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# ACCOUNTING AND TAX OPTIMIZATION OF FIXED ASSETS TRANSACTIONS

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**Abstract:** The correct organization of accounting of transactions with fixed assets is of great importance both for the reliable presentation of information in financial statements and for determining the result of the enterprise's activity both in accounting and for taxation purposes. Due to the fact that operations with fixed assets represent not only the receipt and disposal, depreciation accrual, repair, leasing operations, contribution to the authorized capital, etc., thus the author analyzes the consequences of such operations on the result of the enterprise's activity and income tax liability from entrepreneurial activity. This article considers various situations on operations with fixed assets, as well as their impact on the indicators of financial statements of the enterprise. According to the materials of the conditional examples it is possible to analyze the tax consequences for the enterprise on operations with fixed assets, to outline ways to optimize tax payments and correctly develope a policy of tax planning of the enterprise regarding transactions with fixed assets.

**Keywords:** fixed assets, optimization, taxable income, depreciation

**JEL Classifications: M41**

## Introduction

Transactions with fixed assets are performed by practically every enterprise. At the same time, through different recognition of income and expenses on operations with fixed assets, as well as depreciation and repair, in financial accounting and for tax purposes, there is an adjustment of taxable income, which ultimately affects the calculation of income tax liability from business activities. Thus, a competent policy of the enterprise on operations with fixed assets can significantly contribute to the tax optimization of settlements with the budget in terms of income tax from business activities.

It is well known that the differences between the recognition of elements in financial accounting and for tax purposes, arise on income and expenses. However, the initial recognition of the cost of fixed assets in financial accounting and for tax purposes may be different. Thus, for a more in-depth study of this issue, the provisions should be considered:

1. *Law "On Accounting and Financial Reporting" No. 287 of December 15, 2017,*
2. *Tax Code of the Republic of Moldova, Law 1163/1997,*
3. *"Regulations on the procedure for accounting and accrual of depreciation of fixed assets for tax purposes", approved by the Government of the Republic of Moldova No. 704 of December 27, 2019,*
4. *Resolution on approval of the Catalogue of Fixed Assets No. 941 of December 22, 2020,*
5. *National Accounting Standard (NAS) "Long-term Intangible and Tangible Assets",*
6. *National Accounting Standard (NAS) "Asset Impairment",*
7. *National Accounting Standard (NAS) "Exchange Rate Currency and Amount Differences".*

Let's analyze: what provisions of the National Accounting Standards (NAS) and the Tax Code of the Republic of Moldova differ from each other in terms of transactions with fixed assets, for further tax optimization:

- *Recognition of fixed assets,*
- *Initial valuation of fixed assets,*
- *Income from fixed assets transactions,*
- *Expenses on fixed asset transactions,*

- *Depreciation of fixed assets (including those received free of charge, when partially financing the acquisition of fixed assets from sources of non-taxable income, when fixed assets are received at subsidies),*
- *Repair and maintenance of leased fixed assets (leasing, property lease, operating lease or concessions),*
- *Revaluation of fixed assets.*

**Analysis**

Let us analyze the relevant requirements for fixed assets in accordance with the provisions of the tax legislation of RM and financial accounting.

The initial recognition of fixed assets in financial accounting and for taxation purposes has its differences, which are presented in the table below.

**Table 1. Initial recognition of fixed assets**

| According to the provisions of the National Accounting Standards "Long-term intangible and tangible assets" | According to the provisions of the Tax Code of the Republic of Moldova |
|---|---|
| **Item 4.** Fixed assets are long–term tangible assets that have been put into operation, the unit value of which exceeds the cost limit provided for by tax legislation or the materiality threshold established by the entity in accounting policies. | **Article 26[1].** "Deduction of depreciation of fixed assets". Fixed assets on which depreciation is calculated are tangible property intended for use in entrepreneurial activity, reflected in the balance sheet of the taxpayer in accordance with the legislation, the value of which is expected to decrease with physical and moral deterioration and whose service life exceeds one year, and the cost is 12,000 lei. |

*Source: Elaborated by the author based on NAS* (NAS L.-t. I., 2013) *and Tax Code* (Tax Code of the Republic of Moldova, 1997)

Since neither the provisions of the NAS nor the Law "On Accounting and Financial Reporting" (Law, 2017)establish a specific limit in lei equivalent for the recognition of fixed assets, the limit of 12,000 lei established by the Tax Code is adopted in accounting. If the accounting policies of an enterprise establish a limit for the recognition of fixed assets that differs from that specified in the Tax Code, this may affect the taxable income of the enterprise.

Let us consider the situation: in 200X, an enterprise established the following limits for the recognition of fixed assets in its accounting policies:

a) the limit is set at 10,000 lei (lower than specified in the Tax Code - 12,000 lei),

b) the limit is set at 15,000 lei (higher than specified in the Tax Code - 12,000 lei).

***Case Study:*** Let us consider the impact on taxable income and, consequently, on the amount of income tax liability of the provisions of the accounting policies of the enterprise regarding the limit of recognition of fixed assets. For this purpose, both in case a) and in case b) let us set the taxable income before adjustments in the VEN 12 declaration in the amount of 100 000 lei. Let's assume a depreciation rate of 20% both for taxation purposes and for financial accounting. In case a) we will assume that we have acquired an asset that meets the criteria of being classified as fixed assets in the amount of 11000 lei (the limit of recognition in the accounting policies is 10000 lei), accordingly, in the financial accounting we will calculate depreciation in the amount of 2200 lei (11000 lei x 20%) according to the linear method established by the company. For taxation purposes, the asset is not recognized as fixed asset, because the recognition criterion of 12000 lei is not met and, accordingly, depreciation for taxation purposes will not be charged,

In case b), let us assume that a computer was purchased for the amount of 14000 lei, in the accounting policies this asset is recognized as a fixed asset and will be depreciated, from the taxation point of view the computer will be recognized as a fixed asset and will be depreciated, let us assume in the amount of 2800 lei (14000 lei x20%).

**Table 2. Determination of taxable income and income tax in cases where the accounting policies of the enterprise establish a limit for the recognition of fixed assets that differs from the provisions of the Tax Code**

| Indicators | | Case a) the limit for recognizing fixed assets in the accounting policies of the enterprise is set at 10,000 lei | Case b) the limit for recognizing fixed assets in the accounting policies of the enterprise is set at 15,000 lei |
|---|---|---|---|
| Profit before tax in 200X, lei | | 100 0000,00 | 100 000,00 |
| Depreciation Fixed assets, lei | In financial accounting | 2200 | 0 |
| | For tax purposes | 0 | 2800 |
| | The amount of the difference | 2200,00 | -2800 |
| Taxable income, lei | | 102000 | 97200 |
| The amount of income tax (12%) lei | | 12240 | 11664 |

*Source: Elaborated by the author*

Analyzing the indicators in table 2, it can be stated that if an enterprise has established in its accounting policies a limit for the recognition of fixed assets higher than specified in the provisions of the Tax Code, it has a number of advantages in determining the amount of income tax from business activities, which is presented in the above table.

In addition, one should take into account the fact that in 200X, when when putting into operation a computer with the value of 14,000 lei (case b), according to accounting policies recognized as low-value and quickly wearing items, this amount will reduce pre-tax profit by depreciation.

Thus, when developing accounting policies for fixed assets, an enterprise needs to carefully analyze its investment strategy, forecast purchases of long-term assets, in order to optimize income tax obligations in terms of transactions with fixed assets, in terms of setting a limit on their recognition.

***The initial assessment of fixed assets*** is carried out by forming the initial cost in accordance with the provisions of the National Accounting Standards "Long-term intangible and tangible assets" in financial accounting and the input cost for tax purposes. In accordance with the provisions of paragraph 18 of Article 26[1] "Depreciation of fixed assets" of the Tax Code of the Republic of Moldova: "the input cost of fixed assets is established in accordance with the provisions of National Accounting Standards or IFRS, which do not contradict the provisions of this Code." (Tax Code of the Republic of Moldova, 1997)

Thus, it is necessary to analyze the situations when the provisions of accounting standards and the Tax Code of the Republic of Moldova regarding the formation of the initial value of fixed assets will be different, for example: such situations are possible at:

- ◊ *Import of fixed assets, if the provisions of the accounting policies of the enterprise in terms of applying the exchange rate do not correspond to the provisions of the Tax Code,*
- ◊ *Capitalization of borrowing costs during the creation of a fixed asset, when the rate on loans (credits), which is included in the initial cost in financial accounting is higher than the weighted average interest rate on loans established by the tax legislation,*
- ◊ *Including a provision in the initial cost of a fixed asset, in the case of accounting under IFRS and in some other cases.*

In accordance with the provisions of paragraph 7 of the NAS "Exchange rate and amount differences": "transactions in foreign currency are initially reflected in accounting in the national currency by applying the official exchange rate of the Moldovan lei on the date of initial registration, which is determined depending on the type of transaction: ... export/import of assets, services, works, other international trade transactions:

- ✓ *date of preparation of the customs declaration; or*
- ✓ *date of preparation of the primary document confirming the transfer of ownership of assets or provision of services, works; or*
- ✓ *other date stipulated by the current legislation."* (NAS E. R., 2013)

In accordance with the provisions of paragraph 3 of Article 21 "Special rules relating to income" of the Tax Code, when conducting transactions in foreign currency: "when calculating taxable income, gross income and other receipts, as well as expenses incurred in foreign currency, are converted into the national currency at the official exchange rate of the Moldovan lei effective on the day of the transaction. …...The date of the transaction is considered to be the date reflected on the bank account statement and/or payment account, and in other cases, the date indicated in the primary documents, according to the financial accounting method based on the provisions of National Accounting Standards and IFRS." (Tax Code of the Republic of Moldova, 1997)

Thus, the date of the transaction is indicated in the Tax Code of RM, either the payment document or the primary document, upon import it may be an invoice or a customs declaration.

Let's assume that according to the contract with the non-resident, the resident of the Republic of Moldova imports equipment value €10,000, the euro exchange rate in accordance with the contract date is 20.11 lei, during customs clearance 20.22 lei. Thus, the initial cost of the equipment (we abstract from other customs duties) in financial accounting will be: 201,100 lei, the input cost of the imported equipment will be 202,200 lei. Thus, it is possible to calculate the depreciation of fixed assets in financial accounting, using the linear method, the depreciation rate of 20%, which will amount to 40,220 lei, for tax purposes, under the same conditions it will amount to 40,440 lei.

Thus, the amount of the difference between the accrued depreciation for tax purposes and in financial accounting in 220 lei will reduce the taxable income of the enterprise. If the exchange rate applied in financial accounting is higher than for tax purposes, then the initial cost of the fixed asset reflected in financial accounting will be higher than for tax purposes, as well as the corresponding accrued depreciation. Thus, the difference between the accrued depreciation for tax purposes and in financial accounting will increase the taxable income.

As a summary, it should be noted that the enterprise should take a balanced approach to elaborating accounting policies in terms of applying the exchange rate. If the enterprise does not want deviations between the provisions of the NAS and the Tax Code, then the accounting policies should indicate the date of the transaction, for example, on the date of preparation of the primary document (customs declaration or invoice).

**Income and expenses from operations with fixed assets**

The analysis of the impact of income and expenses on transactions with fixed assets on taxable income can be carried out taking into account the financial result obtained from such transactions, which is presented in Table 3.

**Table 3. Determination of the financial result of transactions with fixed assets for taxation purposes and in financial accounting**

| Fixed Assets Operations | Determination of Financial Result for Tax Purposes | Determination of Financial Result in Financial Accounting | Comments |
|---|---|---|---|
| sale | The tax result is defined as the difference between the income received from alienation and the non-depreciable value for tax purposes of the fixed asset. | The financial result is defined as the difference between account 621 “Income from operations with long-term assets” and account 721 “Expenses associated with long-term assets” | It should be noted that account 721 “Expenses related to long-term assets” also reflects all expenses related to the sale |

| | | | |
|---|---|---|---|
| Donation | the tax result is determined as follows: 1) in the case where at the time of donation the market value of the fixed asset is greater than the non-depreciable value for tax purposes, the tax result is determined as the difference between the market value at the time of donation and the non-depreciable value for tax purposes; 2) in the case where the non-depreciable value for tax purposes is greater than the market value at the time of donation, the tax result is zero. | In the case of a donation, the income is not reflected in the financial accounting of the enterprise that donated the fixed assets; only the expenses for the disposal of the donated fixed assets will be reflected. | In Appendix 1.1 D Reference to line 0207 "Income from donation of assets" of Declaration VEN 12, the largest value between the market and book value of fixed assets donated is determined, the largest of these values is reflected in line 0207 in Appendix 1D "Adjustment (increase/decrease) of income in accordance with tax legislation" of Declaration VEN 12 in column 3 "For tax purposes", in column 2 "In financial accounting" the figure 0 will be reflected. |
| Exchange | the tax result is determined as the difference between the value of the fixed asset received under the contract, adjusted for the amount of cash that must be additionally received or paid in accordance with the contract and the non-depreciable value for tax purposes of the transferred fixed asset. | Reflected in case study 2 | Line 0210 is filled in "Income received in non-monetary form (Tax Code, art. 21, part (1) of Appendix 1D "Adjustment (increase/decrease) of income in accordance with tax legislation" of the Declaration VEN 12 |

*Source: Elaborated by the author*

***Case Study 2***. Firm "Alpha" exchanged the equipment with a book value of 100 000 lei and a contractual value of 130 000 lei for a car with a contractual value of 150 000 lei. At the same time, the company "Alpha", besides the contractual value of the equipment, paid 20 000 lei to the supplier. Accounting records of the exchange for the firm "Alpha" are the following:

*1) The depreciation of the book value of the equipment is reflected:*

Debit account 721 "Expenses associated with long-term assets" - 100,000 lei,
Credit account 123 "Fixed assets" - 100,000 lei.

*2) Income from the disposal of equipment is reflected:*

Debit account 234 "Other current accounts receivable" - 130,000 lei,
Credit account 621 "Income from operations with long-term assets" - 130,000 lei.

*3) The initial cost of the received passenger car is reflected:*

Debit account 123 "Fixed assets" - 150,000 lei,
Credit account 521 "Current commercial liabilities" - 150,000 lei.

*4) The offset of settlements with the supplier of the passenger car is reflected:*

*-for the amount of the contractual cost of the equipment:*
Debit of account 521 "Current commercial liabilities" - 130,000 lei,
Credit of account 234 "Other current accounts receivable" - 130,000 lei.
*- for the amount of transferred funds:*
Debit of account 521 "Current commercial liabilities" - 20,000 lei,
Credit of account 242 "Current accounts in national currency" - 20,000 lei.

**Conclusion**

The main objectives of accounting for fixed assets are correct documentation and timely reflection in the accounting registers of the receipt of fixed assets, their internal movement and disposal; correct calculation and reflection in the accounting of the amount of depreciation of fixed assets; accurate determination of the results of the liquidation of fixed assets; control over the costs of repairing fixed assets, their safety and efficiency of use.

Based on the above mentioned, it can be noted that the provisions for transactions with fixed assets in terms of their recognition, valuation, depreciation, repair costs in financial accounting and for tax purposes have a number of features and differences.

In this regard, when planning its investment policy, an enterprise must first of all take into account the aspects of recognition of fixed assets, as well as their valuation. These provisions must be established in the accounting policies of the enterprise.

Analyzing transactions with fixed assets and their reflection in accounting, one should first refer to the established limit of fixed assets for their recognition, as noted earlier, this limit is established by the Tax Code of the Republic of Moldova.

It should be noted that the limit set by the tax legislation regarding the recognition of fixed assets in the amount of 12,000 lei is very low. Currently, when inflation is high enough and equipment, buildings, and vehicles have a high market value, this limit should be raised at least by an order of magnitude.

In conclusion, it should be noted that when carrying out transactions with fixed assets, many nuances should be taken into account in order to optimize tax obligations to the budget in terms of income tax from business activities. First of all, the provisions of the company's accounting policies regarding operations with fixed assets should be carefully considered. It is imperative to take into account the investment policy of the company.

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