Tax law and accounting paper assignment

Law

Tax Law and Accounting Paper In today's financial world, preparation and reporting of income taxes has become one among the other main reasons why individuals and businesses are keeping and maintain their financial records. However, there has been some controversy between tax laws and accounting under the General Accepted Accounting Principles (GAAP). Simply because IRS is not always agrees with GAAP's principles and thus creates its own tax laws. This paper will discuss the objectives of modern income tax statutes, compare and contrast the GAAS and tax accounting, and differentiate between tax avoidance and tax evasion.

Objectives of Modern Income Tax Statutes The primary objective of the modern income tax statutes was to amend the U. S. Constitution to permit the passage of a federal income tax law in order to collect enough revenues for supporting all government operations (Anderson et. al. , 2008, p. 1-2). Simply because before this amendment, it was ruled by the Supreme Court in 1895, that the tax was in violation of the U. S. Constitution and people were taxed only when the government was in a huge need for more resources (Anderson et. al. , 2008, p. 1-2).

In addition, there are three more objectives of modern income tax statutes. First one is the economic objective that is mainly concerned with stimulation of private investment, reducing unemployment, and mitigate the effects of inflation on the economy (Anderson et. al. , 2008, p. 1-14). Another objective, was a governments attempt to increase certain activities such as creating a good opportunities for opening specialized industries and small businesses. The opportunities included the allowing to write-off all business expenses and paying taxes of the net income.

Moreover, the businesses were expected to pay the reduced corporate tax rates in addition to all individual tax deductions and exemptions, which help individuals and businesses to avoid suffering the tax increases due to the inflation increases. Third objective, was to create a pension plans for the people who are paying taxes, encourage people to contribute to charitable organizations, and discourage others from activities that are contrary to public policy. GAAP vs. Tax Accounting Generally Accepted Accounting Principles (GAAP) is a set of rules created by the Financial Accounting Standards Board (FASB) which are used to prepare ompany's financial statements for reporting purposes. The GAAP simply provide guidance to financial statements preparers on how to account for various types of transactions (Ruppel, 2004, p. 2). While the tax accounting is mainly concerned with preparing statements and reports that are in compliance with the IRS tax laws. According to Plesko (2004), one of the differences between GAAP and tax accounting is that from a tax administration perspective, the book income under the GAAP accounting provides a separate measure of the income and expense items that can be compared to the values reported on the tax return (p.). This mainly results because the GAAP allows any method for income recognition, but IRS uses the cash basis for tax returns. Other differences are the depreciation methods used for asset depreciation. The GAAP typically allows straight line or other acceptable methods, while the Tax Accounting prefers using the MACRS method (White, 2008, p. 1). Another difference includes the interest revenue recognition. Under the GAAP accounting interest revenue is recognized when earned, but under the Tax Accounting the municipal interest income is exempt for tax purposes.

Tax Avoidance vs. Tax Evasion Tax Avoidance is the process of minimizing the tax amount trough legal, but aggressive, tax planning strategies (Perez, 2008, Ch1). It is basically a legal process of avoiding paying too much taxes through finding tax loopholes, by using the existing tax laws at own advantage (Murray, 2008). One example of tax avoidance was shown by Browning in her article, IRS Aims to Curb Offshore Tax-Avoidance Tactic, where she showing on how internationally trading companies try to avoid taxes by using the transfer pricing tactics.

The transfer pricing tactic stands for companies transferring their income back overseas by undercharging or overpaying foreign subsidiaries for goods and services (2008, p. 6). While such companies are supposed to calculate those prices as if they were between independent entities and pay taxes, typically 35 percent, on profits brought back to the United States (Browning, 2008, p. 6). Other examples of tax avoidance include but not limited to various tax allowances for education, medical bills, to reduce some amount for each depended, etc.

Tax evasion, on the other hand, is the other side of the tax avoidance and is considered to be a crime. It is a willfully attempt to evade or defeat the payment of federal income taxes (Lectric Law, 2008). The tax evasion involves failing to report an income, or improperly failing deductions which are not authorized by the IRS. Stark (2008), provides some examples of tax evasion. First example includes sales tax evasion, when a retailer offers to let a customer pay cash and provide a false out-of-state address to avoid paying the city’s sales tax (2008).

Another example, includes evasion of business income tax by either inflating the business expenses, such as cost of goods, to lower the business tax liability, or by suggesting reporting only credit card sales, or the company's owner decides to use his corporate credit card to pay for family vacations, entertaining personal friends, and buying flowers for his wife (Stark, 2008). In addition, tax evasions can be done be individuals same as by the businesses. For example, one can claim a different residence address on their tax return, from the state with lower tax rate, this can be a vacation home, etc. Stark, 2008). Conclusion Income tax is the percentage of money individuals and businesses pay on their income, which is necessary for supporting all government operations. All publicly traded businesses are required to prepare their financial statements in accordance with GAAP regulations. However, when preparing their income tax reports, businesses need to be sure that their financial statements in accordance with tax laws in order to avoid penalties. Simply, because tax laws are not always same as the GAAP regulations and therefore accountants need to know the differences.

Moreover, accountants need to know what the lawful tax avoidance is and what the unlawful tax evasions are. Reference AllBusiness. com (2008). What are Generally Accepted Accounting Principles? Retrieved May 6, 2010, from http://www. allbusiness. com/accounting/methods-standards-generally-accepted-accounting/1261-1. html Anderson K. , Kramer J. , and Pope T. , (2008). Prentice Hall's Federal Taxation 2008: Individuals. Retrieved May 6, 2010, from University of Phoenix, open rEsources, Income Tax Accounting

Course, 21st ed. , Pearson Education Inc. Browning L. , (2008), IRS Aims to Curb Offshore