

Calculating Federal Income Tax

Corporations anticipating annual federal income taxes of \$500.00 or more are required to pay their estimated taxes each quarter. Estimated income tax is paid in quarterly installments in April, June, September, and December. However, the actual federal income tax owed is calculated at the end of the fiscal year. Based on the actual income tax owed for a year, a corporation must file an annual return. Any additional tax owed that was not paid in quarterly installments must be paid when the final return is filed.

Sample Problem: Hobby Shack

Early in 2017, Hobby Shack estimated \$18,000.00 federal income tax for the year. Hobby Shack paid \$4,500.00 in each quarterly installment for a total of \$18,000.00. Each tax payment is recorded as a debit to Federal Income Tax Expense and a credit to Cash.

Federal income tax is an expense of a corporation. However, the amount of tax depends on net income before the tax is recorded. Federal Income Tax Expense is an expense account. The account appears under the major division titled "Income Tax Expense" in Hobby Shack's chart of accounts. Federal Income Tax Payable, a liability account, appears under the heading "Current Liabilities".

In order to make adjustments to federal income tax, you must first determine the net income before federal income tax expense. To calculate, follow these steps:

1. Complete all other adjustments on a worksheet.
2. Extend all amounts except Federal Income Tax Expense to the Income Statement or Balance Sheet columns.
3. On a separate sheet of paper, total the worksheet's Income Statement columns.
4. Calculate the difference between the Income Statement debit and columns. This difference is the net income before federal income tax expense.

Total of Income Statement Credit Column	\$500,253.10
Total of Income Statement Debit Column (excluding Federal Income Tax Expense)	- <u>396,049.91</u>
Net Income Before Federal Income Tax	\$104,203.19

The amount of federal income tax expense a corporation must pay is calculated using a tax rate table furnished by the IRS. Different tax percentages are applied to different portions of the net income (15% on first \$50,000, plus 25% on the next \$25,000, plus 34% on the next \$25,000, etc.) to determine the total federal income tax owed. Hobby Shack's net income before federal income tax is \$104,203.19. Based on the IRS tax tables, Hobby Shack owes \$23,889.24 in federal income tax. The company has already paid \$18,000.00 in estimated payments, so the adjusting entry will be for \$5,889.24 to reflect the additional taxes owed.

Federal Income Tax (from tax tables)	\$23,889.24
Total of Quarterly Installments	- <u>18,000.00</u>
Federal Income Tax Adjustment	\$ 5,889.24

Enter the adjusting entry as a debit to Federal Income Tax Expense and a credit to Federal Income Tax Payable. After the adjusting entry for federal income tax expense has been recorded, the worksheet is ready to be completed. Income Statement columns are used to calculate net income after federal income tax.

TRIAL BALANCE (as of December 31, 2017)

ACCOUNT TITLE	Trial Balance		Adjustments		Income Statement		Balance Sheet	
	Debit	Credit	Debit	Credit	Debit	Credit	Debit	Credit
<i>Accounts Payable</i>		11,583.03						11,583.03
<i>Federal Income Tax Payable</i>				5,889.24				5,889.24
<i>Supplies Expense</i>			2,910.00		2,910.00			
<i>Uncollectible Accounts Expense</i>			1,245.00		1,245.00			
<i>Utilities Expense</i>	3,820.00				3,820.00			
<i>Federal Income Tax Expense</i>	18,000.00		5,889.24		23,889.24			
TOTALS	670,861.59	670,861.59	43,574.24	43,574.24	419,939.15	500,253.10	269,846.68	189,532.73
<i>Net Income after Federal Income Tax</i>					80,313.95			80,313.95
TOTALS					500,253.10	500,253.10	269,846.68	269,846.68

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2017 Date	Account Title	Doc. No.	Post. Ref.	Debit	Credit
December 31	<i>Federal Income Tax Expense</i>			5,889.24	
	<i>Federal Income Tax Payable</i>				5,889.24