How deferred tax assets and liabilities influence US stock prices

This research seeks to determine which parts of deferred tax assets and liabilities are most informative. These data are gathered from the annual report footnote disclosures for the companies within the Fortune 500. The data are then sorted into common categories. The most informative components then are determined from correlation and regression.

Keywords: deferred tax assets, deferred tax liabilities, Fortune 500, price.

Introduction

For many years in all countries, expert advisers, brokers, investors, and creditors have thoroughly reviewed the main text of the financial statements to make predictions about companies’ futures. However, only recently have they in large numbers continued their review by looking at the footnotes to the financial statements.

In the US then, issues exist that some other countries do not experience. The US has two systems of determining income, one for determining financial accounting income (book income) under generally accepted accounting principles (GAAP) and one for determining taxable income as the basis for ascertaining how much must be paid to the government. Even though public company financial statements must be released, US company tax returns are not publicly disclosed. Because the financial statements must not omit any material fact, public companies must provide reconciling information between book and taxable income in the financial statements. These disclosures are in the general categories of deferred tax assets (DTAs), representing tax obligations already paid but not included on the books, and deferred tax liabilities (DTLs), representing future tax obligations already included on the books. Financial statement users generally view the DTAs as beneficial to future

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earnings but DTLs as detrimental to future earnings. However, this view is not always accurate.

For some reason in the US, the deferred tax items, such as this deferred tax liability, provide incremental information to determining stock prices. This research seeks to determine which components of DTAs and DTLs are more informative of price than others.

The objective of this research is to determine which components of DTAs and DTLs are making the aggregate accounts of DTA and DTL so influential toward US stock prices.

The following tasks are necessary to reach that objective:

- Hand collection of the annual report footnote disclosures for every Fortune 500 company;
- Sorting of the components of DTAs and DTLs reported in each disclosure into common categories;
- Use of Pearson correlations and linear regression on price to determine which components influence price;
- Discussion of the results.

The research methods applied include evaluating and discussing the relevant literature; evaluating and sorting company information; running Pearson correlations and linear regressions on price; and anything else incidental to meeting the objective.

The research results are that the following components of deferred tax assets (DTAs) and deferred tax liabilities (DTLs) provide statistically significant influences on US stock prices: the DTAs of unearned income, tax carry forwards, bad debt allowances, long-term debt items, reserves, and accrued expenses and the DTLs of prepaid expenses, deferred revenue, unrealized gains, and other items. The following influence price to increase as they increase: the DTAs of long-term debt items and accrued expenses and the DTLs of deferred revenue, unrealized gains, and other items. The others predict price to decrease as they increase.

The reason for this lack of inquiry into an extraordinarily important series of disclosures is that these components are disclosed in footnotes to the financial statements, and no computerized database has included them to date. Thus, these data must be hand collected and hand sorted. Even worse, there is no standardized means of reporting these components within the footnotes, so different terms prevail. With the ease of use of computers, researchers have difficulty wanting to return to the laborious days of gathering and sorting data on their own. Instead, they find other interests to pursue and leave this extraordinarily important task to some other time.

Depreciation provides the most commonly occurring example of deferred tax items. For book purposes in the US, most companies utilize straight-line depreciation. This method takes the number of years of useful life for equipment and divides the cost of the property (less any salvage value) by this number of years. The result becomes the number for depreciation expense for that item on the income statement.

However, for tax, the government provides companies with accelerated depreciation options. They can write off $250,000 of the property purchased immediately as cost recovery subject to limits on the dollar number of property placed in service during the year and only to the extent of business income. Then, companies in recent years have also received the bonus depreciation deduction of 50 percent of the cost of property placed in service during the current year (after deducting any of the
$250,000 write offs taken). These previous cost recoveries under depreciation can be utilized only in the first year of placing the property in service. The accelerated depreciation present every year is under the modified accelerated cost recovery system (MACRS). This system begins depreciation cost recoveries at two times the straight-line number after making some changes for the half-year convention.

For instance, some hypothetical company purchased and started using $500,000 of equipment last year. The useful life of the equipment is 10 years, and no salvage value is expected for the time at the end of its useful life. Thus, book depreciation in that year would be $50,000.

However, for tax, $250,000 could be written off immediately. Then, bonus depreciation would be determined at 50 percent times that $250,000, resulting in $125,000 more of cost recovery. Finally, the remaining $125,000 would be subjected to MACRS. Under this accelerated system, the 10 percent written off each year under straight-line depreciation is taken times two. This 20 percent number (only in the first year and, if it is before the property is fully depreciated, the year of sale) is taken times the fraction of 1 over 2. The result of 10 percent is then taken times the remaining $125,000 to get $12,500. The total tax depreciation would be $387,500.

The difference between book and tax depreciation is $337,500. Because depreciation is an expense, it reduces book and taxable income. Here, taxable income would be reduced more than book income. The corporate income tax in the US is 35 percent on average. If the company had $1,000,000 of book net income without any other differences from the tax income except for depreciation, the journal entry would be the following:

Income Tax Expense (Book tax expense) ($950,000 times 35 percent) $332,500
Deferred Tax Liabilities (balancing figure or $337,500 times 35 percent) $118,125
Income Taxes Payable (paid to the government) ($612,500 times 35 percent) $214,375

The other example involves unrealized gains here. This category also is includable within other comprehensive income. For instance, the hypothetical company could purchase derivatives to lock in energy prices and remove the risk from fluctuations in these prices. Investors would consider such moves as successful management.

However, companies must mark these prices to market. This rule means that, at the end of every reporting period, companies should report the derivatives at fair value on the balance sheet. Any changes in fair value would be placed on the income statement, resulting in gain realization.

Nevertheless, for tax purposes then, no gain would be reported. The tax system requires four hoops to be successfully negotiated before some item can be placed on the tax return. The first hoop is the realization hoop. This item just requires an economic event to occur, such as sales, exchanges, trades, etc. Here, without any sale or exchange, there would not be any realization.

However, if this hoop were successfully negotiated, the next hoop would be the recognition one. At this stage then, certain provisions of the tax code emphasize substance over form. Thus, if an entity has merely changed its form as from sole proprietorship to any corporation, Internal Revenue Code (IRC) 351 would make that realized gain not recognized and therein not have to be reported on the income tax.
return. However, only property could be used in exchange for the stock, and 80 percent control would have to be purchased in the transaction.

Any services provided do not count toward the 80 percent control and must be recognized as gain here. The exception is if property worth at least 10 percent of the value of the services is provided as well.

Anything sent to the shareholder other than qualifying stock becomes boot. This boot must be recognized to the lesser of the realized gain or boot received.

Any liabilities transferred to the corporation could result in boot treatment. If liabilities are greater than the basis of assets transferred, IRC 357(c) requires treatment of that difference as boot. Thus, the lesser of the realized gain or boot received must be recognized.

If any personal use liabilities are transferred with business use liabilities in the IRC 351 exchange, all the liabilities transferred are considered to be boot. Then, the lesser of the realized gain or boot received must be recognized.

If the entity moved from sole proprietorship to any partnership, IRC 721 would make that realized gain not recognized. Any services transferred result in gain recognition. However, the rules for qualifying are less difficult here. IRC 721 can work for transfers from corporate to partnership form because there is no change in substance.

IRC 368 provides nonrecognition treatment for corporate reorganizations. However, sufficient control must be purchased. Mergers under state law qualify here. Stock-for-stock acquisitions meet the conditions under B reorganizations. Assets-for-stock acquisitions qualify if 80 percent control is purchased through the use of stock under C reorganizations.

Spinoffs, split-offs, and split-ups also qualify under D reorganizations. Changes in names, place of incorporation, or capitalization qualify under E and F reorganizations.

If real estate were traded for real estate, IRC 1031 would provide nonrecognition treatment. If personality were traded for personality, IRC 1031 would provide nonrecognition treatment. However, realty for personality or personality for realty would not work. Likewise, stock or partnership interests for stock or partnership interests would not work.

If property were destroyed through natural disasters or government condemnation, then IRC 1033 would provide nonrecognition treatment. Here, the proceeds would have to be utilized within certain time periods for certain qualifying property to get the nonrecognition treatment.

The next hoop is the disallowed hoop. This hoop applies only to losses, which are not put on the tax return as they are generated from non-arm’s length transactions between related parties.

The final hoop is the character hoop. This part classifies the type of gain or loss so that it can be placed in the proper place on the income tax return.

For the purposes here, the derivatives are not put on the income tax return because there is no realization event. They are not sold, exchanged, traded, etc. Thus, even though the income statement reports gain for any increase in fair value, the income tax return would not report that gain at all. Thus, this temporary difference exists until the derivatives experience that realization event and move through all four hoops.

Thus, if the derivative gain for book purposes is $100,000, the gain for tax purposes is $0. The journal entry would be the following:
Income Tax Expense ($100,000 times 35 percent) $35,000

Deferred Tax Liabilities ($100,000 times 35 percent) $35,000

**Background**

Studies have demonstrated that in aggregate DTAs and DTLs provide incremental value to predicting US stock prices (Ayers, et al., 2009; Chen, et al., 2007; Hanlon, 2005; Lev, Nissim, 2004). However, this important set of discoveries provides little help to individuals trying to utilize this information. There are so many components to DTAs and DTLs that they cannot determine why these categories should be informative (Graham, et al., 2010). Even more important then, these individuals cannot ascertain which components drive the incremental informational content of DTAs and DTLs (Graham, et al., 2010). No extant research has shown which ones are predictive of stock prices (Graham, et al., 2010). However, some of the most prominent economists and tax researchers have remarked that this research should be the top priority (Graham, et al. 2010). Thus, this research seeks to show which elements are predictive.

The importance of DTAs and DTLs to stock price emerges from the fact that they signal to the market how well each company is minimizing taxes (Hanlon, Heitzman, 2009). These items also show the quality of earnings by disclosing to some extent whether earnings management is occurring (Seidman, 2008; Dhaliwal, et al., 2004).

Large book-tax differences tend to signal successful companies. DTLs in aggregate tend to be larger than DTAs for successful companies (Poterba, et al., 2009). Depreciation of property, plant, and equipment tends to be the largest category (Poterba, et al., 2009).

The timing of differences in book and tax reversing influences stock prices differentially (Guenther, Sansing, 2004). Some researchers believe that deferred tax items’ influences on stock prices are not immediate but instead delayed (Thomas, Zhang, 2007).

**Sample**

As hand collection is the rule here, the companies of the Fortune 500 provide the sample for this research. The Fortune 500 index is the most prestigious measure of successful companies in the US. Other researchers have utilized this index before in their research endeavors. In tax, this sample set has especially been useful (Lev, Nissim, 2004). The prices for these companies are gathered utilizing Compustat.

**Methodology**

The methodology to this research is to correlate and regress on price changes from the end of 2008 through the end of 2009. This fact means that close to 1,000 company years have been gathered. The annual reports for each of the Fortune 500 companies are consulted to compile the deferred tax information from their footnotes. The information is sorted into 25 DTA categories and 12 DTL categories. The reason for this disparity is that companies tend to be more specific in describing their assets and less specific in describing their liabilities. This tendency should be somewhat expected as it exists in other areas of financial statement reporting.
The DTA variables are depreciation (Depr.); employee benefits (EB); inventory (Inv.); employee equity compensation plans (ESOP); unearned income (Unearn.); unrealized losses (Unreal.); items from partners and subsidiaries (Eq. Meth.); self-insurance reserves and other insurance items (Ins.); net operating loss, credit, capital loss, and other tax carry forwards (NOL, etc.); net operating loss carry forwards (NOL); tax credit carry forwards (Credit); research and development tax credit carry forwards (R&D Cred.); capital loss carry forwards (Cap. Loss); foreign tax credits (FTC); state and local tax deductibility carry forwards (Tax Bene.); bad debt allowances (Bad Debts); lease activities (Leases); capitalized expenditures (Cap. R&D); long-term debt related items (Acq. Loans); securitization activities (Securi.); legal reserves (Reserves); customer rewards (Rewards); intangible items (Intan.); accrued expenses (Acc. Exp.); and other items, which include less than 5 percent of the total that do not have to be disclosed separately, (Other).

The DTL variables include depreciation (Depr.); employee benefits (EB); inventory (Inv.); prepaid expenses (Pre. Exp.); deferred revenues (Def. Rev.); unrealized gains on other comprehensive income items (Unreal.); items from partners and subsidiaries (Eq. Meth.); intangible items (Intan.); long-term debt related items (Discount); leasing activities (Leasing); servicing assets (Serv. Assets); and other items, which are less than 5 percent of the total that do not have to be disclosed separately, (Other).

Depreciation represents the difference between accelerated cost recovery under the tax system and the general trend toward straight-line depreciation for book purposes. The reason for the difference is that the tax system wants to stimulate capital acquisition through in effect lowering the price of these goods through providing more cost recovery in early years as tax deductions. The financial reasoning for straight-line is establishing systematic and rational allocation of expense over time.

The category of employee benefits stands for all types of employee compensation other than in equity. The difference results from employee compensation beyond salary and wages not being currently deductible for tax purposes.

Inventory represents the fact that, for tax, certain inventory items can be capitalized under UNICAP. However, for book, they would not be. Also, for book, lower of cost or market adjustments to inventory on hand can be made before these items’ sale. The tax system does not permit these lower of cost or market adjustments to be recognized as deductions on the tax return until the inventory is sold.

Employee equity compensation plans signify employers’ provision of stock or options to employees as part of their compensation. Differences exist because of financial reporting being more expedient in realizing and recognizing gains thereon than the tax system.

Unearned income emerges from situations where customers must give cash in advance of the receipt of goods or services. For tax purposes then, on receipt, this cash advance is required to be recognized as income on the tax return. However, for book purposes, the receipt is not recognized as income until the payments have been earned through the provision of goods or services.

Unrealized losses involve investments that have declined in value during the reporting time period. This category includes derivatives, hedging, available-for-sale
securities, and any other fair value reporting. These losses are reported for book purposes. However, for tax, they are not realized and recognized on the tax return until the ultimate sale, exchange, etc. of these items.

Equity method refers to the fact that, for book purposes then, companies must include some of their subsidiaries’ income as part of their income reliant on the percentage of ownership. This situation can differ between book and tax, which creates this deferred tax item.

Insurance stands for self-insurance reserves, which are established to fulfill any future claims that would emerge. Companies cannot always get policies to insure every activity in which they engage. Sometimes, if these policies could be provided, the cost would be prohibitive. In these situations then, they establish reserves as the substitute for insurance.

The terms net operating losses, etc. refer to all tax-related adjustments that differ between the book and tax systems. Some companies report these tax adjustments in the aggregate whereas others separate the net operating loss component from the other tax-related items. Net operating losses occur where companies report negative net income for the year. This reporting is acceptable for book purposes but not acceptable for tax purposes. The tax system provides no benefits for reporting anything less than breaking even for the year. However, it does permit carrying back the net operating losses to the previous two tax returns or forward to the future twenty years of tax returns until they provide some benefit from their deductibility. The difference between the book and tax system, as always, provides the basis for this deferred tax item being reported.

The tax credit carry forwards represent dollar-for-dollar reductions of actual tax liability not provided within the book system. This general category does not include companies’ research and development credits to the extent they are separately disclosed.

The research and development credit signifies the fact that the tax system provides dollar-for-dollar reductions of actual tax liability for portions of money invested in these research and development pursuits. The reasoning is for stimulating the economy as new inventions provide higher profit margins and therein tax collections for the government. The book reporting system provides no extra incentive for such investments and instead treats them as expenses or capitalized items.

Capital loss carry forwards represent losses incurred on long-lived assets’ sale, exchange, etc. For tax purposes then, corporations can deduct only capital losses to the extent of capital gains in any year. The remainder can be carried back three years or forward five years. The book system reports the full loss in the year incurred.

Foreign tax credits represent overseas income that is not subject to tax twice. The US tax system would put tax on that income but also provides dollar-for-dollar reductions of that tax liability for certain levels of overseas income. The book system just considers this income as any other income without imposing an extra tax expense or any resulting credit for that extra tax.

The category of tax benefits incorporates all state and local tax differences from book reporting principles. This category includes dollar-for-dollar reductions of tax liabilities as well.

Bad debt allowances emerge as differences because the tax system does not permit bad debts to be deducted until the
actual account is involved. The book system enables estimates to be made of bad debt expenses. Then, at the time of an individual account being considered to be uncollectible, no expense is then reported as it has already moved through the income statement. The timing is exactly the opposite for tax.

Leasing activities involve operating leases, etc. where expenses are deducted at different times for book and for tax. For financial purposes here, determining whether the lease is in the operating or capital category becomes paramount.

Capitalized research and development expenditures involve items that are spent in pursuing innovations in current products or new products altogether. These expenditures are capitalized for book purposes but more properly expensed for the tax system.

Long-term related debt involves differences between book and tax that emerge from the amortization of discounts or premiums on bonds for book purposes. However, for tax purposes, an entirely different valuation system could be in play.

Securitization activities relate to collateralizing financing activities. Differences do emerge between book and tax.

Legal reserves involve companies setting to the side some assets for no purpose but taking care of legal liabilities that emerge. Generally, these reserves are made as expectations that cases are to be resolved contrary to the companies’ stances develop. For book purposes then, some of these reserves can be reported as expenses under contingent liabilities principles. However, for tax purposes, these reserves are not expenses that are deductible until the actual settlement payments are made to the opposing parties.

Rewards involve providing customers with incentives for commitment to acquiring the companies’ goods or utilizing the companies’ services. These rewards could be reported for book purposes on establishing the category, but they would not be deductible for tax until transfer to the ultimate consumer.

Intangible items include goodwill as the excess of purchase price paid in acquisitions over the fair market value of assets, copyrights, patents, and trademarks. Differences emerge because tax could permit deductibility over time whereas book could require capitalization without any subsequent transfer over to an expense category.

The category of accrued expenses represents all deferred expenses that are incurred but not paid at the end of the reporting time period. For book, they can be reported as expenses. For tax, they cannot in some situations be deductible until actually paid. This difference creates the deferred situation.

The other category takes on all remaining differences not reportable separately because they are too small to be required to do so. These differences still are important for consideration.

Prepaid expense is the opposite side of accrued expenses just as deferred revenue is the counter to unearned income. Unrealized gains emerge in the identical context as unrealized losses. The category of servicing assets is the counter to securitization.

Results

The DTAs of unearned income, NOLs, etc., bad debts, long-term related debt adjustments, legal reserves, accrued expenses, and other and the DTLs of prepaid expenses, deferred revenues, unrealized
### Table 1

**Correlations and Regression: Prices v. Deferred Tax Items**

<table>
<thead>
<tr>
<th></th>
<th>Changes</th>
<th>2009</th>
<th>2008</th>
<th>Regression</th>
<th>t-statistic</th>
</tr>
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<td><strong>DTAs</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depr.</td>
<td>-.001</td>
<td>-.039</td>
<td>-.011</td>
<td>.072</td>
<td>(1.568)</td>
</tr>
<tr>
<td>EB</td>
<td>-.006</td>
<td>-.011</td>
<td>.039</td>
<td>.008</td>
<td>(-.170)</td>
</tr>
<tr>
<td>Inv.</td>
<td>.003</td>
<td>.077</td>
<td>.059</td>
<td>-.037</td>
<td>(-.851)</td>
</tr>
<tr>
<td>ESOP</td>
<td>-.020</td>
<td>.090</td>
<td>.156</td>
<td>-.023</td>
<td>(-.601)</td>
</tr>
<tr>
<td>Unearn.</td>
<td>-.001</td>
<td>.037</td>
<td>.041</td>
<td>-.234**</td>
<td>(-2.800)</td>
</tr>
<tr>
<td>Unreal.</td>
<td>-.005</td>
<td>.114</td>
<td>.094</td>
<td>-.026</td>
<td>(-.473)</td>
</tr>
<tr>
<td>Eq. Meth.</td>
<td>.002</td>
<td>-.214</td>
<td>-.305</td>
<td>-.069</td>
<td>(-1.219)</td>
</tr>
<tr>
<td>Ins.</td>
<td>.004</td>
<td>.030</td>
<td>-.010</td>
<td>.033</td>
<td>(-.925)</td>
</tr>
<tr>
<td>NOL, etc.</td>
<td>-.005</td>
<td>-.128</td>
<td>-.182*</td>
<td>-.142*</td>
<td>(-1.937)</td>
</tr>
<tr>
<td>NOL</td>
<td>-.006</td>
<td>-.040</td>
<td>-.102</td>
<td>.026</td>
<td>(.607)</td>
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<tr>
<td>Credit</td>
<td>-.009</td>
<td>-.157</td>
<td>-.110</td>
<td>-.098</td>
<td>(-1.188)</td>
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<td>R&amp;D Cred.</td>
<td>-.006</td>
<td>-.347</td>
<td>-.949*</td>
<td>.010</td>
<td>(.297)</td>
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<tr>
<td>Cap. Loss</td>
<td>-.003</td>
<td>-.005</td>
<td>.000</td>
<td>.110</td>
<td>(1.439)</td>
</tr>
<tr>
<td>FTC</td>
<td>-.010</td>
<td>.191</td>
<td>.327*</td>
<td>.020</td>
<td>(.544)</td>
</tr>
<tr>
<td>Tax Bene.</td>
<td>.000</td>
<td>-.012</td>
<td>-.058</td>
<td>-.080</td>
<td>(-1.127)</td>
</tr>
<tr>
<td>Bad Debts</td>
<td>-.012</td>
<td>-.126</td>
<td>-.088</td>
<td>-.293**</td>
<td>(-4.449)</td>
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<tr>
<td>Leases</td>
<td>.010</td>
<td>-.080</td>
<td>-.032</td>
<td>.002</td>
<td>(.056)</td>
</tr>
<tr>
<td>Cap. R&amp;D</td>
<td>-.011</td>
<td>.045</td>
<td>.251</td>
<td>.062</td>
<td>(1.107)</td>
</tr>
<tr>
<td>Acq. Loans</td>
<td>.002</td>
<td>-.215</td>
<td>-.031</td>
<td>.457**</td>
<td>(7.042)</td>
</tr>
<tr>
<td>Securi.</td>
<td>.007</td>
<td>-.315</td>
<td>-.095</td>
<td>.026</td>
<td>(-.350)</td>
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<td>Reserves</td>
<td>-.146**</td>
<td>.035</td>
<td>.059</td>
<td>-.186**</td>
<td>(-3.953)</td>
</tr>
<tr>
<td>Rewards</td>
<td>-.005</td>
<td>-.232</td>
<td>-.230</td>
<td>-.041</td>
<td>(-1.056)</td>
</tr>
<tr>
<td>Intan.</td>
<td>-.007</td>
<td>-.176</td>
<td>.120</td>
<td>.085</td>
<td>(1.659)</td>
</tr>
<tr>
<td>Acc. Exp.</td>
<td>-.005</td>
<td>.085</td>
<td>.157*</td>
<td>-.196*</td>
<td>(2.294)</td>
</tr>
<tr>
<td>Other</td>
<td>.052</td>
<td>.282**</td>
<td>.279**</td>
<td>-.005</td>
<td>(-.087)</td>
</tr>
<tr>
<td><strong>DTLs</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depr.</td>
<td>.006</td>
<td>.128*</td>
<td>-.001</td>
<td>.009</td>
<td>(.257)</td>
</tr>
<tr>
<td>EB</td>
<td>.007</td>
<td>-.048</td>
<td>-.083</td>
<td>.011</td>
<td>(.261)</td>
</tr>
<tr>
<td>Inv.</td>
<td>-.001</td>
<td>.125</td>
<td>.302*</td>
<td>.030</td>
<td>(6.641)</td>
</tr>
<tr>
<td>Pre. Exp.</td>
<td>-.182**</td>
<td>.071</td>
<td>.063</td>
<td>-.117*</td>
<td>(-2.218)</td>
</tr>
<tr>
<td>Def. Rev.</td>
<td>.276**</td>
<td>.200</td>
<td>-.232</td>
<td>.122**</td>
<td>(2.614)</td>
</tr>
<tr>
<td>Unreal.</td>
<td>.540**</td>
<td>.650**</td>
<td>.495**</td>
<td>.751**</td>
<td>(17.365)</td>
</tr>
<tr>
<td>Eq. Meth.</td>
<td>-.008</td>
<td>-.006</td>
<td>.018</td>
<td>.043</td>
<td>(8.483)</td>
</tr>
<tr>
<td>Intan.</td>
<td>-.006</td>
<td>-.010</td>
<td>.044</td>
<td>-.002</td>
<td>(-.037)</td>
</tr>
<tr>
<td>Discount</td>
<td>-.005</td>
<td>-.091</td>
<td>-.056</td>
<td>.030</td>
<td>(.421)</td>
</tr>
<tr>
<td>Leasing</td>
<td>.011</td>
<td>.106</td>
<td>-.042</td>
<td>-.001</td>
<td>(-.014)</td>
</tr>
<tr>
<td>Serv. Assets</td>
<td>.000</td>
<td>-.124</td>
<td>.035</td>
<td>.101</td>
<td>(1.823)</td>
</tr>
<tr>
<td>Other</td>
<td>.021</td>
<td>.364**</td>
<td>.347**</td>
<td>.075*</td>
<td>(2.002)</td>
</tr>
</tbody>
</table>

* Statistically significant at the .05 level; ** Statistically significant at the .01 level;

Column 1 Correlations: Change in Price v. Change in Deferred Items (2008 v. the 2009); Column 2 and Column 3 Correlations: Prices v. Deferred Tax Items as of 12/31/09 and 12/31/08; Column 4 Regression Coefficient: Change in Price v. Change in Deferred Items (2008 v. the 2009) and then Regression t-statistic.
gains, and other are certainly statistically significant to stock prices.

What is extraordinary in the results is that the item most explanatory of price changes is the category of unrealized gains, which is comprised of other comprehensive income items, such as derivatives results, currency translations, investment changes from mark-to-market, etc. Other researchers have shown little value from other comprehensive income as related to stock price, so this finding could lead to greater investigation of this area.

Somewhat expected is that items reported nowhere else in the financial statements are statistically significant, such as unearned income and deferred revenue. As expected, increases in unearned income diminish stock price, and increases in deferred revenue increase stock price.

Somewhat surprising is that items reported elsewhere in the financial statements provide statistically significant influences on stock price, the other discussed elements.

**Implications**

These extraordinary findings based on many hours of work show that investors must follow taxes to almost the extent (if not more than) they follow other components of the financial statements. There are many company attributes only shown through these components of DTAs and DTLs. Most investors would consider DTAs to be the most influential to increases in prices. This tendency emerges from the belief that all asset increases lead to price increases, and all liability increases result in price decreases. This research counters this belief in the strongest of terms.

The Securities and Exchange Commission (SEC) is actually on pace to make the results of this research even more beneficial to investors. The SEC is discussing requiring the provision of more machine-readable data, including footnote disclosures from annual reports. This requirement would empower Compustat and other providers to include these footnotes without much extra cost and be timelier in doing so. Then, investors could capitalize on this extraordinary review of the influential components of DTAs and DTLs.

Future research opportunities exist out there. International Financial Reporting Standards (IFRS) could replace current accounting standards in the future. Right now, US companies have been advised that the US is on the path to implementing IFRS within the next four years. However, the economic difficulties that have targeted not just the US market but also the entire world have delayed implementation. The concern is that the extra costs from first-time implementation could diminish stock prices even more than they have been currently. Also, some feel the extra fair value reporting from IFRS could have made the economic difficulties worse if this extra reporting did not in fact create the economic difficulties in some fashion.

Any researcher can do this research without the benefit of costly research tools. However, early trends have indicated that IFRS deferred tax items under International Accounting Standard 12 are less influential of stock prices. The fact lowering their influence is that not every tax item has to be reconciled.

Many have discussed having one common system for financial accounting and income tax. This situation would significantly reduce transaction costs. However, this cost reduction would be at the price
of less value relevant financial statements. After consideration of these research findings, investors’ reactions should be that having two separate systems is good, especially if reconciliation on the financial statements is required. This process produces more predictive power for pricing stocks.

An interesting research topic would be whether countries that disclose tax information already would have any incremental value to deferred tax items. Even with the public disclosure of this tax information, incremental predictive value could still be generated.

All these discussions though are meaningless if income taxes no longer exist. The move toward value added tax in so many countries could eventually lead to that system replacing any requirement for income taxes.

Other interesting research would be determining whether samples of sophisticated investors can currently ascertain anything from deferred tax item disclosures or whether they have to be educated in the process.

Determining whether the Internal Revenue Service (IRS) reviews deferred tax disclosures in deciding whether to more heavily audit any company would also be interesting.

References


The paper submitted: August 20, 2010
Prepared for publication: December 01, 2010
Jau daug metų visose šalyse ekspertai-patarėjai, brokeriai, investuotojai ir kreditoriai peržiūrėti finansinės atskaitomybės atskaitas tam, kad galečų numatyti įmonių ateitį. Tačiau tik pastaraisiais metais jie pradėjo kreipti dėmesį į finansinėse ataskaitose esančias smulkmenas.


Šie atrasti faktai rodo, kad investuotojai turi stebėti mokesčius tiek pat (jei ne daugiau), kiek stebi ir kitus finansinius ataskaitos komponentus. Daug įmonių požymių atsispindi tik per šiuos AMT ir AMĮ komponentus. Daugelis investuotojų mano, kad AMT labiausiai įtakoja kainų augimą. Ši tendencija pasireiškia dėl to, kad viso turto vertė padidėjus padidina ir kainas, o atsakomybės didėjimas lemia kainų mažėjimą. Straipsnio tyrimas atskleidžia, kad negautų pajamų, blogų paskolų, ilgalaikų skolų patikslinimus, privalomų rezervų, sukauptų išlaidų AMT ir iš anksto apmokėtų išlaidų, atidėtųjų pajamų, nerealizuoto pelno AMĮ statistiškai reikšmingai įtakoja JAV akcijų kainas.