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THE DIFFERENCE BETWEEN ACCOUNTING AMORTIZATION AND FISCAL AMORTIZATION

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ABSTRACT

Although the issue of deferred taxes is very important, it is very little known to the taxpayers and to the fiscal bodies, both in meaning and content and in the practical methodology of application. This paper describes the meaning and the content of deferred income taxes, the distinction between accounting amortization and fiscal amortization, the practical methodology for the application of deferred income, all of these in the line of tax facilities granted as accelerated amortization applied pursuant to art. 24 paragraph (9) of the Tax Code.

Keywords

Income tax, taxable profit, accounting loss, fiscal loss, fiscal amortization, accounting amortization, recovery of losses, linear amortization, accelerated amortization

1. Introduction

The taxpayers, the fiscal bodies and other experts of the financial, accounting, and fiscal field encounter difficulties relating to the meaning and contents of deferred taxes and, most of all, relating to the *difference* between accounting amortization and fiscal amortization, as well as to the practical methodology for the application of deferred taxes.

These problems will be clarified if we look at the following legal provisions, even if, surprisingly, they do not include regulations in this direction.

2. Accounting Amortization and Fiscal Amortization

The ***Law no.82/1991 – The Accounting Law*** stipulates the following aspects:

Art. 19. (1) In accounting, profit or less is established cumulatively from the beginning of the financial year. Usually, the

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closing of the income and expense accounts occurs at the end of the financial year.

(2) The final result of the financial year is established at the closing of such year.

(3) Profit (income) distribution is entered in accounting according to destinations, after the approval of the annual financial statements.

(4) Accounting loss brought forward is covered from the profit of the financial year and from the profit brought forward, as well as from reserves, share premium and share capital, in accordance with the decision of the general shareholders' assembly. […].

The **Tax Code** stipulates:

"*Art. 24 – Fiscal amortization. [...]*

(9) Regarding the method of accelerated amortization, the amortization is calculated in the following manner:

a) for the first year of use, amortization cannot exceed 50 % of the initial cost of the asset;

b) for the following years of use, amortization is calculated by relating the remaining amortization value of the fixed asset to its normal remaining duration".

Art. 26. Fiscal losses

(1) Annual loss, established by the income tax return, is recovered from the taxable income obtained in the following 5 consecutive years. The recovery of loss will occur in the order of their entry, on each term of payment of the income tax, according to the legal provisions in force in the year of their entry.[…].

Having as example a fixed asset with an inventory value in the amount of 10,000 lei and the allowed service time (d.s.n.) of five years, ***table no. 1*** describes the expenses fiscally deductible with the linear amortization, which are substantially different from those generated by *accelerated* amortization.

Table no. 1

No.	I.V.	D.S.N.	Year					Total amortization
			1	2	3	4	5	
0	1	2	3	4	5	6	7	8=3+4+5+6+7
1	Deductible expenses with ***linear amortization***							
2	10,000	5	2,000	2,000	2,000	2,000	2,000	10,000
3	Deductible expenses with ***accelerated amortization***							
4	10,000	5	5,000	1,250	1,250	1,250	1,250	10,000

NOTES: I.V. = Inventory value. D.S.N. or d.s.n. = Allowed service duration.

If the *accelerated,* amortization method is applied, in accordance with art. 24 para. (15) of the Tax Code, amortization is calculated in the manner described hereunder:

a) for the first year of use, amortization = 50 % of the fixed asset initial cost = 50 % x 10,000 lei = 5,000 lei;

b) for each of the 4 subsequent years remaining at amortization = the fixed asset value that remains to be amortized: it normal remaining duration = (10,000 – 5,000) lei : (5 – 1) years= 5,000 lei : 4 years = 1,250 lei.

When ***accelerated*** amortization is applied, considerable, sometimes even radical changes occur, in the unit's ***fiscal*** result.

The application of accelerated amortization results, in the year of use, in either the sometimes substantial decrease of the taxable income and, thus, of the income tax due, or the write-off, when the unit no longer owes income tax.

It is particularly important to keep in mind that ***negative fiscal effects generated by the application of accelerated amortization (seen either in the decrease of the taxable income, or in the unit's fiscal write-off) are only temporary, only in the first year(s) of use of the fixed asset subject to accelerated amortization.***

In other words, the negative fiscal effects generated by the application of accelerated amortization occur only in the first year(s) of the allowed service duration of the fixed asset subject to accelerated amortization.

Throughout the entire allowed service duration (d.s.n.) of the fixed asset for which accelerated amortization was applied (which led to such a change in the fiscal result), in normal conditions, the same fiscal result as the one that could have

been obtained in the case of linear amortization was bound to be obtained.

If the unit entered fiscal loss in the first year of use of the fixed asset subject to accelerated amortization, this loss will be recovered from the taxable income obtained in the following 5 consecutive years, according to art. 26 of the Tax Code.

The recovery of losses will occur in the order of their entry, on each payment term for the income tax, pursuant to the legal provisions in force in the year of their entry.

Fiscal modifications are only "re-distributive", only within the allowed service duration of fixed asset subject to accelerated amortization.

At the end of the allowed duration of the fixed asset subject to accelerated amortization, the fiscal result (taxable income and income tax to the state budget, cumulative, should be the same, by both methods of amortization. In the case of linear amortization, where amortization, in absolute terms, is the same, even, for the entire allowed service duration of the fixed asset subject to amortization, we cannot talk about deferred taxes. In other words, from all the applied systems of amortization, admitted by the law, it is only the application of accelerated amortization that leads to deferred taxes.

For a correct and complete understanding of the issue of deferred taxation, we will start from the example in ***table no. 2***, which illustrates the situation of a unit's accounting and fiscal result, both when linear amortization is applied and when accelerated amortization is put in practice.

Table no. 2

Line (**L**).	Indicator	Year 1	Year 2	Year 3	Year 4	Year 5	Total
0	1	2	3	4	5	6	7=2+3+4+5+6
	In the conditions of ***linear amortization***						
1	Total income.	50,000	50,000	50,000	50,000	50,000	250,000
2	Expenses, without amortization expenses	47,000	47,000	47,000	47,000	45,000	235,000
3	Amortization expenses.	2,000	2,000	2,000	2,000	2,000	10,000
4	Total expenses = L2 + L3	49,000	49,000	49,000	49,000	49,000	245,000
5	Taxable income, distinct per year = L1–L4	1,000	1,000	1,000	1,000	1,000	5,000
6	Income tax, distinct per year = L5 x 16%	160	160	160	160	160	800
7	Taxable income, cumulative.	1,000	2,000	3,000	4,000	5,000	5,000
8	Income tax, cumulative.	160	320	480	640	800	800
	In the conditions of ***accelerated amortization***						
9	Total income.	50,000	50,000	50,000	50,000	50,000	500,000
10	Expenses, without amortization expenses	47,000	47,000	47,000	47,000	45,000	235,000
11	Accelerated amortization expenses.	5,000	1, 250	1, 250	1, 250	1, 250	10,000
12	Total expenses = L9 + l10	52,000	48,250	48,250	48,250	48,250	245,000
13	Taxable income, distinct per year = L9 – L12	–2,000	1,750	1,750	1,750	1,750	5,000
14	Income tax, distinct per year = L13 x 16%	–320	280	280	280	280	800
15	Taxable income, cumulative.	–2,000	–250	1,500	3,250	5,000	5,000
16	Income tax, cumulative.	–320	–40	240	520	800	800

Notes:

L = line/row. Pf. = profit. Iz. = tax. Pf. iz. = taxable income. Iz. pf. = income tax.

The table indicator are calculated only on 5-year amortization periods.

In accordance with art.19 of the Tax Code: taxable income (Pf.iz.) = total revenues (V.t.) – total expenses (C.t.) – non-taxable income (V.niz.) + non-deductible expenses (C.ned.).

Pf.iz. = V.t. – C.t. – V.niz. + C.ned. = (V.t. – V.niz.) – (C.t. – C.ned.)

If V.niz. = 0 and C.ned. = 0, like in this example: taxable income (Pf.iz.) = total revenues (V.t.) – total expenses (C.t.) – 0 + 0 = total revenues (V.t.) – total expenses (C.t.).

Pf.iz. = V.t. – C.t. – 0 + 0 = V.t. – C.t.

Income tax (Iz.pf.) is calculated by the application of the income tax rate (C.iz.pf.), of 16 %, on the taxable income (Pf.iz.).

Iz.pf. = C.iz.pf. x Pf.iz. = 16 % x Pf.iz.

Taxable income, entered at row 15, is calculated ***cumulative***, with the recovery of the fiscal loss, in the amount of 320 lei, from the first year of amortization.

In the first year:

– taxable income = – 2,000 lei → fiscal loss (Pd.fs.) = 2,000 lei.

– income tax = – 2,000 x 16 % = 0 lei taxable income x 16 % = 0 lei.

In the second year:

– taxable income from the first year + second year taxable year = –2,000 + 1,750 = – 250 lei → fiscal loss (Pd.fs.) = 250 lei. The fiscal loss, in the amount of 250 lei, does not come the fact that profit was not obtained in this year, but from the fact that the taxable income earned in the second year, in the amount of 1,750 lei, was not sufficient (of more than 2,000 lei) to cover fully the fiscal loss from the first year, i.e. 2,000 lei, a rather considerable loss cause by the application of accelerated amortization.

– income tax = – 250 x 16% = 0 lei taxable income x 16% = 0 lei.

In the third year:

– taxable income = taxable income from the first year + second year taxable year + third year taxable income = – 2,000 – 250 + 1,750 = 1,500 lei.

– income tax = 1,500 x 16% = 240 lei.

In the fourth year:

– taxable income = taxable income from the first year + second year taxable year + third year taxable income + fourth year taxable income = – 2,000 – 250 + 1,750 + 1,750 = 3,250 lei.

– income tax =3,250 x 16% = 520 lei.

In the fifth year:

– taxable income = taxable income from the first year + second year taxable year + third year taxable income + fourth year taxable income + fifth year taxable income = – 2,000 – 250 + 1,750 + 1,750 + 1,750 = 5,000 lei.

– income tax = 5,000 x 16 % = 800 lei.

The data in table no. 2 helps us with the following ***conclusions***:

1. In the case of linear amortization, income tax is 160 lei annually, respectively 160 lei per year: 12 months = 13.34 lei per month.

At the end of the 5 years of linear amortization, cumulative, the unit enter a taxable income of 5,000 lei and an income tax in the amount of 800 lei.

As we have said, in the case of linear amortization, which is the normal, regular situation, we cannot talk about deferred taxes.

In the case of ***accelerated*** amortization, the situation changes radically: in the first 2 years the unit goes from taxable income (calculated distinctly, per year), in the amount of 160 lei, from the first year, and in the amount of 160 lei, in the second year, to fiscal loss, in the amount of 320 lei, from the first year, and of 40 lei, in the second year.

Fiscal loss is also registered in the 3rd year, respectively on (360 – 320): 13.34 = 40 : 13.34 = 3 months.

It is only starting from the fourth month (April), in the third year that the unit start to appear with taxable income (fiscal).

At the end of the 5 years of accelerated amortization, the unit appears, cumulative, with the same taxable income, in the amount of 5,000 lei, and with the same income tax, 800 lei, like in the case of linear amortization.

The changes of the taxable income and of the income tax (distinct per year and cumulative, until the end) were only "in structure, only between years, not in total (at the end of the 5 years).

Table no. 2 was used as basis for the creation of ***table no. 3***, which shows clearly and accurately the meaning and the content of the notion of "deferred taxes".

The application of tax incentives granted under art. 24 para. (9) of the Tax Code, meaning the acceptance of amortization expenses deductible at the calculation of the taxable income, in the amount of 5,000 lei (in the case of accelerated amortization), instead of 2000 lei (in the case of the linear amortizations) led to a radical change in the unit's fiscal result, during the 5 years of amortization (= allowed service duration for amortization).

In the context of linear amortizations, the tax due is uniform each year, in the amount of ***160 lei per year***, respectively160 lei yearly: 12 months = ***13.34 lei per month***.

In the context of accelerated amortization, the unit reduced its tax burden and, furthermore, in the first year it entered a rather large ***fiscal loss***, ***of 320 lei***, equal with the income tax due in the first 2 years in the context of linear amortizations.

More precisely, in the first year the state budget sees a "taxation gap", a non-received tax in the amount of 160 lei, generated by the deliberate, aware acceptance of the granting of tax incentive [under art. 24 para. (9) of the Tax Code] sub forma accelerated amortization.

The tax loss, from the first year, is 320 lei.

This "tax gap" is only temporary, it is not final: the state accepted well ware, deliberately a "***deferral in the payment of the tax***", 160 lei, from the first year + 160 lei, from the second = 320 lei.

The state did not abandon definitively the tax loss, in the amount of 320 lei, registered in the first 2 years after the granting of the tax incentive in the form of accelerated amortization.

After the first year (when accelerated amortization was applied), uniformity is seen at the level of the amortization, an annual linear amortization, which leads to uniformity in the increase of the other indicators.

The situation is different in the level of the taxable income and, especially of the income tax, cumulative, because here we can note the influence of "the taxes deferred" in the first 2 years and 3 months.

For a better understanding of the issue, we have the example of a company for which the following situation was registered.

1 – Total income = 10,000 lei.

2 – The unit does not appear with non-taxable income.

3 – Total expenses, **without** amortization expenses = 47,000 lei.

4 – The unit does not appear with non-deductible expenses.

5 – Amortization expenses: are described in table no. 1.

6 – Income tax rate = 16%.

7 – Income tax is illustrated in table no. 2, both in the context of the application of linear amortization, and in the context of the application of accelerated amortization.

8 – Deferred payment taxes, generated by the granting of tax incentives in the form of accelerated amortization, according to art. 24 para. (15) of the Tax Code, are described in ***table no. 3***.

In the context of accelerated amortization, annual unrealized income tax, cumulative = annual deferred tax, as seen from table no. 3.

Annual deferred tax = annual tax, calculated cumulative, in the context of linear amortization – annual tax, calculated cumulative, in the context of accelerated amortization.

In the case of linear amortization, respectively of the absence of tax incentives, we cannot talk about deferred taxes.

Deferred taxes appear and exist only in the context of tax incentives.

Table no. 3

Deferred taxes

No.	Indicator		Year					Total
			1	2	3	4	5	
0	1		2	3	4	5	6	7
1	Tax cumulative, in the context of ***amortization:***	Linear	160	320	480	640	800	800
2		Accelerated	0	0	+240	+520	+800	800
3	Deferred income, in the context of ***amortization:***	Linear	0	0	0	0	0	0
4		Accelerated = l.1 – l.2	160 – 0 = 160	320 – 0 = 320	480 – 240 = 240	640 – 520 = 120	800 – 800 = 0	0

3. Conclusions

We list below the Fiscal and Accounting Regulations strictly required for consideration when we want to approach adequately the issues of:

1. Accounting amortization.
2. Fiscal amortization.
3. The impact of fixed asset revaluation on:
   3.1. The *accounting* and *fiscal* value of the amortizable fixed assets
   3.2. *Accounting* and *fiscal* amortizations.
   3.5. The taxable income and deferred taxes.

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