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Accounting of the Operations Regarding the Calculation and Recording of Tax on Profit

Camelia Madalina Beldiman¹

Abstract: The present paper highlights the importance of the corporate income tax when setting up public financial resources to the State Budget through taxes, contributions and any income of a fiscal nature. The tax is a form of collecting part of the incomes of legal entities, which enters the state's patrimony for the payment and coverage of public expenses. This collection is mandatory, with a non-refundable title and without direct benefit from the state. Taxation is a bridge between the state and legal entities and taxes are necessary, without their existence, the state cannot exercise its powers. At the same time, the tax on profit remains the main way of taxing the income from the economic activities and an important direct tax, with an essential role in the constitution of the public financial resources. The activity of the economic agents that fall according to the turnover to pay the tax on profit is carried out on the basis of a complex legislation that clearly establishes which are the revenues, which are the expenses and which is the part of the realized profit subject to taxation.

Keywords: closing the income and expenditure accounts; profit tax; profit distribution; public financial resources; the state budget

JEL Classification: M41

1. Introduction to Taxation

The complexity of contemporary economies generates many difficulties, in managing the activities carried out by legal or natural persons in order to obtain income. These activities implicitly involve fiscal aspects, which must be known and integrated in the decision-making process.

At the macroeconomic level, the tax on profit generates a fiscal burden borne directly by the companies, but also a series of indirect costs, of administration of this tax.

The profit tax is a direct tax, it is due by the companies, it is easily calculated, it is applied to the income of the companies, it is collected to the state budget and represents a real contribution to the state income. Taxes generally represents the cash contribution required and with the non-reimbursable title that is due within the term of the budget law by natural and legal persons for the income they obtain, for the goods they own, respectively for the goods they produce or the works and the services they provide or perform.

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1.1. The Scope of the Tax

According to the Fiscal Code¹ article 14, Title 2, the tax on profit is applied as follows:

- In the case of the Romanian legal persons, of foreign legal persons having the place of exercising the effective management in Romania, as well as of the legal persons with the registered office in Romania, established according to the European legislation, on the taxable profit obtained from any source, both from Romania and from abroad;
- In the case of foreign legal entities that carry out activity through the permanent headquarters / several permanent establishments in Romania, the taxable profit at the level of the permanent headquarters designated to fulfill the fiscal obligations.

Income tax is the main form of taxation of the corporate income, representing a direct tax with major impact on the activity of a company, which is at the same time subject and supporter of this tax. According to the legislation in force in Romania, the statutory tax rate is 16%, applied to the taxable profit.

Taxable profit = (Total income - Non-taxable income) - (Total expenses - Non-deductible expenses) - Tax losses² = Taxable income - deductible expenses - tax losses.

2. Analysis of Incomes and Expenses

An important role in determining the taxable profit is the non-taxable income, which represents that part of the total income that is not subject to the profit tax.

A few examples of non-taxable income: dividends from a Romanian or foreign legal entity; the revenues from the sale/ assignment of the participation titles held to a Romanian legal entity or to a foreign legal person; revenues from the liquidation of another Romanian legal entity or a foreign legal entity,

In order to determine the taxable profit, it must be determined whether an expense is deductible or non-deductible. From a fiscal point of view, there are 3 categories of expenses: deductible expenses; expenses with limited deductibility; non-deductible expenses.

2.1. Deductible Expenses

For the determination of the taxable profit, only the expenses incurred for the purpose of making taxable income are considered deductible expenses, as follows (only some examples):

- the expenses with the purchase of the packages, during the lifetime established by the taxpayer;
- expenses incurred for the protection of work and expenses for the prevention of accidents at work and occupational diseases;

¹ Government Emergency Ordinance no.3 / 2017 Regarding the modification and completion of Law no.227 of 2015 on the Fiscal Code

² Tax losses can be recovered for a period of seven consecutive years starting with 2009.



- advertising expenses incurred for the purpose of popularizing the company, products or services, based on a written contract, as well as the costs associated with producing the necessary materials for the dissemination of advertising messages;
- transportation and accommodation expenses in the country and abroad made by employees and administrators;
- registration fees, compulsory contributions and contributions for the fund intended to negotiate the collective labor agreement;
- expenditure on environmental protection and conservation of resources.

2.2. Limited Deductible Expenses

The deductibility of certain expenses is limited as follows:

1. Protocol expenses (within a limit of 2% applied on the difference between the total revenue and the expenses recorded according to the accounting regulations, make fiscal adjustments). Thus, from the total the expenses with the tax on the current and deferred profit are deducted, the protocol expenses, the expenses related to the non-taxable income; and from the total of the income subtract the non-taxable income;
2. Social expenses (within a limit of up to 2% applied on the value of expenses with personnel salaries).

Some examples of such social expenses:

- Birth and funeral aids;
 - Expenses for the proper functioning of some activities or units in the administration of the taxpayers: kindergartens, nurseries, libraries, canteens, sports bases, as well as for the schools under their patronage;
 - Expenses representing gifts in cash or in kind, including gift vouchers offered minor children and employees, as well as childcare vouchers.
3. Expenses representing meal vouchers, granted by employers monthly, in the last decade of a month for the following month, corresponding to the number of working days in the month from which the distribution is made;
 4. Expenses with provisions and reserves (for example, provisions for good performance guarantees granted to customers);
 5. Operating, maintenance and repair expenses related to cars used by the persons with management and administration functions of the legal person; interest and exchange rate expenses;
 6. Amortization, within a limit of 1,500 lei / month (for means of transport for persons having at most nine passenger seats, including the driver's seat).



2.3. Non- Deductible Expenses

Several expenses are considered non-deductible:

1. Own expenses of the taxpayer with the tax on profit due (running of the account 691 Income tax" cumulated the quarter prior to the calculation);
2. Interest / delay penalties, fines, confiscation and penalties due to Romanian authorities;
3. Expenditure on assets such as stocks or tangible assets discovered as missing or degraded;
4. Expenses recorded in accounting that are not based on a supporting document according to the law;
5. Expenses with insurance premiums paid by the employer on behalf of the employee, which are not included in the employee's salary income;
6. Other wage expenses and / or assimilated to them, which are not taxed on the employee;
7. Expenditure on consulting and management services, consultancy, assistance or other services.

3. Calculation of the Tax on the Profit and the Recording in the Accounting

Let's try to go through all the steps necessary to prove how the calculation of the income tax should be performed by an accountant. For this task, we will use the numbers provided by the Agricultural Society "Covurlui Hill" from Baleni, Galati County.

Table 1. Income Realized in 2019 by the Agricultural Company "Covurlui Hill" from Baleni

| Accounts | Name | Amount |
|----------------------|---|------------------------|
| 701 | Sales of finished goods | 7. 147. 772,70 |
| 703 | Sales of residual products | 41. 344,40 |
| 704 | Services rendered | 226. 275,43 |
| 706 | Rental and royalty income | 84. 892,23 |
| 707 | Sale of goods purchased for resale | 175. 070,75 |
| 708 | Revenues from sundry activities | 6. 845,11 |
| 711 | Revenues associated with the costs of the completed production | 13. 709. 171,05 |
| 7411 | Subsidies related to the turnover | 2. 630. 547,06 |
| 7581 | Compensations, fines and penalties | 500,00 |
| 7583 | Proceeds from disposal of assets and other capital transactions | 5. 645,16 |
| 7584 | Amortization of investment subsidies | 23. 100,00 |
| 7588 | Other operating revenues | 165,72 |
| 766 | Interest income | 594,89 |
| TOTAL REVENUE | | 24. 051. 924,50 |

In the revenues' structure related to the year 2019 there is the account 711 "Revenues associated with the costs of the completed production" which is a bifunctional account. With this account, the cost of production of the stored production is kept as well as its variation.

When analyzing account 711, "Revenues associated with the costs of the completed production", there are a few aspects that are worth mentioning:

- is charged with the cost of production or the standard price of the indefinite products or production coming out of administration and with the related price differences;
- is credited with the cost of production or the standard price of both the products and indefinite products and with the related price difference;



- the debtor turnover represents the production cost of the output produced during the time frame;
- credit turnover, represents the production cost of the production obtained during the time frame;
- the final debit balance represents a decrease in the stock of products compared to the beginning of the time frame;
- the final credit balance represents the increase of the stock of products compared to the beginning of the time frame.

For the calculation of the profit tax from the total revenues registered in 2019 by the Agricultural Company “Covurlui Hill”, the value of the total amounts of the 711 account is deducted together with the debtor balance amounting to 48,274 lei (row 08, Form 20, P&L account).

Table 2. Expenses Incurred in 2019 by the Agricultural Company “Covurlui Hill”, from Baleni

| Accounts | Name | Amount |
|-----------------------|---|------------------------|
| 601 | Raw materials | 11. 537,00 |
| 6021 | Auxiliary materials | 10. 371,05 |
| 6022 | Fuel | 1. 212. 882,48 |
| 6024 | Spare parts | 611. 438,85 |
| 6025 | Seeds and sapling | 655. 774. 02 |
| 6028 | Other consumables | 2. 197. 990,75 |
| 603 | Materials in the form of small inventory | 1. 278,40 |
| 604 | Materials not stored | 13. 834,39 |
| 605 | Electricity, heating and water | 23. 304,82 |
| 607 | Goods for resale | 175. 156,97 |
| 608 | Packaging costs | 3. 630,00 |
| 609 | Trade discounts received | (-262. 023,37) |
| 611 | Maintenance and repair expenses | 24. 078,71 |
| 612 | Royalties and rental expenses | 29. 014,54 |
| 613 | Insurance premiums | 87. 693,67 |
| 614 | Research expenses | 1. 035,81 |
| 621 | Externally contracted manpower | 88. 997,87 |
| 623 | Entertaining, promotion and advertising | 3. 381,25 |
| 624 | Transport of goods and personnel | 5. 983,36 |
| 626 | Postage and telecommunications | 4. 638,74 |
| 628 | Other third-party services | 307. 117,05 |
| 635 | Other taxes, duties and similar expenses | 388. 871,63 |
| 641 | Salaries | 1. 240. 421,00 |
| 6451 | Company's contribution to social security | 236. 622,00 |
| 6452 | Company's contribution to unemployment fund | 5. 532,00 |
| 6453 | Company's contribution to health insurance | 62. 813,00 |
| 6458 | Other social security and welfare contributions | 3. 419,00 |
| 6581 | Compensations, fines and penalties | 112. 893,42 |
| 6582 | Gifts and subsidies granted | 10. 437,20 |
| 6588 | Other operating expenses | 1. 630. 307,26 |
| 666 | Interest expense | 24. 157,40 |
| 6811 | Depreciation of non-current assets | 497. 580,89 |
| 691 | Income tax | 149. 665,00 |
| TOTAL EXPENSES | | 10. 090. 882,90 |



In the structure of the expenses incurred by the Agricultural Company “Covurlui Hill”, we will find the account 609 “Trade discounts received” which is keeping the record of the commercial discounts, received after the invoice, regardless of the period to which it refers.

The accounts in class 6 “Expense accounts” are accounts with an asset function, except for the account 609 “Trade discounts received”, which has a liability function and operates as income. It is closed by the credit of the account 121 “Profit and loss” although it is a liability account. This is because the reductions granted are negative amounts and represent a decrease in the purchase cost. Account 609 is deducted from the total of deductible expenses, and it practically diminishes the expenses.

Account 6581 “Compensation, fines and penalties” is a non-deductible account when calculating corporate income tax.

Account 6582 “Gifts and subsidies granted” is also a non-deductible account when calculating corporate income tax. When the donations are granted under the conditions of the law, their value is deducted from the tax on the calculated and due profit.

3.1. Calculation of the Profit tax for 2019

Going deeper into further details, let's perform step by step the operations to compute the profit tax for the Agricultural Company “Covurlui Hill”.

Tax on profit = 16% x Taxable profit (Total income - Total expenses - Non-taxable income + Non-deductible expenses)

Total revenue = Total class 7 accounts = **24,051,924. 50**

Total expenses = Total accounts class 6 - Account 609 “Trade discounts received” = 10,090,882. 90 - 262,023. 37 = **9,828,859. 53**

Non-taxable income = Account turnover 711 “Revenues associated with the costs of the completed production” + Account debtor balance 711 “Revenues associated with the costs of the completed production” (row 08 Form 20 profit and loss account) = 13,709,171. 05 + 48,274. 00 = **13,757,445. 05**

Non-deductible expenses = Account 6581 “Compensation, fines and penalties” + Account 6582 “Gifts and subsidies granted” + Account 691 “Income tax” + Account 609 “Trade discounts received” = 112,893. 42 + 10,437. 20 + 149,665. 00 + 262,023. 37 = **535,018. 99**

Accounting profit = Total income - Total expenses = 24,051,924. 50 - 9,828,859. 53 = **14,223,064. 47**

Taxable profit = Accounting profit - Non-taxable income + Non-deductible expenses = 14,223,064. 47 - 13,757,445. 05 + 535,018. 99 = **1,000,638. 91**

Cumulative profit tax = 1,000,638. 91 x 16% = **160,102. 23**

Sponsorship granted according to the law: 10,437. 20

Income tax due prior: 331,244. 00

Profit tax due Quarter 4: Cumulative profit tax - Sponsorship granted according to the law - Income tax due prior = 160,102. 23 - 10,437. 20 - 331,244. 00



= - 181,578. 97

Highlighting profit tax accounting

(+ A) 691 = 4411 (+ P) 160,102. 23

3.2. Profit tax for Quarter IV 2019

We will analyze the records between January 1st and December 31st, 2019, from the Fiscal Evidence Register.

Table 3. Cumulated Values for 2019

| No. | Explanations of operations and corporate income tax | Amount (lei) |
|-------------|--|---------------------|
| 1 | TOTAL REVENUE | 10,294,479. 45 |
| from which: | | |
| 1. 1 | Account 711 balance "Revenues associated with the costs of the completed production" | -48,274. 00 |
| 1. 2 | Account 712 balance "Revenues associated with the cost of services in "progress" | 0 |
| 1. 3 | Account 709 "Trade discounts offered" | 0 |
| 2 | TOTAL EXPENDITURE - excluding account 691 "Income tax" | 9,417,171. 16 |
| from which: | | |
| 2. 1 | Account 609 "Trade discounts received" | 262,023. 37 |
| 3 | GROSS PROFIT (1-2) | 877,308. 29 |
| 4 | NON-TAXABLE REVENUE | 0 |
| from which: | | |
| 4. 1 | Account 7581 "Compensations, fines and penalties" | 0 |
| 4. 2 | Income from dividends received from legal entities | 0 |
| 4. 3 | Other non-taxable income | 0 |
| 5 | NON-DEDUCTIBLE EXPENSES | 123,330. 62 |
| from which: | | |
| 5. 1 | Account 6581 "Compensations, fines and penalties" | 112,893. 42 |
| 5. 2 | Account 6231 "Entertaining, promotion and advertising" | 0 |
| 5. 3 | Account 6582 "Gifts and subsidies granted" | 10,437. 20 |
| 5. 4 | Social expenses over norm | 0 |
| 5. 5 | Expenses with traveling over norm | 0 |
| 5. 6 | 50% non-deductible fuel | 0 |
| 5. 7 | Non-deductible depreciation | 0 |
| 5. 8 | Other non-deductible expenses | 0 |
| 6 | DEDUCTIBLE LEGAL RESERVE | 0 |
| 7 | OTHER AMOUNTS DEDUCTIBLE | 0 |
| 7. 1 | Items similar to income | 0 |
| 7. 2 | Items similar to expenses | 0 |
| 8 | AGGREGATE GROSS PROFIT (3 - 4 + 5 - 6 - 7. 1 + 7. 2 - 7. 3) | 1,000,638. 91 |
| 9 | FISCAL LOSS TO RECOVER FROM PREVIOUS YEARS | 0 |
| 10 | INCOME TAXABLE PROFIT (8 - 9) | 1,000,638. 91 |
| 11 | INCOME TAX (10 x 16%) | 160,102. 08 |
| 12 | PROFIT VALUE REINVESTED | 0 |
| 13 | PROFIT TAX EXEMPT (reinvested earnings) | 0 |
| 14 | SPONSORSHIPS BY LAW | 10,437. 20 |
| 15 | TAX ON PREVIOUS DEBT PROFIT (Account 691 "Income tax") | 331,244. 00 |
| 16 | TAX ON PROFIT DEBT QUARTER IV 2019 (11-13-14-15) | -181,579. 00 |

3.3. Other Financial Indicators

Coming back from the accountants' daily work, let's try to analyze what else can influence the profit and the according tax.

Table 4. The Values of the Main Financial Indicators for the 2017 – 2019 Timeframe

| No | Chart of specifications | accounts' Unit | Timeframe | | |
|----|-----------------------------|----------------|------------|------------|-----------|
| | | | 2017 | 2018 | 2019 |
| 1 | Turnover | Lei | 9,760,294 | 10,312,748 | 7,348,215 |
| 2 | The result of the operation | Lei | 181,010 | 900,870 | 1,388,198 |
| 3 | Total income | Lei | 10,158,655 | 10,294,480 | 9,515,776 |
| 4 | Total expenses | Lei | 10,002,938 | 9,417,172 | 8,218,763 |
| 5 | Gross profit | Lei | 155,717 | 877,308 | 1,297,013 |
| 6 | Tax | Lei | 33,258 | 149,665 | 0 |
| 7 | Reinvested profit | Lei | 0 | 0 | 1,297,013 |

Someone may find easy to state that a bigger turnover will imply a bigger profit and an increased tax. But analyzing the above figures from our Agricultural Company "Covurlui Hill", this is true only for the 2018 vs 2017, because in 2019 – despite the fact that the turnover decreased, the profit increased and the tax was null, due to an accountant specific trick, who redirected the whole profit to investments (see row 7).

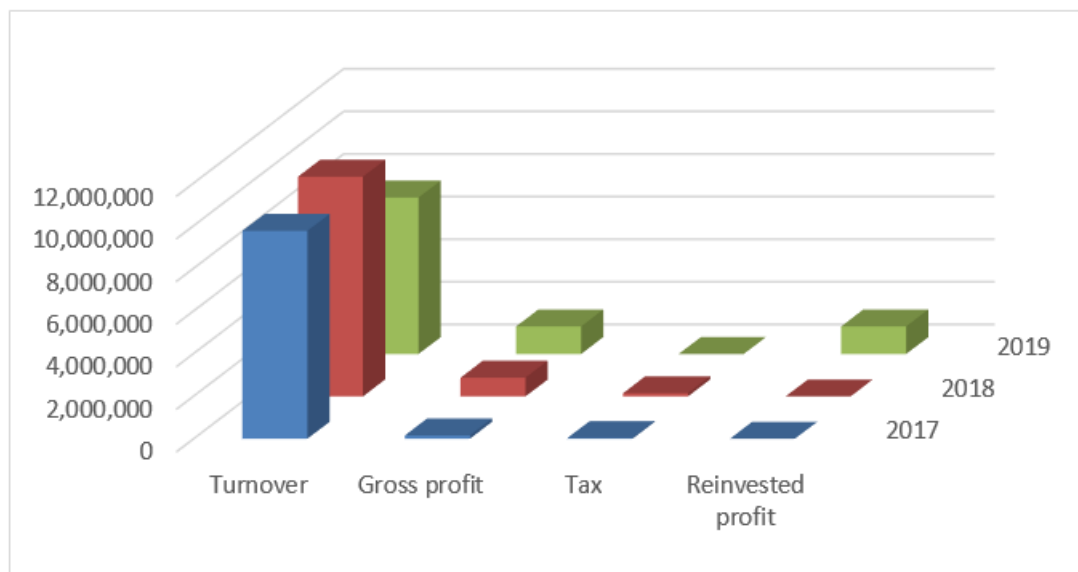


Figure 1. Evolution of Economic Indicators during 2017-2019



4. Conclusions

From the paper we may conclude that in order to carry out its functions, the state needs important financial resources, mobilized through the fiscal system. The tax is a form of collecting part of the incomes of legal and natural persons, who enter state ownership for the payment and cover of public expenses. Companies, by their nature works for profit, so we can state that profit is a simple income resulting from economic activities. The role of the tax on profit is an important one and diversified, due to the common functions that we encounter based on all state taxes.

The tax code specifies the categories of taxpayers who must pay these taxes, as well as how they are calculated. The fiscal obligation represents the responsibility to declare and pay the taxes and fees that are incumbent on the taxpayer legal person according to the legal norms in force. By deliberately not paying the tax due to the state or by breaking the regulations regarding the payment obligation on the taxpayers' side, the tax evasion is born.

Tax evasion is the phenomenon of violation of tax regulations that has as a financial consequence the payment of taxes and fees lower than the legal ones due, or even of non-payment of taxes and fees. The limitation of tax evasion appears to be necessary due to its effects, it recovers directly on the diminution of tax revenues and favors the appearance of distortions in the market mechanism, unjustifiably consolidating the market position of those who evade from taxation, contributing to the accentuation of social inequities.

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