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DEFERRED TAX – MADE SIMPLE

It's not extra tax. It's just a timing difference.

1. WHAT IS DEFERRED TAX?

Deferred tax is tax that will be paid or saved in the future because accounting rules and tax rules recognise income or expenses at **different times.**

TWO SETS OF RULES

ACCOUNTANT		LHDN (TAX)
Follows Accounting Standards	≠	Follows Income Tax Act
Calculates Accounting Profit		Calculates Taxable Profit

Sometimes they don't agree **TODAY**, but they usually agree **LATER**.
That "later" creates **DEFERRED TAX.**

2. HOW DOES IT ARISE? (TEMPORARY DIFFERENCES)

A. DEFERRED TAX LIABILITY (DTL)

Pay **less tax** today,
Pay **more** tax **later.**

EXAMPLE: CAPITAL ALLOWANCE vs DEPRECIATION

You buy a machine for RM100,000

Year	Accounting (Depreciation)	Tax (LHDN) (Capital Allowance)
1	Expense RM10,000	Deduction RM40,000
Taxable Profit	Higher	Lower
Tax Paid Today	More	Less

You pay LESS tax today, but LHDN will allow LESS deduction in future years.
The future extra tax you will pay =
DEFERRED TAX LIABILITY (DTL)

YEAR 1		YEAR 2		YEAR n
Less tax paid today	→	More tax paid later	→	Eventually equals out

B. DEFERRED TAX ASSET (DTA)

Pay **more** tax today,
Pay **less** tax later.

EXAMPLE: OUTSTANDING LEAVE PROVISION

Employees earn leave, but not yet paid.

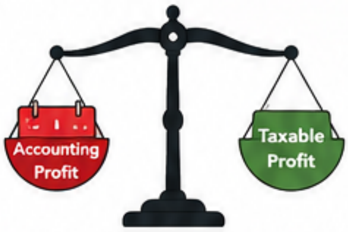
Year	Accounting (Expense)	Tax (LHDN) (Allowed Deduction)
1	Expense RM50,000	Deduction RM0
Taxable Profit	Lower	Higher
Tax Paid Today	More	More

You pay MORE tax today, but LHDN will allow the deduction in future when paid.
The future tax benefit you will receive =
DEFERRED TAX ASSET (DTA)

YEAR 1		YEAR 2		YEAR n
More tax paid today	→	Less tax benefit later	→	Eventually equals out

3. KEY RULE TO REMEMBER

Deferred tax arises because of **TEMPORARY DIFFERENCES** between accounting profit and taxable profit.



Different today, Same later.

4. QUICK COMPARISON

Item	Deferred Tax Liability (DTL)	Deferred Tax Asset (DTA)
What it means	You will pay more tax in the future.	You will pay less tax in the future.
Reason	Taxable profit today < Accounting profit today	Taxable profit today > Accounting profit today
Effect on tax paid today	Less tax paid today	More tax paid today
Effect in future	More tax to be paid later	Less tax (benefit) later
How it appears in Balance Sheet	Liability (Current or Non-current)	Asset (Current or Non-current)
Example	Capital allowance > Depreciation Provision not allowed by LHDN	Leave provision Bonus provision (not yet paid) Doubtful debt provision (if not allowed by LHDN yet)
Journal Entry	**Dr Tax Expense** **Cr Deferred Tax Liability**	**Dr Deferred Tax Asset** **Cr Tax Expense**

5. COMMON MALAYSIAN EXAMPLES

✓ Creates Deferred Tax (Temporary Difference)

- Capital Allowance vs Depreciation
- Leave Provision
- Bonus Provision (not yet paid)
- Doubtful Debt Provision
- Warranty Provision
- Prepaid Expenses (different period)

✗ Does NOT create Deferred Tax (Permanent Difference)

- Entertainment Expenses (non-deductible)
- Fines / Penalties / Traffic Summons
- Donations not tax deductible
- Non-deductible expenses under Income Tax Act

6. IMPACT ON FINANCIAL STATEMENTS

Income Statement

Tax Expense
= Current Tax Expense
+ / – Deferred Tax
(Expense or Income)

Balance Sheet

Show Deferred Tax Asset or Deferred Tax Liability
(Net of each other if allowed)

7. ONE SENTENCE TO REMEMBER

"Deferred tax arises because accounting standards and tax laws recognise income and expenses at different times, creating temporary differences that reverse in future periods."

MEMORY TRICK

DTL = Delayed Tax Payment
(I saved tax today, will pay later)

DTA = Delayed Tax Benefit
(I paid more tax today, will get benefit later)

★ IMPORTANT NOTE

Deferred tax is **NOT** cash.
It is an **accounting adjustment** based on timing differences.

Over time, temporary differences reverse, and deferred tax balances become zero.

8. SIMPLE STORY

Deferred Tax Liability (DTL)

You pay RM60 tax today instead of RM100. → Later, you pay the remaining RM40. → Total tax over time = RM100 (same in the end)

Deferred Tax Asset (DTA)

You pay RM140 tax today instead of RM100. → Later, you get RM40 tax relief. → Total tax over time = RM100 (same in the end)