Investigating the reasons of difference between taxable income and income assessed by tax authorities (a case study: the tax offices in Yazd province)

Hossein Azarniyooosh
M.A, Student, Department of Accounting, Tabas branch, Islamic Azad university, Tabas, Iran

Mohsen Jalali Majidi
Member of Faculty Department of Management, Mashhad branch, Islamic Azad University, Mashhad, Iran

Abstract

The concept of income tax focuses on the fitness of the demanded tax on the earned income. In a developed society, it is expected that the payers do not flee from paying the tax due to promotion of tax culture, thus the culture of self-tax return will be institutionalized. However, the concern for tax is serious in Iran and there is an ever-to-be conflict between financial sectors and payers. The tax dispute resolution committees and tax supreme council are usually active and the tax claims are usually brought in the Supreme Court. Considering these problems, the paper aims at investigating the reasons and factors making the difference between the declared taxable income of Production Companies and the taxable income assessed by the tax authorities. The results revealed a significant difference between the declared taxable income of Production Companies and the taxable income assessed by the tax authorities; additionally, the causes of this difference, each by them, have a significant reliability.

Keywords: taxable income assessed by the tax authorities, financial sectors.
Introduction

Tax has been a double of the first human societies. By societies being developed and the public needs increased, tax collection in cash or in goods became common. Thousands of years have been passed from the human life, and tax collection has been as 'tribute'. Developing the human societies and turning a village into a town, and expansion of cities made the concept of tax rational. An overview of the change procedure of the role of tax in society shows the role has been effectual in all affairs of social life, and it has become more extended and efficient. The purpose to ordain and collect tax in the past was to satisfy the finance of the governments, but gradually, the financial measures of government realized, the tax was construed as a tool for growth, stability and reduce of inequalities. The government uses the tax as major variables to have desired effect on both the macro variables such as economic growth, inflation, unemployment, etc. and assign the resources and distribute income. An increase in the role of tax in providing the government spending causes a decrease in the adverse effects of economy. Thus, the tax has been long a matter of interest for the economic and financial researchers, and the tax laws evolved in their path.

In advanced countries, tax is considered as a strong leverage to conduct financial and economic policies, social activities and government funding. In these countries, the tax revenue is at the apex of the public income of government. The share of tax revenues of the overall incomes of government is often more than the other incomes in different countries of the world. In our country, the income of the sale of oil is the main income of the government. However, Based on the fifth five-year development plan, Iran should: to fully drop the dependence on the fund toward the gas and oil revenue through increasing the share of public incomes, a measure should be taken so that: finalizing the plan, the ratio of tax to gross production, providing lack of increase in the direct tax rate and expansion of tax base, reaches to at least 10%. Therefore, taking a strategic tax-based policy is deeply felt. Reforming the tax structure and developing the civil tax system have been aims of the government in the years away. To name some attempts done are direct law legislation (adopted on March 1987); the amendment on January 17, 2002; and value added tax (VAT) enforcement on October 2008. Making a proper structure, whether for the law legislation or for institution is essential for the taxation process on the basis of science and justice. A desired tax system is the one having the most favorable economic effects. The VAT of corporate and legal entities is one of the most important income revenues resources. However, determining the taxable income is often difficult. The study attempts to investigate the difference between the declared taxable income of Production Companies as payer and the income assessed by tax authorities of department of Yazd province as the authority.

Significance of the study

In the economy of Iran, the oil revenues were considered as one of the most effectual factors on the economic agents. Even from the economic experts' perspective, Iran has a single-product economy, depending upon the oil revenues; and the dependence has made the country go through irreparable blows in the fluctuations of the oil industry. This is much important in the economy of Iran considering that OPEC interfere less in determining the price of oil, and it is exogenous in the economy. In one hand, as it is an exhaustible resource, the lack of oil will have adverse effects on the behavior of government, private sector and consumers. So it
is strongly felt that it is a necessity to replace the oil revenues in the economy with a resource or resources, in addition to providing sufficient constant income for the government, could bring about favorable conditions for the economic agents, and in case of crisis or commercial cycles, decrease the damage of crisis and cycles as automatic stabilizer. Tax will function as an inter-system automatic stabilizer if it is a function of national income because less tax will be collected in the economic downturn meaning increase in consumption and investment, which the expansionary fiscal policy will be automatically adopted and, in addition, will not require interruption policy. The action of discretionary expansionary fiscal policy is accompanied by the government with assessment interruption, decision, implementation and impact. In the economic prosperity, more tax is collected meaning decrease in consumption and investment, which contradictory fiscal policy will be automatically adopted. It could be argued that the discretionary fiscal policy should be used only in case of inflation and great depression. The economic experts are concerned about the weakness of tax culture and lack of adequacy of tax share in providing the economic growth of the country. The income tax of legal entities in our country is of utmost importance so that the statistics show a high percentage of tax income is collected from the legal entities. One of the legal entities are the trading companies having an active role in the economic and social movements, making jobs and providing raw materials in society so that any unjustified modification could have a destructive consequence. Variety of studies and investigation were conducted concerning costs and the way to deal with them and also established tax exemption in the tax law to play the role of tax as tax reforms. Determining the taxable income of companies is often difficult to calculate. Although the taxable income of every company is apparently gained by subtracting the costs performed from the sum of revenue, the type of costs and methods selected for calculation and the established exemptions in the tax law are various and it seems impossible to determine a unified procedure to assess the taxable income of companies. Thus, the study attempts to analyze the reasons of difference between the declared taxable income of trading companies and the taxable income assessed by tax authorities.

**Purposes of research**

With progress in industrialization movement and expansion of economic firms' trade in the legal form, the companies were made and began to work. In most of the economic systems, governments made a specific tax named corporate tax. Corporate tax is mainly capital gain tax. In our country, income tax of the legal entities such as the corporations is collected by the virtue of article 105 of direct tax, and includes a considerable part of tax income. The study attempts to investigate the difference between the declared taxable income of Production Companies and the taxable income assessed by the tax authorities. The general purposes are: The difference between the declared taxable income of Production Companies as payer and the taxable income assessed by the tax authorities in tax departments of Yazd province. Payer in the position of assessor identifies the major reasons of difference with the required suggestions.

**Literature review**

Ronald Cummins et al (2005) in his article titled "The effects of tax morale than tax compliance" argue that the compulsory endeavor of tax agency could promote the tax compliance. Christina Murphy (2008) in her article title "Enforcing tax compliance: to punish
or persuade?" mentions that there are two strategies for compliance: the first is to a strategy based on punishing and the second is about the strategy based on the persuading. Laura Sour (2004) in her article titled "An economic model of tax compliance with individual morality and group" investigated both types of personal and social behavior of compliance. She continues that the high tax rates will lead to more tax evasion, and also when the payer realize there are so many people not complying for their tax, they will begin to commit tax evasion.

Henrik (2009) in his article titled "The problem of tax evasion and the importance of trust" analyzes the concept of tax evasion in ten different types of tax and deals with how to pay the tax. He mentions that the different taxes should be reviewed separately instead of disputing over the concept as a usual phenomenon. He adds those who do not trust their citizens most probably believe they evade paying tax, but the lack of trust of politicians have a more profound impact, especially for taxes re-distributed and or should be paid in financial terms. So, it is important for the politicians to trust each other to be able to collect the taxes for maintaining the welfare.

Martini (2003) in his article titled "Tax evasion and physiology of social control" argues that in the public view about the economics in tax payment evasion, the choice of the tax payers to avoid paying the tax depends on the impartiality in the tax system. The purpose of this article is to make a foundation of physiology to divert the attentions concerning the human behavior as a process of following the laws. Based on the main theory, the tax payers are more agreed upon the tax laws, of which they are more satisfied.

Chen (2003) in his article titled "Tax evasion in a model of endogenous growth" optimizes the rate of tax in this pattern, but the individuals optimize tax evasion. This pattern investigates rate of tax, tax evasion and economic growth and compares them with the similar-to-each-other economic systems (except for those that are away from the tax evasion). It also studies about the impact of three policies of government concerning rate of tax, tax evasion and economic growth and found that increase in costs and penalties for tax evasion made reduce in tax evasion. Increase in tax investigation will decrease the tax evasion only when the cost of tax implementation is not so high. Basically, these three policies will have adverse effects on the economic growth due to indirect impact on tax evasion and favorable tax rate. This pattern was set to quantitatively assess the impacts of the mentioned policies. It became apparent that these three policies are quantitatively effectual in the source of tax evasion, but they accompany with low growth effects unless the externality of the government is so high.

In another piece of study, Alireza Hashemi (2007) in his article titled "Efficient management of tax", which was done for the Tehran chamber of commerce, industries and mines, regards one of the important aspects of efficient management of tax system promotion of culture and tax compliance. About the tax compliance it was suggested that how we could achieve it and he mentions two views for that, the first is through comparing profit and risk and the second from the perspective of a responsible citizen. In the first one, an individual attempts to improve his status desirability through maximizing the income and wealth, so when he realizes he can improve his power by lack of tax compliance, he will seek for that. In the second, the view of community, individual social status, age, sex, race and culture are
effectual in compliance. The view of community toward the tax management and institution, sense of existence or lack of justice and a common ideology is important.

Methodology

Deductive-inductive method was implemented in this study. Statistically, the study is a correlational one. For this purpose, library method is used in collecting and editing the texts of research, and magazines, journals, websites, etc. are used by going to the library. And in the field method, the data available in the tax files are used for collecting the required ones concerning the research. Finally, using the computational statistical methods, the findings of researched were assessed. In this study, T-distribution was used for testing the assumption considering that the population distribution is undetermined (normal or non-normal) and it is assumed the standard deviation of population is unknown. So, regarding that the population is large (30), the distribution is normal approximation according to the central limit theorem).

In the next step, the assumptions were tested citing statistical data and with the help of SPSS. The results are presented in Table 1.

Table 1: the results of assumption test

<table>
<thead>
<tr>
<th>Error rate α</th>
<th>Statistic t</th>
<th>Degree of freedom</th>
<th>Variable</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.000</td>
<td>139</td>
<td>7.715</td>
<td>Se</td>
</tr>
<tr>
<td>0.001</td>
<td>139</td>
<td>4.14</td>
<td>btmn</td>
</tr>
<tr>
<td>0.005</td>
<td>139</td>
<td>6.39</td>
<td>aetm</td>
</tr>
<tr>
<td>0.003</td>
<td>139</td>
<td>5.5</td>
<td>frm</td>
</tr>
<tr>
<td>0.000</td>
<td>139</td>
<td>5.1</td>
<td>tgm</td>
</tr>
<tr>
<td>0.002</td>
<td>139</td>
<td>3.23</td>
<td>rhnm</td>
</tr>
<tr>
<td>0.006</td>
<td>139</td>
<td>8.311</td>
<td>mehm</td>
</tr>
</tbody>
</table>

Having the results, all the assumptions are approved. On other words, the mentioned variables could be a factor a difference between declared taxable income and the taxable income assessed by the tax authorities.

To realize the significance of variables in making the mentioned difference, the ranking of factors is carried out. The ranking provides the accountant and tax payers with the opportunity to classify the factors of making difference based on the significance and validity so that the tax payers begin to carry out what it takes by prioritizing to remove the defects.

If the numerical value of each variable is divided by the difference between the declared taxable income and the taxable income assessed by the tax authorities, the portion of variable of the mentioned difference will result. This portion is somehow showing the significance of variable in making this difference.
Table 2: portion of each variable in difference between the declared taxable income and the taxable income assessed by the tax authorities

<table>
<thead>
<tr>
<th>Variable</th>
<th>btnm</th>
<th>aetm</th>
<th>frm</th>
<th>tsgm</th>
<th>rhnm</th>
<th>mehm</th>
</tr>
</thead>
<tbody>
<tr>
<td>portion of the variable</td>
<td>0.0678</td>
<td>0.2402</td>
<td>0.1672</td>
<td>0.0699</td>
<td>0.0474</td>
<td>0.4075</td>
</tr>
<tr>
<td>from the total</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The results in the table shows that in prioritizing, respectively, contradiction among accounting standards and impossibility of providing documents and supporting documentation, and finally not-following the established limit in the tax laws make difference between the declared taxable income and the taxable income assessed by the tax authorities.

Friedman Test

In this test, the variable having a higher mean is more significant and enjoys having more priority. Friedman is conducted with the variable causing difference between the declared taxable income and the taxable income assessed by the tax authorities. The results are presented in the Table 3.

Table 3: Friedman test results (variable ranking)

<table>
<thead>
<tr>
<th>Variable</th>
<th>btnm</th>
<th>aetm</th>
<th>frm</th>
<th>tsgm</th>
<th>rhnm</th>
<th>mehm</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean rank</td>
<td>2.5</td>
<td>4.73</td>
<td>3.31</td>
<td>2.71</td>
<td>2.1</td>
<td>5.74</td>
</tr>
</tbody>
</table>

The results in the table depicts that in prioritizing, respectively, contradiction among accounting standards and impossibility of providing documents and supporting documentation, and at last stage not-following the established limit in the tax laws will make difference between the declared taxable income and the taxable income assessed by the tax authorities.

Conclusion

Considering the difference between the declared taxable income and the taxable income assessed by the tax authorities, it is observed that the difference agent between accepted principles and standards of accounting and tax law forms 822 billion Rials, 40.75% of the total difference from the total 2019 billion Rials difference in the randomized sample of population.

The other results coming from the random sample investigations and differences are: Impossibility to provide valid and supporting documentations about the costs, and mismatch of the tax laws with the current economic conditions are the factor of difference. Tax evasion causes coming and making conflicts between declared income and taxable income assessed by the tax authorities.
The established exemptions in the law of direct tax will cause difference between declared income and taxable income assessed by the tax authorities. Irrelevance of declared costs has become a factor of difference between the declared income and taxable income assessed by the tax authorities.

Considering the above-mentioned results, it is observed that the difference is more in the perspective of production companies than the differences in tax system perspective. We should attend that the main factor of this conclusion is the difference between declared income and taxable income assessed by the tax authorities. As it is gained quantitatively and in numbers, it cannot be assessed obviously, it could be mentioned that in many cases of differences a shadow of this purpose of government income can be observed. The experience and knowledge of workers in the assessment and their authority over the assessment is one of factors that could be observed only through conducted modification on the tax files carried out by the tax dispute resolution committees. And because these obtained figures for investigating the step of assessing the tax are before its finality, this difference cannot be explained and assessed in determined numbers and figures.

To reduce the difference between declared taxable income of production companies and taxable income of assessed tax by the tax authorities, these steps are suggested:
- Increase in the number of authorities, increase in tax expert or technician for every tax authority, employing awards and appropriate advantages for the active assessment agents, activating the tax crimes, precise and complete implementation of VAT, and increase in quantity and quality of notices about the tax benefits.
References:


Henrik, h, Sveerker, g., Katarina, n., (2009), "perceived tax evasion and the importance of trust", the Journal of Socio-Economics, vol.5 nol pp 238-245.


Murphy, k., (2008)," Enforcing Tax Compliance: To Punish or Persuade?, ECONOMIC ANALYSIS & POLICY", VOL. 38 NO. 1, March 2008, Faculty of Arts and Education, Deakin University.