

TAX PLANNING IN A PRIVATE COMPANY AS THE BASIS FOR IMPROVING THE EFFICIENCY OF ITS ACTIVITIES

Nataly Podolyakina, Maxim Kaimov

Abstract: *Tax planning allows you to significantly reduce the cost of maintaining an enterprise due to a well-thought-out strategy for optimizing the tax burden. Using the financial statements and internal accounting documents of the investigated object, namely a Latvian company, a decline in the rate of development of the company and a decrease in the main indicators of the financial position of the company for the last analyzed years were revealed. An important role in business development is played by the amount of costs associated with paying taxes, the payer of which is the enterprise. There is an increase in the tax burden on the enterprise. The level of tax burden at the enterprise indicates that the enterprise needs regular tax planning activities.*

Keywords: *taxation, tax planning, tax burden, financial rate, efficiency*

JEL classifications: *H71, H26*

1 INTRODUCTION

Tax planning is an important and integral part of the internal planning of the enterprise, which is a component of the financial management system in the enterprise. This is due to the fact that taxation is associated with all spheres of production, financial and economic activities of an enterprise throughout the entire period of its existence.

In conditions of high tax rates, incorrect or insufficient accounting of the tax factor can lead to very unfavorable consequences or even cause bankruptcy of the enterprise. On the other hand, the correct use of benefits and discounts provided by tax legislation can ensure not only the safety of the received financial savings, but also the possibility of financing the expansion of activities, new investments due to savings on taxes or even due to the return of tax payments from the treasury.

2 TAX PLANNING AND THE EFFICIENCY OF THE PRIVATE COMPANY ACTIVITIES

First of all, when studying tax payments and their effect on the enterprise's financial results it is necessary to determine the payer of which taxes of the Republic of Latvia the study object is.

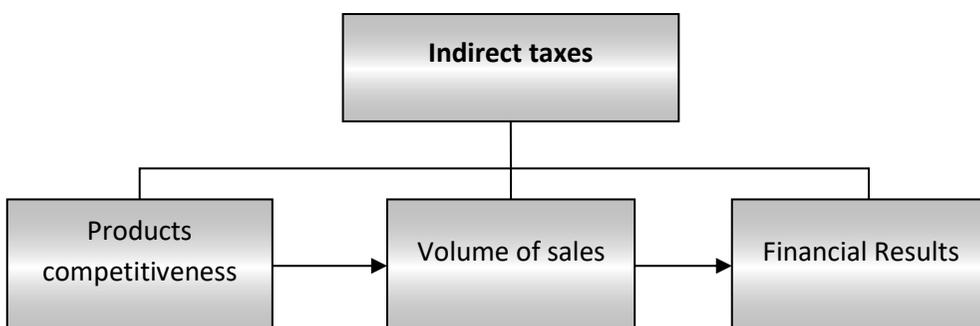
At present, there are 15 types of taxes in Latvia. They are both direct and indirect taxes. The direct taxes, compared to indirect ones, are believed to have the greatest effect on the enterprise's financial results.

Indirect taxes are included in the products price; the public is their actual payer, as the final consumer of products and services. But this does not mean that indirect taxes do not affect the enterprise's financial results.

Indirect taxes are paid by intermediaries (producers of taxed goods), who then reimburse them from the third parties (consumers). Indirect taxes are included in the price of a product or service, therefore, it increases, while the competitiveness of the product or service decreases. A decrease in the competitiveness of a product or service negatively affects the volume of sales, cost, and, ultimately, the enterprise's profit.

The mechanism of the effect of indirect taxes on the enterprise's financial results is shown in Figure 1.

Figure 1: The Mechanism of Indirect Taxes Effect on the Financial Results of the Enterprise's Activities



Source: (Зарунова, 2014)

Direct taxes are taxes that are directly collected from a taxpayer's income or property. A direct tax payer bears obligations related to the payment of tax and does not transfer them to the third parties. When direct taxes are collected,

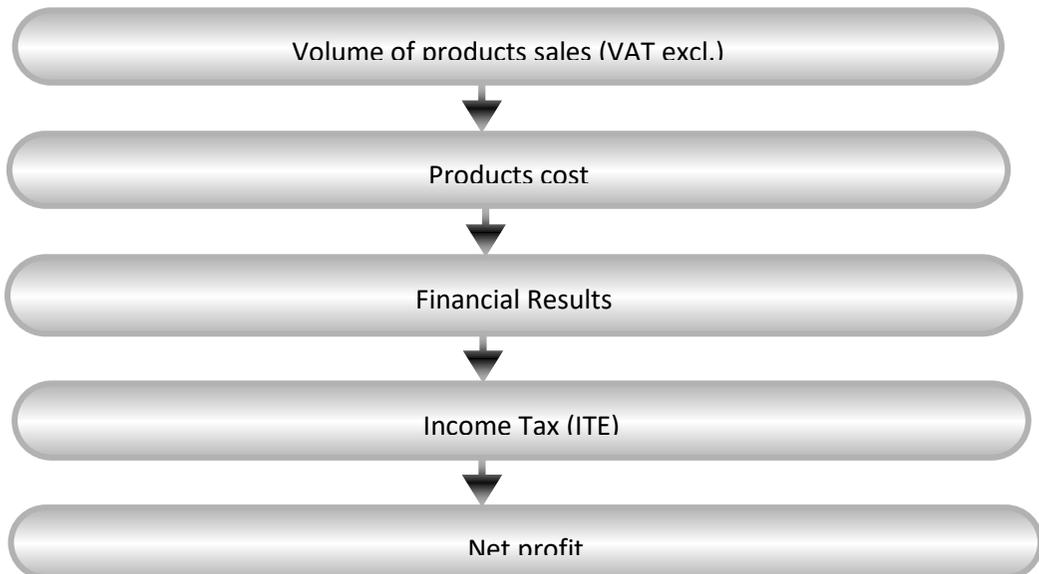
the state faces the actual taxpayers. The mechanism of the direct taxes effect on the enterprise's financial results is shown in Figure 2.

In accordance with the classification above, the study object is a legal entity, a resident of Latvia who is independently obliged to calculate and pay taxes to the budget of Latvia.

The study object is a payer of the following taxes and duties in accordance with the legislation of the Republic of Latvia in force:

- VAT
- Public income tax
- Mandatory social transfers
- Income tax on enterprises
- Natural resources tax
- Business risk state duty

Figure 2: The Mechanism of Direct Taxes Effect on the Financial Results of the Enterprise's Activities



Source: (Zapunova, 2014)

When analyzing tax payments and their effect on the enterprise's financial results, it is important to draw up a tax calendar that allows gaining insight of the tax obligations of the studied enterprise and controlling the correctness of the calculation and compliance with the deadlines for the tax payments, as well as the reporting (Ketners K., 2008).

Table 1. Tax calendar (Author)

Tax type	Tax object	Tax rate	Taxation period	Reporting term	Tax payment term
VAT	Supply of goods for a fee, including self-consumption	21%	1 month*	Within 20 days after the taxation period	Within 20 days after the taxation period
Public income tax	Employee's gross wage excluding social benefits, tax-exempt minimum and trust-funders benefits	20% 23%	1 month	By the 15 th day of each next month	By the 15 th day of each next month
Income tax on the enterprise	Dividends, conventional dividends, non-business expenses	20%	1 month	No later than January 15 after the end of the reporting year	Within 15 days after submission of the monthly declaration
Mandatory social transfers	Employee's gross wage	24.09% and 11%	1 month	By the 15 th day of each next month	By the 15 th day of each next month
Natural resources tax	Plastic or polyethylene packaging	0.65 euro/kg	1 quarter	Once per quarter by the 20 th day of the next month	Once per quarter by the 20 th day of the next month
Business risk state duty		0.36 euro/employee	1 month	By the 15 th day of each next month	By the 15 th day of each next month

* such a taxation period is provided for the studied enterprise, since it falls under the criteria described in the law "On VAT"; taxation period of 1 month is for those taxpayers who sell products or provide services to the EU countries or their taxed transactions within the previous taxation period (12 months) exceeded 40,000 euros; taxation period of 1 quarter is for those

payers whose volume of taxed transactions within the previous taxation year did not exceed 40,000 euros and who do not sell goods or provide services to EU countries.

The next step in the analysis of tax payments is to analyze the dynamics and structure of tax payments for the study object. The studied period covers 5 years. Table 2. provides the main financial indicators and tax payments, the payer of which is the enterprise.

Table 2: The Enterprise's tax payments for 2015-2019, euro [10]

Indicators/Year	2015	2016	2017	2018	2019
Income	134590	177940	249970	246431	182467
Net profit	21905	37631	51669	43090	25603
Public income tax	4187.70	2239.71	4331.00	5435.00	4233.45
Mandatory social transfers, including:	3440.27	4819.47	9935.00	12656.0	7753.85
Mandatory social transfers (employee)	935.75	1310.90	2702.32	3442.36	2108.92
Mandatory social transfers (employer)	2504.52	3508.57	7232.68	9213.69	5644.93
Business risk state duty	47.600	40.000	46.000	46.000	36.000
VAT	25973.69	32030.77	45655.00	44358.00	38315.46
ITE (income tax on enterprises)	4187.00	6778.20	9404.00	8202.00	5221.00
Natural resources tax	110.00	80.97	62.00	263.00	180.00
Taxes paid	37946.26	45989.12	69433.00	70960.00	55739.76

Studying the indicators provided in the table, there is a tendency for a decline in the enterprise development within the period from 2018 to 2019, the income from the products sale decreased by 26% in 2019, the net profit decreased by 40%, with an increase in the share of the cost in the income from 52% in 2018 to 62% in 2019. The slump in the enterprise's financial performance in 2019 resulted a reduction in tax payments of 15,220 euros, which is 21% less than in 2018.

Table 3: Analysis of the dynamics of tax payments for 2015-2019 (Author)

Indicators/Year	Absolute deviation (2016/2015)	Absolute deviation (2017/2016)	Absolute deviation (2018/2017)	Absolute deviation (2019/2018)
Income	43350.00	72030.00	-3539.00	-63964.00
Public income tax	-1947.99	2091.29	1104.00	-1201.55
Mandatory social transfers, including:	1379.20	5115.53	2721.00	-4902.15
Mandatory social transfers (employee)	375.14	1391.42	740.04	-1333.44
Mandatory social transfers (employer)	1004.06	3724.11	1981.01	-3568.76
Business risk state duty	-7.60	6.00	0.00	-10.00
VAT	6057.08	13624.23	-1297.00	-6042.54
ITE (income tax on enterprises)	2591.20	2625.80	-1202.00	-2981.00
Natural resources tax	-29.03	-18.97	201.00	-83.00
Taxes paid	8042.86	23443.88	1527.00	-15220.24

The analysis of the tax payments dynamics for 2019 indicates a decrease in tax payments on all types of taxes, the payer of which is the enterprise.

Tax payments on VAT decreased to a greater extent, then a decrease in tax payments on mandatory state social insurance contributions (Mandatory social transfers) can be observed. As for the analysis of the structure of tax payments, the data are summarized in Table 4.

Table 4: The Analysis of the Structure of Tax Payments for 2015-2019 (Author)

Indicators/Year	2015	2016	2017	2018	2019
Public income tax	11.04	4.87	6.24	7.66	7.60
Mandatory social transfers, including:	9.07	10.48	14.31	17.84	13.91
Mandatory social transfers (employee)	2.47	2.85	3.89	4.85	3.78
Mandatory social transfers (employer)	6.60	7.63	10.42	12.98	10.13
Business risk state duty	0.13	0.09	0.07	0.06	0.06
VAT	68.45	69.65	65.75	62.51	68.74
ITE ((income tax on enterprises)	11.03	14.74	13.54	11.56	9.37
Natural resources tax	0.29	0.18	0.09	0.37	0.32
Taxes paid	100%	100%	100%	100%	100%

Based on the analysis of the structure of tax payments, we can conclude that the largest share in the taxes paid by the enterprise are VAT payments - 68.74% of the amount of all tax payments.

The second tax in terms of cross section in tax payments is the mandatory state social insurance contributions (Mandatory social transfers).

Tax payments also affect the structure of products cost. Tax burden indicator may be determined by the formula (Зарипова, 2014)

$$TB_c = TP_c / C \quad (1)$$

Where TB_c – indicator of tax burden on products cost

TP_c – tax payments amount, included to the products cost

C – products total cost

Table 5: Tax Burden on the Cost for 2015-2019 (Author)

Indicators/Year	2015	2016	2017	2018	2019
Total cost	107383	131625	185261	190320	146603
tax payments, included to the cost	7785.57	7180.15	14374	18400	12203.3
Tax burden on the cost	0.073	0.055	0.078	0.097	0.083

When analyzing the indicators of the tax burden on the products cost within the period of 2016 - 2018 there is a tendency for this indicator growth, which negatively affects the price of manufactured products.

Tax payments affect the pricing of products manufactured. The wholesale price consists of the following components (Спирина, 2007):

$$\text{Wholesale price} = \text{Cost} + \text{Profit} + \text{Excise} + \text{VAT} \quad (2)$$

Table 6: Determination of Wholesale Price and Tax Payments Share in the Cost for 2015-2019 (Author)

Indicators/Year	2015	2016	2017	2018	2019
VAT	25973.69	32030.77	45655	44358	38316
ITE	4187	6778.2	9404	8202	5221
Total cost	107383	131625	185261	190320	146603
tax payments, included to the cost	7785.57	7180.15	14374	18400	12203.3
Wholesale price	159448.69	208064.97	291989	285970	215742.46
Tax payments share in the wholesale price	23.80%	22.10%	23.78%	24.81%	25.84%

With increase of the share of tax payments, the tax burden for the enterprise is increased in the wholesale price and vice versa. The trend of growth of the share in the tax payments in the wholesale in 2016-2019 is characteristic for the studied object, which also negatively influences the financial results of the enterprise activities. The share of the tax payments in the wholesale price can be determined using the following formula (Зарипова, 2014)

$$d = (T_c + E + VAT + T_{FR} + T_p) / \text{Wholesale price} \times 100\% \quad (3)$$

Where d – share of the tax payments in the wholesale price, %

T_c – sum of the tax payments in the cost price

E – excise

T_{FR} – taxes attributed to the financial results

T_p – taxes paid from the organization's profit.

The next important stage in the analysis of the tax payments and their influence on the financial results of the enterprise activities and tax planning is the determination of the tax burden degree. As mentioned above, this study has no clear positions in determination of the tax burden on the enterprise.

The authors have made a decision to consider several approaches in determination of the tax burden.

One of which, the tax burden shall be calculated using the following formula (Зарипова, 2014):

$$TB_{ee} = TP / RS \times 100 \% \quad (4)$$

where TB_{ee} – the tax burden coefficient on the economic entity

RS – total revenue from the sale of products and other sales, including indirect taxes

TP – all tax payments to be made by the enterprise.

As mentioned above, some researches of this problem suggest to determine the tax burden as the ration of tax payments to the newly created cost.

The newly created cost shall be calculated by the formula (Зарипова, 2014):

$$NCC = LC + TP + P, \quad (5)$$

where NCC – newly created cost

LC – labour costs

TP – all tax payments to be made by the enterprise.

P – profit.

In this case, the tax burden shall be calculated by the formula (Зарипова, 2014)

$$TB_{ee} = TP / NCC \quad (6)$$

Table 7: Determination of the tax burden on the enterprise for 2015-2019 (Author)

Indicators/Year	2015	2016	2017	2018	2019
Revenue	160,563.69	209,970.77	295,625.00	290,789.00	220,782.46
Tax payments, total	37,946.26	45,989.12	69,433.00	70,960.00	55,739.76
Tax burden	23.63%	21.90%	23.49%	24.40%	25.25%
Labour costs	12,916.00	18,155.00	36,749.00	47,707.00	29,154.58
Profit	26,087	44,409	61,073	51,555	30,824
Newly created cost	76,949.26	108,553.12	167,255.00	170,222.00	115,718.34
Tax burden (NCC)	49.31%	42.37%	41.51%	41.69%	48.17%

The first indicator of the tax burden calculated in table allows us to determine the share of taxes in the revenue for sale of products. The larger this value, the higher the tax burden on the enterprise. The tax burden on the enterprise has the tendency of growth, and this indicator has made up 25.25% in 2019.

The necessity and volume of the tax planning is directly related to the tax burden degree in a particular tax jurisdiction.

The necessity in tax planning can be analysed based on the tax burden degree on the enterprise. Below there is the table allowing to assess the need in the tax planning based on the tax burden degree.

Table 8: The tax planning level at the certain level of the tax burden (Ketner, K., Lukašina, O., 2008)

TB/IRR	Tax planning level	Need in planning level
10-15%	<ul style="list-style-type: none"> accurate accounting, internal document flow, and use of direct benefits professional accountant level one-time consultations with an external tax consultant In such a situation, tax payments can be monitored by an accountant, or one of his deputies, or an external consultant. 	Minimal, one-time events
<u>20-40%</u>	<ul style="list-style-type: none"> tax planning becomes part of the general system of financial management and control, special preparation (planning) of contract schemes for standard, large and long-term contracts requires specially trained personnel, supervision and guidance from the CFO subscription service in a specialized company Taxes become the object of the general system of current financial control; short and medium term forecasts of tax payments of the enterprise are carried out. 	Necessary, regular activities
45-60%	<ul style="list-style-type: none"> the most important element of the creation and strategic planning of the organization's activities and its current daily activities in all external and internal directions requires specially trained personnel and organization of close interaction with all services of the organization constant work with an external tax consultant and the presence of a tax attorney special development program, mandatory tax analysis and expertise of any organizational, legal or financial measures and innovations by tax consultants 	vital, daily activities

45-60%	<ul style="list-style-type: none"> • Tax planning is becoming the most important element of financial and economic work at all enterprises. Supervision of tax payments should be carried out at the level of the senior executive of the company. Large enterprises have tax planning departments and external tax consultants. 	vital, daily activities
more than 60%	<ul style="list-style-type: none"> • change of field of activities and/or tax jurisdiction 	no comment

To determine the level of tax planning based on the size of the tax burden, the tax burden indicator calculated as the share of taxes in the revenues from product sales shall be applied. In accordance with the values of the tax burden in the range of 22% - 25 %, the company needs tax planning with regular activities. Tax planning should be a part of financial management and control, a specialist or external consultant on tax planning matters should be available, short and medium-term forecasts of the company's tax payments should be carried out.

Professor Karlis Ketner of Riga Technical University proposed to determine the tax burden for each tax, and the following indicators are used for this, the values of some of them are presented in Table 9, with their correlation with the object of taxation. These indicators will help us to determine which taxes have the greatest impact on the tax burden degree (Ketner, K., 2006).

Table 9: Analysis of the tax burden of individual tax groups in relation to the sources of payment at the enterprise (Author)

Indicators/Year	2015	2016	2017	2018	2019
Tax burden affecting sales volume	16.18%	15.25%	15.44%	15.25%	17.35%
Tax burden affecting profits	16.47%	15.45%	15.50%	16.50%	17.52%

Another stage of tax planning is to determine the effectiveness of tax management or tax planning.

The effectiveness of the implementation of tax planning shall be determined using the number of indicators, the general scheme of which provides for the ratio of the totality of tax expenses or individual components to the volume of

sales, cost price or profit. Indicators can be calculated both in shares and in percentages.

The indicators of the effectiveness of the implementation of tax planning are given in the table. These indicators characterize the efficiency of tax planning. However, it is impossible to provide recommended values for all coefficients.

Table 10: Indicators of the effectiveness of the tax planning implementation (Author)

Indicator name	2015	2016	2017	2018	2019
General coefficient of tax planning efficiency	57.73%	81.83%	74.42%	60.72%	45.93%
Tax/sales ratio	23.63%	21.90%	23.49%	24.40%	25.25%
Profit tax rate	16.47%	15.45%	15.50%	16.50%	17.52%

These indicators comprehensively characterize the efficiency of tax planning (Бернштейн, Л., 2003). However, there are no recommended or valid values. The assessment of the efficiency is possible only on the basis of dynamic calculations, which allow to determine trends for each enterprise. Analyzing the dynamics of indicators, we can conclude that the overall coefficient of tax planning will decrease in 2019, but at the same time, there will be an increase in the indicators of the tax/sales ration and taxation of profits (profit before taxes was used in the calculations).

Summing up the results of the analysis of the financial situation and the analysis of tax payments of the enterprise, we can conclude that the main financial indicators for the last analyzed years have decreased: in 2019, the net turnover decreased by 26%, net profit - by 40%, the share of the cost price increased from 52% up to 62%, which influenced the result of the company's activity, namely, the share of net profit decreased from 17.5% to 14%; however, the company maintained its financial strength, with a slight decrease in net operating current assets and total current assets; liquidity indicators indicate the stability of the enterprise, and the profitability of the company's sales decreased during 2018-2019; as for the analysis of tax payments, tax payments decreased in 2019 by 15,220 euros in 2019, which was 21% of the same indicator in 2018; there was an increase in the tax burden on the company in 2019.

3 RESULTS

An important factor influencing the financial results of the company in 2019 was the list of changes in the tax legislation of Latvia, namely, an increase in tax rates on main taxes, and a reduction in the amount of benefits and discounts for taxpayers. The same changes and cuts in the tax legislation of Latvia came into force in 2018. The main goal of such government decisions was to increase budget revenues. The increase in tax rates did not bring the desired result, but, on the contrary, reduced budget revenues. Which once again proves the consistency of Arthur Laffer's theory of the relationship between tax revenues and the dynamics of tax rates. In this regard, it is necessary to assess the impact and degree of dependence of tax payments and increases in tax rates on the main macroeconomic indicators, namely on GDP.

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AUTHORS

Assoc. Prof. Nataly Podolyakina, Dr.oec., Transport & Management Faculty, Transport and Telecommunication Institute, Lomonosova str. 1, Riga, Latvia, e-mail: Podolakina.N@tsi.lv.

Maxim Kaimov, Mg.oec., MARX LLC Board Member, ENGELS LLC Financial Advisor, Lomonosova str. 1, Riga, Latvia, e-mail: maxkaimov@inbox.lv.