach and allowed asset recognition if the deferred tax asset will more likely than not be realized.

The FASB's conservative arguments against recognizing deferred tax assets can likewise be made for deferred tax liabilities. It is clear that the only way to recognize a deferred asset or liability for future reversals of temporary differences (an individual events perspective) is to make assumptions regarding future events, namely future income (an aggregate events perspective). In fact, this is exactly the argument that the Board used in *SFAS No. 109* to record a deferred tax asset for future tax effects of temporary differences or loss carry forwards:

One objective of accounting for income taxes is to recognize the amount of taxes payable or refundable for the current year. A second objective is to recognize deferred tax liabilities and assets for the future tax consequences of events that have been recognized in an enterprise's financial statements or tax returns. Ideally, the

second objective might be stated more specifically to recognize the expected future tax consequences of events that have been recognized in the financial statements or tax returns (FASB, 1992, pars.6-7).

Income Tax Allocation at the Aggregate Level

The following example illustrates how the deferred tax liability can grow over time. Assume that a company acquires a machine with a residual value of $80,000, a useful life of 5 years, and a cost of $1,000,000 every year. In addition, the company uses double declining balance depreciation for tax purposes and straight line depreciation for financial reporting. The tax rate is 34%. The effect of the assumptions on the deferred tax liability is illustrated in Table 3.

Table 3 shows that the liability reaches a constant level after five years. The resulting tax liability will not be paid unless the company fails to replace a machine as it is worn out. On the other hand, the deferred tax liability is likely to increase as the company expands and adds more machines. Further, if it is assumed that the firm is holding its productive capacity stable, it will continue to acquire new machines. These additional machines will probably cost more and lead to an increased deferred tax liability. The liability is reduced only if the firm discontinues its capital investment in new machinery and starts to curtail operations. However, there are very few industries where such an outcome is probable at the aggregate level (Magee, 1984, Ch. 5).

Any individual difference between the accounting rules used for tax purposes and those used for book purposes will follow a reversing process. If, however, several accounting phenomena are simultaneously creating tax deferrals, the nature of the aggregate deferral would not necessarily correspond to that exhibited by an individual difference.

An examination of the financial statements of many companies reveals that the deferred tax item is either stable or growing over time (Jeter and Chaney, 1988; Magee, 1984, Ch. 4). This suggests that processes such as those described in the above example exist for many firms. To the extent that this is so, the accounting profession is faced with a dilemma.

A liability is defined as a situation requiring future sacrifice of assets resulting from an unavoidable obligation. If one considers the deferred tax process as resulting from an individual difference, the deferred tax liability declines in those years where the tax payment exceeds the tax expense. An argument can be made, as the FASB has, that the deferred tax liability represents a future sacrifice of assets. However, as it is demonstrated above, liability recognition for individual differences is dependent upon future occurrence of aggregate income or loss, which clearly violates one of the criteria

Table 3
Illustration of Growth in Aggregate Deferred Tax Liability

	Year 1	Year 2	Year 3	Year 4	Year 5
Increase Due to Purchase in Current Year (t)	73.4	73.4	73.4	73.4	73.4
Increase Due to Purchase in Prior Year (t-1)		19.0	19.0	19.0	19.0
Decrease Due to Reversal From Year (t-2)			(13.6)	(13.6)	(13.6)
Decrease Due to Reversal From Year (t-3)				(33.2)	(33.2)
Decrease Due to Reversal From Year (t-4)					(45.6)
Total Increase	73.4	92.4	78.8	45.6	---
Liability Balance	73.4	165.8	244.6	290.2	290.2

for liability recognition.

If, on the other hand, one views the deferred tax process from an aggregate perspective, considering the joint effects of many differences, the deferred asset or liability balances may remain on the company's balance sheet for years. Although the item may represent a future sacrifice of assets, the sacrifice will be avoided indefinitely if the company continues to act in ways which maintain the aforementioned equilibrium. Accordingly, many deferred tax items do not satisfy the liability definition if viewed in the aggregate.

The Choice of an Accounting Perspective

The choice of perspective from which to evaluate a class of accounting phenomena should be based upon our understanding of their underlying nature. If the phenomena are seen as members of a group where each member's range of potential behavior has impact only to the extent that it contributes to the behavior of the group, then the aggregate perspective is suggested. Alternatively, if this range of potential is fully realizable for each phenomenon under normal conditions, then an individual perspective is suggested.

The act of taxation is an aggregate phenomenon. The total tax to be paid in a period of time is determined based on taxable income plus or minus tax credits or other offsets. Individual transactions or events are not "taxed." Only aggregate financial results lead to a transfer of funds to various governments. The recognition of tax expense and tax assets or liabilities on individual events is not representationally faithful.

The Board has, in fact, acknowledges the aggregate nature of income tax determination by allowing companies to utilize tax planning strategies when scheduling the future years' effects of temporary differences (FASB, 1987, par. 19). Thus, the Board recognizes that one objective of corporate tax policies is to minimize the annual tax obligations and that it is possible that all or a portion of a deferred tax obligation will not be paid.

Since the FASB's "deferred tax liability" cannot be supported from either an individual event perspective or from an aggregate perspective, the FASB should abandon the liability method of accounting for income taxes. Income tax is an aggregate event and an aggregate perspective is required in order to properly account for corporate income taxes. Partial allocation is advocated by some critics of *SFAS No. 96* and *SFAS No. 109* who have adopted an aggregate perspective. The partial allocation method recognizes that several temporary differences net out over time and never reverse (the permanent deferral) and does not require liability recognition for those items. However, there is a recognition in the method that a small class of temporary differences are distinct enough that an individual event perspective is required. These temporary differences are deemed likely to reverse and a liability or asset is recognized. The adoption of partial allocation is not appropriate for two reasons. First, the income tax is based on the aggregate taxable income of the enterprise. Therefore, mixing individual and aggregate perspectives in arriving at the appropriate accounting is inconsistent. Second, the assertion that temporary differences cannot result in liabilities without presuming future taxable income also applies to the temporary differences that are "likely" to reverse.

The Impact of Implementing the Flow Through Method

All deferred tax account balances will be combined with equity balances when the flow through method is first implemented. To assess the economic consequences of this accounting method change, the debt-to-equity ratios of a sample of industrial (i.e., mainly manufacturing) companies with substantial deferred tax balances are analyzed. The debt-to-equity ratio is chosen because this ratio best portrays the riskiness of a firm. In addition, reclassifying deferred tax balances as equity has its greatest impact on the

debt-to-equity ratio, while the impact on return on assets, return on equity, and earnings per share measures is slight.

The 1995 edition of *Moody's Industrial Manual* is used to create a sample of 112 manufacturing companies. The sample is randomly selected, except that the company chosen must have net deferred tax balances and positive equity amounts for the year 1994 (latest year available). Next, the sample is divided into five categories. First, 17 companies with 1994 deferred tax balances in excess of $850 million are chosen. Second, the remaining 95 companies are divided into four groups of roughly equal size according to the amount of their total assets. Total liability and equity amounts for 1994 are determined, along with the deferred tax amounts for 1992 and 1993 to observe whether these accounts have growing balances. The latter is a frequent assertion of the critics of deferred tax standards.

Using the total liability and equity amounts, debt-to-equity ratios are computed. Next, the net deferred tax balances (all net balances were credits or liabilities) are deducted from total liabilities and added to total equities. These adjusted amounts form the basis of the new debt-to-equity ratios. Finally, the differences in the debt-to-equity ratios are computed and one-tailed (the debt-to-equity ratios will decline) t-tests are carried out to determine whether these differences are statistically significant.

Table 4 summarizes the results of the empirical tests and observations. The group with the large deferred tax balances exhibits the maximum impact of eliminating these balances, with a difference of 29% decrease in the average debt-to-equity ratio. The four groups that are categorized by their total assets exhibit changes in their debt-to-equity ratios ranging from 19% (500 < total assets < 1,000) to 9% (total assets > 1,000). All of the group differences are significant at 99% ($\mu = .01$) or above. Finally, the Appendix shows that the average deferred tax account balances have grown each year (1992-1994).

Thus, the implementation of the flow through method will result in significant changes in a key ratio that is used in the financial evaluation of most manufacturing companies. Conversely, the debt-to-equity ratios used at present in the financial evaluation of companies are flawed because the net deferred tax balances are included in liabilities, when it is clear that these

Table 4
Summary of Empirical Tests & Observations

Group (in millions)	Sample Size	DTERB (Average)	DTERA (Average)	DIF (Average)	t-stat	Significance Level of DIF
DT > $850	17	3.04	2.17	0.87	6.39	> 99%
$50 < TA < $100	24	1.07	0.94	0.13	5.91	> 99%
$100 < TA < $500	24	1.68	1.38	0.30	2.42	> 99%
$500 < TA < $1,000	25	2.16	1.74	0.42	3.62	> 99%
TA > $1,000	22	1.70	1.55	0.15	3.75	> 99%
Entire Sample	112	1.87	1.52	0.35		

Legend:

DT = Net deferred tax balances; TA = Total assets; DTERB = Debt-to-equity ratio before reclassifying DT as equity; DTERA = Debt-to-equity ratio after reclassifying DT as equity; and DIF = DTERB - DTERA.

accounts do not meet the liability criteria specified in accounting theory.

Conclusion

This paper argues that the use of inconsistent perspectives by the *SFAS No. 96* and *SFAS No. 109* are the basis of the disagreements most critics have with the Board's positions. The simultaneous use of both the individual and aggregate perspectives as the basis of the Board's decisions is the source of these disagreements. The FASB adopted both individual and aggregate event perspectives, thus arguing both sides of the coin simultaneously and drawing insupportable conclusions regarding the recognition of liabilities and assets.

Some of the opponents of *SFAS No. 96* and *SFAS No. 109* have criticized the Statements from an individual event perspective. They have recommended that (1) *SFAS Nos. 96 and 109* modify the liability method to allow the discounting of the deferred tax liability, (2) *SFAS No. 96* be modified so that asset and liability recognition is consistent (which was done under *SFAS No. 109)*, or (3) both *SFAS Nos. 96 and 109* be dropped in favor of the "net of tax" method. Other opponents of the Board's position have argued from the aggregate perspective and advocated that the liability method be abandoned in favor of the partial allocation approach. Many other opponents have argued that the standards are too complex, too costly to apply, and fail tests of usefulness.

This study concludes that the taxation of a corporation is an aggregate phenomenon and an aggregate perspective is required. Based upon this, the study advocates the adoption of the flow through method of income tax accounting along with adequate disclosure of the potential effects of temporary differences as an appropriation of retained earning and in footnotes. In addition, the flow through method has conceptual merit and eliminates the implementation complexity that has plagued the FASB for decades. The FASB should reconsider the entire income tax accounting issue, giving serious consideration to the unit problem presented in this paper. The controversy will not diminish until such action is taken.

Suggestions for Future Research

Future research can examine the impact of using the flow through method of income tax accounting on net income, and earnings per share. In addition, the economic consequences of this accounting change should be analyzed by observing its impact, if any, on share prices and stock returns. Finally, it will be interesting to see if the adoption of this accounting change ensures the consideration of the unit problem during other FASB deliberations. 🕮

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