

## SOME CONSIDERATIONS ON TAX INVESTIGATIONS IN THE CONTEXT OF NEW REGULATIONS

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**Abstract:** *Romanian fiscal system is declarative, based on voluntary action of the taxpayer to calculate, declare and pay its obligations to the state. Checking the accuracy of calculations, statements and payments made by the taxpayer is done through specific procedures of tax control. Fiscal control represents all the activities carried out by the tax authorities to verify the fulfillment by the taxpayer or payer of the obligations under tax law and accounting.*

*Fiscal control according to the Fiscal Procedure Code is realized in the form of tax audit and unannounced check. The tax audit is carried out exclusively, directly and unhindered through the National Agency for Fiscal Administration or, where appropriate, by specialized departments of local authorities, as required by law, or by other authorities that are competent by law to administer taxes, fees, contributions or other amounts owed to the general consolidated budget. The tax audit is meant to verify the legality and compliance of tax returns, correctness and accuracy of obligations by taxpayers, checking taxation bases and the differences of debts.*

**Keywords:** *tax control, tax audit, tax procedure, tax inspection report, tax inspection documents.*

### 1. TAX AUDIT

The tax audit is carried out exclusively, directly and unhindered through the National Agency for Fiscal Administration or, where appropriate, by specialized departments of local authorities, as required by law, or by other authorities that are competent by law to administer taxes, fees, contributions or other amounts owed to the general consolidated budget. The tax audit involves carrying out the following stages: preparation of tax audit; the realization of tax audit; completion of the audit.

#### 1.1. Preparing a Tax Audit

In this case, there are the following stages: selecting taxpayers to be subject to tax audit, preparation of the tax audit and its communication, appointing the tax inspection team.

### **a. Selection of tax payers**

The selection of taxpayers to be checked is carried out by competent territorial fiscal body in whose jurisdiction they have the residence and the selection procedure cannot be contested by the taxpayer. Selecting taxpayers or taxpayers to be subject to tax audits by the competent tax auditors, depends on the level of risk. The risk level is determined by risk analysis. Taxpayers who have a reduced fiscal risk, tax file information were positive while the previous fiscal checks, underlining a lack of differences in taxes, with an insignificant debt, should not be a priority. According to the principle of uniformity of taxation, in cases of multiple tax payers with the same risks, the rate of tax audits should be similar throughout the country. The period subject to tax audit starts at the end of the previous controlled period.

### **b. The Tax Audit**

Before the tax audit, the tax auditor shall notify in writing the taxpayer by sending a notice of tax audit. The tax audit begins by communicating to the taxpayer the intention. In this regard, he will send the taxpayer a tax audit notice. Initiation of tax is performed in different time periods, from the communication of the tax audit, as follows: within 15 days for small taxpayers; within 30 days for important tax payers. The two deadlines for taxpayers do not start from the date the tax audit is initiated by the tax authorities, but from the date of acknowledgment by the taxpayer.

The start date is the date mentioned in the tax audit single register control whenever there is an obligation to keep it. If that does not take taxpayer or payer or tax auditors no single register control, this date is written in a report finding. If the tax audit can not start later than 5 working days from the date provided in the notice, the taxpayer is notified in writing of the new data of the tax audit. It is not necessary to communicate the tax audit in the following situations: when performing inspections or paying tax on a taxpayer located in insolvency proceedings; where, following an unannounced inspection, required immediate start of tax audit; for periods extending tax audit or tax receivables other than those contained in the original notice of tax audit; if recovery following a tax audit settlement decisions of the appeal; if the taxpayer requests / payer whose solution, following the risk analysis is necessary to perform the audit.

During a tax audit initiated at the request of the taxpayer, the inspection body may decide to extend the control. Thus, one can resort to a partial or general inspection, without the required approval by 30 and 15 days before, as appropriate. In this case, the notice of tax audit is communicated to the taxpayer over control, to address his request.

### **c. appointing the team**

Appointing the tax inspection team includes the following: choosing team members depending on the tax inspectors' workload and the complexity of the control, and their turnover; analyzing weaknesses by studying taxpayers' files training of tax inspectors by analyzing legislation related to the themes of control; the timing and duration of the control, recommending to avoid checks during the peak of activity as their duration should be minimized and should be limited strictly to verify the objectives set; the issue of service notice to appoint the tax inspection team.

## **1.2. Carrying out a Tax Audit**

To carry out a tax audit is to perform the following tasks: determine the place of tax audit; determine the duration of the tax audit, on-site intervention.

### **a. Establishing the place where the tax audit should be carried out**

Depending on the circumstances, the tax audit may or may not take place at the taxpayer's place or the place where taxable income is generated. Thus, the tax audit may be exercised: at taxpayer's venue. If the taxpayer does not have suitable premises, then a written notice will motivate it; at the headquarters of the tax authority. The tax audit will take place at the fiscal body's quarters, only if the time, theme or operations and controlled documents are not extended in time; the taxpayer will agree to the venue.

No matter where the tax audit is conducted, the tax auditor has the right to inspect the venue where it operates, or where the goods are taxable in the presence of the taxpayer or a person designated by him. The tax audit is usually conducted during working hours of the taxpayer. The tax audit can be carried out after the working hours of the taxpayer or the payer with written consent and the approval of the tax auditors.

### **b. Duration of tax audit**

Normally the duration of a tax audit is 3-5 days. The maximum duration of tax inspection is differentiated according to the size of taxpayer: 180 days for the large taxpayers and for taxpayers or payers that have secondary offices regardless of size; 90 days for medium taxpayers; 45 days for other taxpayers.

If the tax audit is not completed within a period representing twice the periods above, tax audit ceases without issuing a tax audit report and the tax decision or decision by not modifying the tax base. In this case, the tax auditor can resume inspection, with the approval of the superior body which has initially approved the original tax inspection, for the same period and the same tax obligations under the law. The beginning of this interval is the date of the first presentation of the inspection team at the taxpayer. The end of the interval

is the date when the taxpayer communicates the findings of the inspection team. The inspection is done within the term of prescription of the right to set tax receivables. The period subject to tax audit starts at the end of the previous control.

### **c. On-site Intervention**

On-site tax audit intervention implies three stages: the presentation of the inspection team at the taxpayer; proper conduct tax audit; the final discussion with the taxpayer. As allotted time, the three stages vary, but they are equally important for the tax audit in its entirety.

#### **c1. Tax inspection team at the taxpayer**

At the first on-site intervention the following occurs: presentation of members of the inspection team at the entity's management, when they present the order of service; determination of the identity and quality of designated interlocutor, respectively whether it is appropriate or not; visiting workspaces. In the presence of the taxpayer, the tax inspector will visit workspaces or the locations where the taxable goods are or income generating activities take place; tax audit programming, establishing schedule for future interventions; establishing the daily schedule according to which the inspection may take place, depending on the work program of the taxpayer; establishing are the persons responsible for providing the documents in question, who will provide assistance to the control team etc.

#### **c2. Proper conduct of tax audit**

It is the stage in which the vast majority of control procedures and objectives take place. The main objectives to control the taxes are:

**a. Regarding the income tax on wages**, control bodies check: how to grant the personal deductions; aggregation of all labor rights; proper preparation of payrolls; the correct leadership of the income tax accounting; verifying the legality and reality of granting salary, bonuses, allowances, leave, awards, payments in kind; checking the correct assessment of gross wages and correct assessment of the payroll tax; check remittance on time applying the payroll tax and interest and penalties for late payment; correct completion of tax records and sending them to the tax, the legal term; retention and archiving proper payroll etc.

**b. With regard to tax on profit**, control bodies shall check: if expenditures are properly accounted for and related to the line of business; if revenues are properly accounted for and related to the line of business; if the determination of taxable earnings, was done by deducting from the accounting result, the taxable income and adding the resulting sum, of the deductible working expenses; the reality of revenues and expenditures in

advance and proper allocation of the results; proper exploitation of the results of the annual inventory, of imputable shortages, of degradation, impairments of any kind and the VAT; correct recording of depreciation expenses, with overhaul, manufacturing, services etc.; if they were properly recorded as deductible expenses, interest, penalties, fines set out in previous controls; if they have not exceeded deductible entertainment expenses, per diem, social and cultural activities; if tax has been properly established and paid on time etc.

**c. With regard to tax, control bodies shall check:** if expenditures are properly accounted for and related to the lines of business; if revenues are properly accounted for and related to the lines of business; if the determination of taxable earnings was done by deducting from the accounting result, the taxable income and adding the resulting sum, the deductible working expenses; the reality of revenues and expenditures in advance and proper allocation of the results; proper exploitation of the results of the annual inventory, imputable shortages, of degradation, impairments of any kind and the VAT; correct recording of depreciation expenses, with overhaul, manufacturing, services etc.; if they were properly recorded as deductible expenses, interest, penalties, fines set out in previous controls; if they have not exceeded deductible entertainment expenses, per diem, social and cultural activities; if tax has been properly established and paid on time etc.

### **c.3. The final discussion with the taxpayer.**

The tax audit ends with a final discussion between the taxpayer and the tax authority representatives, in most cases, the tax inspection team members. The taxpayer or the payer must be informed during the tax audit about issues identified in the action on tax inspection and termination of the findings and their tax consequences.

Tax auditors communicate to the taxpayer or payer the audit draft report, electronically or on paper, giving them the opportunity to express their point of view. Thus, with the draft report, tax auditors communicate the date, time and place when the final discussion will take place.

The taxpayer or the payer may waive the final discussion, notifying tax auditors.

The end date of the tax audit is scheduled for final discussion with the taxpayer or the payer or a notification by the taxpayer or payer should be issued to renounce this right.

The taxpayer or the payer has the right to submit in writing their views on the findings of the tax auditors, no later than 5 business days from the date of conclusion of the audit. For large taxpayers the term is 7 working days. The term may be extended for justified reasons in agreement with the tax authorities.

### **1.3. Completion of tax audit**

Upon completion of inspection, the inspection team will prepare tax documents in close correlation with the findings.

The main tax inspection documents are prepared: a) the tax audit report; b) Minutes of control; c) Minutes of contraventions; d) Annexes.

#### **a) Tax Audit Report**

The results of tax audits will be recorded in a tax audit report. It will be made regardless if differences are found, more or less, to the existing tax receivable at the time of the initial findings. Findings are inserted in the tax audit report, which will result in the issuance of the tax decision if the tax base changes. If basis does not change, a decision will be prepared not to modify the tax base. The above decisions are issued not later than 25 working days from the date of conclusion of the audit. The tax audit report is prepared at the completion of tax audit and includes all findings related to tax liabilities periods which are verified, and in connection with other obligations under tax law and accounting that were subject to verification.

#### **b) Minutes of control**

It is an act of control, which records the tax inspectors' findings resulting from actions by unannounced control on the spot recording the acts of criminal nature. Findings recorded in the minutes will result in the issuance of a tax decision. It can be attached to the tax inspection report. The minutes is accompanied by appendices, which are detailed findings or additional evidence.

#### **c) Minutes of contraventions**

In specific legislation for taxation, especially in the Fiscal Procedure Code offenses which meet the conditions necessary to be classified as misdemeanors are punished. The penalty will be set by drawing up a report on misdemeanors.

#### **d) Annexes**

Annexes to the main tax inspection acts are: The tax audit; service order; Explanatory note; Minutes of refund documents; Minutes of sealing or unsealing; the declaration by the taxpayer; other annexes.

For failure to pay the tax debts to the state budget default interest and late payment penalties will be applied. Interest shall be calculated for each day of delay from the day following the payment deadline until the date of settlement including the amount due. Additional claims for tax differences resulting from the correction of statements or modification of a tax decision, interest is due from the day following the due tax which was set up to lead and settlement date inclusively. As of 1 January 2016, the amount of interest is

0.02% per day, a figure that may change in the annual budget laws. The late payment charges are calculated for each day of delay from the day following the payment deadline until the date of settlement including the amount due. The level of interest on arrears is 0.01% for each day of delay. The default does not remove the obligation to pay interest. The default does not apply to undeclared tax liabilities of taxpayer main payer and the tax auditors determined by tax decision. The late payment fee does not remove the obligation to pay default interest. For main tax obligations undeclared or incorrectly declared by the taxpayer or the payer and the tax auditors determined by the tax notice, the taxpayer or the payer owes a penalty for concealing 0.08% per day (tax body does not determine the penalty for failure to declare whether it less than 50 lei) from the day immediately following the due date until the date of settlement of the amount due including the main tax obligations undeclared or incorrectly declared by the taxpayer or the payer and the tax auditor established by tax decision. The penalty for failure to declare to the tax auditor, determined by tax decision is reduced at the request of the taxpayer or payer, with 75% if the main tax obligations set by decision:

- are paid by the legal deadline or compensated;
- are rescheduled for payment, under the law. In this case, the reduction is granted upon completion of payment rescheduling.

The penalty for failure to declare, established by tax auditors through taxation decisions shall be increased by 100% when the main tax obligations have resulted from committing acts of tax evasion detected by the judicial organs according to law. If claims by local budgets due to delay penalties amount to 1% of the principal tax liabilities, calculated for each month or fraction of a month.

The period for which postponements were granted or rescheduled, the main fiscal obligations with scheduled or deferred payment is due, late interest at 0.5% per month or fraction of a month, the equivalent of injury will be paid.

## 2. CASE STUDY

Establish tax, interest, penalties and delay and other sanctions, knowing that the cumulative period of 2016, after the tax audit the following findings were noted:

1. total income 70.000 lei out of which:
  - the cancellation of provisions for impairment of inventories 1.000 lei;
  - dividends for the shares 1.000 lei;
  - revenue from annulment of increased debts to government 1.000 lei;
  - revenue from annulment of increased debts to business partners 1.000 lei.

2. Total expenses 22.000 lei out of which:

- Income tax expense 2,000 lei;
- Salary costs 10,000 lei;
- Entertaining expenses 1,000 lei;
- Sponsorship expenses 1,000 lei;
- Expenses related to socio-cultural activities 1,000 lei;
- Expenses of RON 1,000 fines owed to the state;
- Increases due to business with 1,000 lei;
- Shortages in raw materials inventory 1,000 lei;
- perishable commodities during storage over limit 1.000 lei.

3. Turnover was 50.000 lei.

Problem solving:

1. *Determination of tax by control bodies (Ipc):*

Ipc: 16% ( Pb - Vni + Cn )

2. *Gross profit (Pb):* Pb: VT - CT: VT - (CT - Ip) = 70.000 - (22.000 - 2.000 ) = 50.000 lei.

3. *Non-taxable income Vni:*

-Vn1: income from cancellation of adjustments for impairment (because when they were made, they were non-deductible expenses): 1.000 lei.

-Vn2: dividends (because they were taxed): 1.000 lei.

- Vn3: revenue from annulment of increased debts to government (increases were not deductible): 1000.

Total Vni = 3.000 lei.

4. *Non-deductible expenses:*

-Cn1: non-deductible protocol: 1.000 – 1.020: 0 lei

Total protocol: 1.000 lei

deductible protocol: 2% (Pb + deductibil protocol ) = 2% \* (50.000+1.000) : 1.020 lei

- Cn2: sponsorship: 1.000 lei

- Cn3: non-deductible social –cultural activities: 1000 – 500 : 500 lei

Total activities: 1.000 lei

Deductible activities: 5% x salaries: 5% x 10.000 = 500 lei

- Cn4: fines: 1.000 lei

- Cn5: shortages of raw materials non-imputable: 1.000 lei + 20% VAT (adjustment of deductible VAT): 1.200 lei.

- Cn6: perishables: 1.000 lei +20% VAT (adjustment of deductible VAT): 1.200 lei.

Cn= Cn1+... Cn6 = 4.900 lei.



5.  $Ipc = 16\% (50.000 - 3.000 + 4.900) = 8.304$  lei (tax on control).

6. *Setting related decline in sponsorship (Rip), which is the minimum reduction of the following:*

- $20\% * Ipc = 20\% * 8.304 = 1.661$  lei
- $5/1000 * CA: 5/1000 * 50.000 = 250$  lei
- sponsorship expenses = 1.000 lei

Rip : 250 lei

7. *Finally when determining the tax reduction control after deducting:*

Ipcf:  $Ipc - Rip = 8.304 - 250 = 8.054$  lei

8. *Establishing additional payment obligations: the inspection establishes an additional obligation to pay profit tax, that is:*

$\Delta_{IPCF} : Ipcf - Ipe = 8.054 - 2.000 = + 6.054$ , difference registered in accounting as:

$$691 = 4411 \quad 6.054 \text{ lei.}$$

9. *Setting default interest for the year 2016:*

$$Mi = 6.054 * 365 * 0,02\% = 442 \text{ lei}$$

$$6581 = 4481 \quad 442 \text{ lei.}$$

10. *Establish penalties for failure to declare the year 2016:*

$$Pn = 6.054 * 365 * 0,08\% = 1.768 \text{ lei}$$

$$6581 = 4481 \quad 1.768 \text{ lei.}$$

11. *Setting the fine by accounting law, the amount of 1.000 lei:*

$$6581 = 4481 \quad 1.000 \text{ lei.}$$

12. *75% reduction for paying the penalty for failure to declare in time (75% \* 1.768 = 1.326 lei):*

$$4481 = 7588 \quad 1.326 \text{ lei.}$$

13. *payment of remaining outstanding tax liabilities due within 20 days:*

|             |              |
|-------------|--------------|
| $\% = 5121$ | <u>7.938</u> |
| $4411$      | 6.054        |

$$4481 \quad 1.884 \quad (442 + 442 + 1.000)$$

### 3. Conclusions

The main aspects of governance interest that the statutory auditor must communicate are:

- Romanian fiscal system is declarative, based on voluntary action of the taxpayer to calculate, declare and pay its obligations to the state;
- Tax audit is exercised exclusively, directly and unhindered through the National Agency for Fiscal Administration or, where appropriate, by specialized departments of local authorities, as required by law, or by other authorities that are competent by law to administer taxes, fees, contributions or other amounts owed to the general consolidated budget;
- Tax inspection is to verify the legality and compliance of tax returns, correctness and accuracy of obligations by taxpayers, for the provisions of the tax and accounting, verification or establishment, as appropriate, taxation bases and the determination of differences of liabilities and corresponding accessories thereof;
- Tax audit involves carrying out the following stages: preparation of tax audit; the realization of tax audit; completion of tax audit;
- Preparation of tax audit involves selecting taxpayers to be verified, transmitting notices tax audit and tax audit defense establishment;
- Completion of the tax audit is to perform the following tasks: determine the place of tax audit; determine the duration of the tax audit and verify proper way out of tax obligations;
- At the end of the inspection: the inspection team will prepare tax documents in close correlation with the findings, establishing if any interest, late fees, penalties and fines for failure to declare more to be paid.

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