

Tax law and accounting assignment

Law



Tax Law and Accounting As much as everyone hates the “ T” word, taxes are an essential part of our society. Taxes pay for many of the services we are entitled to as citizens of the United States. Services like the military, Medicare, and welfare are all paid for with tax dollars. Taxes often fund things that stir up quite the controversy because of the service provided, but they are important nonetheless. There are different levels of taxes as well. There are Federal taxes, which cover what was mentioned above. There are state taxes that cover services on a state level, such as highway’s and state parks.

Then there are local city taxes that pay for emergency services and local recreational parks. There is not a day that goes by that American’s do not see their tax dollars at work, but yet, people do not want to pay taxes. No nation can stand and succeed without an efficient taxation system. Here in the United States, we have a very complex tax system. To monitor the taxes, we have the Internal Revenue Service (IRS). The job of the IRS is to make sure all the tax laws are followed and enforce the laws. The three letters IRS scare every citizen in the United States because of the power they have.

A person can fill out every form right, file correctly every year and still worry about the potential IRS tax audit. As time goes on and the Federal deficit grows, there is always more fear of audits, especially if they have large returns coming back to them. The best line of action an individual can take is to dot their I’s and cross their T’s and save all back up documents for 7 rolling years and keep them together. Tax laws change on a very frequent basis. These changes can be to add to existing tax laws or to take away from existing laws. An example of these changes was seen very recently.

When the housing market “ crashed,” many people lost their houses and this caused potential buyers decided to keep renting for a variety of reasons. To counter act this, the Government started offering tax credits for first time home buyers to try to jump start the market. Then, the tax credit was extended for another year to continue promoting the housing market to continue to recover. There have been many statutes introduced over the years similar to this one. Another example is the tax credit for purchasing fuel efficient cars. The thing about these statutes is there is usually a cap on them.

The caps are either a specific amount of time (years) and total amount the Government is willing to give out. There are many objectives of the modern tax statutes but ultimately, the statutes are set to try to control the economy. A normal individual hears about taxes and they automatically assume personal taxes. However, taxes also affect businesses in more ways then. Not only does the company have to account for sales tax, but they also have to worry about income tax. This can prove to be difficult for some because of the differences in income tax accounting and Generally Accepted Accounting Principles (GAAP).

This can be a hard concept to grasp because during all years a person is learning about accounting, GAAP is the king. GAAP is what is learned from day one until it is all finished so by adding income tax accounting in the mix is like throwing a wrench into a set of gears for some. There are distinct differences between GAAP and tax accounting. One of the main differences is the regulators. Tax accounting is regulated by Internal Revenue Code (IRC) whereas GAAP is regulated by the Financial Accounting Standards Board
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(FASB). GAAP is an American term of how the United States requires companies to prepare financial statements.

Tax accounting is designed to focus exclusively on how a company accounts for their taxes. With tax accounting, there are typically two different methods used for tax accounting. The cash method and the accrual method are the methods typically used. There are others used as well but they must be approved by the IRS before a company can use them. GAAP has more methods of reporting that can be used. The biggest difference in GAAP and tax accounting is their uses. Tax accounting is used for income tax accounting and GAAP is used for reporting the financial statements to FASB.

The reason the difference is needed is because tax accounting and GAAP are two separate items. GAAP covers the overall financial reporting and tax accounting focuses on the reporting of the taxes. With all the tax statutes and laws in effect, it is not feasible for FASB to have to monitor the numbers and the tax laws. By keeping the two separate like they are, it allows the regulating board of the IRC to do their jobs. Ultimately, this allows for more accurate numbers to be reported in financial statements and with their tax reporting. One of the many duties of the IRS is to watch for tax evasion and avoidance.

Many individuals interpret these as the same, and these individuals are mistaken. According to Investorwords. com (2010), tax evasion is, “ Illegally avoiding paying taxes, failing to report, or reporting inaccurately. The government imposes strict and serious penalties for tax evasion. Tax evasion is different from tax avoidance, which is making use of legal methods to

minimize a tax burden” (definition). Whereas tax avoidance is, “ Lawful minimization of tax liability through sound financial planning techniques such as phasing the sale of assets over a period long enough to effect maximum exemption from capital gains tax.

Whereas tax avoidance is legal, tax evasion is not” (Businessdictionary. com, 2010). As it is shown here, tax evasion is illegal where tax avoidance is a legal way to pay less in taxes. Tax evasion is what dominates the news though. Tax evasion was prominent in history with mobsters like Al Capone, and remains relevant today, such as the accused actor Wesley Snipes. The biggest thing to remember is avoidance is not illegal, it is just dumping assets, where as evasion is refusing to pay altogether. Taxes play a very dominate role just like they should.

However, due to the importance of reporting from businesses and individuals, taxes need to be monitored and restructured very closely. The IRS and the IRC are there to ensure that they filings and laws are followed. These two regulating organization keep order in a very complex world and therefore need to be strict like they are. References Businessdictionary. com. (2010). Tax Avoidance. Retrieved from <http://www.businessdictionary.com/definition/tax-avoidance.html> Investorwords. com. (2010). Tax Evasion. Retrieved from http://www.investorwords.com/4895/tax_evasion.html