International Journal of Economics, Commerce and Management
United Kingdom Vol. IV, Issue 6, June 2016
http://ijecm.co.uk/ ISSN 2348 0386

THE ORIENTATION OF THE RELATIONSHIP BETWEEN ACCOUNTING AND TAXATION IN ALBANIA: THE INFLUENCES OF THE EUROPEAN ACCOUNTING REGULATIONS

Eriona Vadinaj
PhD Candidate, Department of Finance-Accounting
Faculty of Economy, University "LuigjGurakuqi", Shkodër, Albania
evadinaj@gmail.com

Abstract

The purpose of this paper is to explore the relationship between financial and tax regulations in Albania, under the spectrum of European regulations. This relationship is a highly debated issue in the international accounting and tax literature. Based on this assumption, it is important to analyze the orientation of this relationship according to different theories from different authors. To explore this relationship, it is important to give a short description of the development of accounting and taxation. As other developing countries, Albania has strengthened its accounting regulations as part of broader programs of the market-oriented regulatory reform. The taxation system is still in process and has been faced with many challenges that require more effectiveness and efficiency, led by the aspiration to be close to European Standards. This paper, under the spectrum of an analysis, aims to conduct the orientation of the relationship between accounting and taxation in Albania.

Keywords: Relationship, accounting, taxation, orientation, regulations

INTRODUCTION

Since the current trend of an integrated global economy, the accounting and taxation cannot be treated only in the main jurisdiction but they have become very important factors of a complex and dynamic world. Nowadays, the relationship between accounting and taxation is a highly debated issue in the international accounting and tax literature. Such relationship has existed, still exist and will further exist. Over the past two decades, a lot of papers and analysis has been conducted in order to capture the influences which exist between them.

Over the past two decades, as other developing countries, Albania has strengthened its accounting regulations as part of broader programs of the market-oriented regulatory reform. This paper aims to conduct the relationship between accounting and taxation in Albania.

LITERATURE REVIEW

Many studies have examined the relationship between accounting and taxation in last two decades. We can mention many of foreign authors, whose contribution is very valuable, such as Radebaugh and Gray (1993), Doupnik and Salter (1995), Labatut and Pardo (1995), Hoogendoorn (1996), Pierce (1996), Lamb et al. (1998), Blake (1997), Epstein and Mirza (2001), Richardson and Lanis (2001), Shackelford and Shevlin (2001), Choi, Frost and Meek (2002), Aisbitt (2002), Nobes and Parker (2002), Alley and James (2005), Berinde (2005), Desai (2005), Tzovas (2006), Gielen and Hegarty (2007), Shaviro (2009), Fekete et al (2009), Graham et al (2011), Cuzdriorean (2011), Partenie (2014).

This relationship is studied even by albanian authors such as Dhuci (2012), Kapllani and Duhanxhiu (2012), Bollano (2012-2013), Qurku (2013) andUjkani (2013). Many analyses and publications are realized supported by National Accounting Council.

Blake *et al.* (1997) analyzed the relationship between accounting and taxation in Sweden. The authors captured two approaches of the relationship: as a formal legal accounting system based on a binding tax-accounting link and as private-sector- standard-setting body seeking to break that link.

Hoogendoorn (1996) has developed a taxonomy regarding the relationship between accounting and taxation in major EU countries, exactly in 13 countries. He studied this taxonomy based in on factors of influence, realizing a limitation between countries included in the case of Anglo-Saxon System (disconnection), and European Continental System (connection). This taxonomy is presented as follows:

- Accounting and taxation are characterized as being dependent and this relationship is not expected to change.
- Accounting and taxation are dependent and this relationship is not expected to change.
- Accounting and taxation are still dependent, but the aim to break the relationship between them is desired.
- Accounting and taxation are formally independent; in practice the connection between them is very strong.
- Accounting and taxation are independent.

- Accounting and taxation are independent and there are also specific deferred taxation regulations.

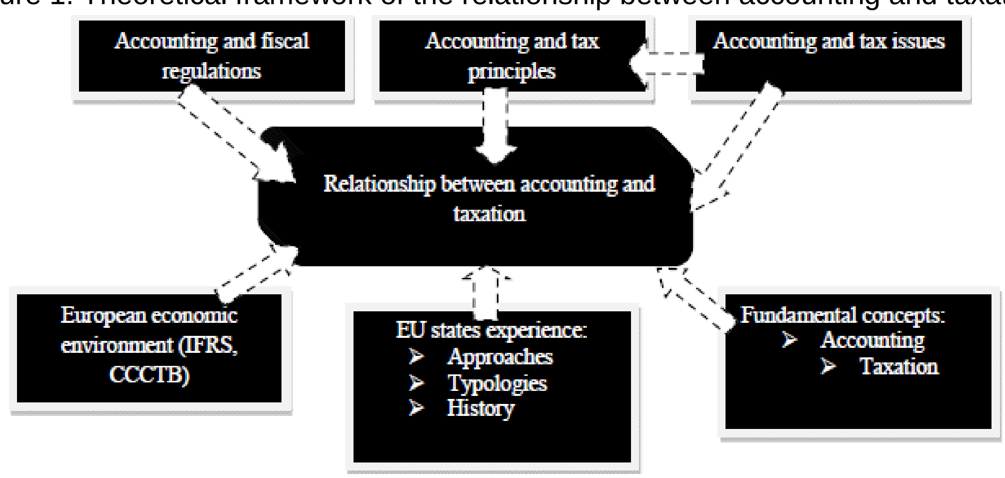
Lamb et al. (1998) have developed a classification of the relationship between accounting and taxation. This classification is based on five cases, presented as follows:

- *Case I - Disconnection:* Different tax and financial reporting rules
- *Case II - Identity:* There is identity between tax and financial reporting rules/regulations.
- *Case III - Accounting leads:* A financial/accounting rule is followed for financial reporting purposes, and even for tax purposes, perhaps because of the absence of a specific tax rule/regulation.
- *Case IV - Tax leads:* A tax rule/regulation is followed for tax purposes and even for financial purposes, perhaps because of absence of a specific financial/accounting rule.
- *Case V -Tax dominates:* A tax rule/regulation is followed for tax and financial/accounting reporting purposes, where there is a conflicting reporting rule.

Gallegro (2004), Nobes and Schwencke (2006) mentioned that this connection is characterized by complexity and dynamism. Given this connection, the implementation of IFRS in Europe generated a whole set of accounting standards examined by tax authorities and not only. A whole theoretical framework could be developed based on this fact.

One thing is certain, when this connection is addressed, the following factors have to be mentioned: accounting and fiscal regulations; accounting and tax concepts; the European economic environment under the IFRS and CCCTB influence; accounting and tax principles; the relationship between accounting and taxation based on the EU states experience (Cuzdriorean, D., Matis, D., 2012). The figure below suggests such a framework, for an integrated approach to the relationship between accounting and taxation.

Figure 1: Theoretical framework of the relationship between accounting and taxation



(Source: Cuzdriorean, 2012)

The implementation of IAS/IFRS in EU and their influences on the relationship between accounting-taxation

The introduction of the Fourth Directive represented a very important step towards the implementation of IAS/IFRS in EU. In countries such as Spain, the introduction of these standards brought changes in the relationship between accounting and taxation (Gallego, 1995) However, the adoption of IAS/IFRS has raised several questions and concerns, especially in inn evaluating the impact of taxation on accounting or accounting on taxation.

The connection between accounting and taxation is one of the main reasons that the implementation of IAS/IFRS has become a point of debate in EU based on legislative and cultural diversity. In this point, it is important to investigate and look over the two accounting systems: European-Continental (macro-oriented) and Anglo-Saxon(micro-oriented):

- The micro-orientation provides financial statements prepared especially for shareholders and not influenced by tax regulations.
- The macro-orientation is oriented especially for creditors and there is an influence of tax regulations over accounting.

The influence of taxation on the consolidated financial statements based on IFRS, is the subject of a study conducted by the authors Gee *et al.* (2010). These authors prepared a comparative analyze of Germany and UK. The two countries were chosen for analysis because they are often used as examples of two different accounting systems, therefore they are considered as the exemplars of the differences of the relationship between accounting and taxation in different countries. The results of analyze show that the influence of taxation in the consolidated financial statements in Germany has decreased, and this influence is also identical to the UK.

The Development of accounting and tax regulations

Over the two decades, as other developing countries, Albania has strengthened its accounting regulations, in order to be adopted and involved in the global market economy. Even the taxation system has changed a lot. This reform is still in process and has faced with many challenges that require more effectiveness and efficiency, led by the aspiration to be close to European standards. Fiscal issues and accounting objectives are different, in conceptual level as well as in optical level, as a regulatory structure that operates in any jurisdiction and that depends on local circumstances. Accounting rules and tax rules are two concepts that are drafted by two different authorities, which have two different purposes.

Based on the taxonomy of Lamb (1998), in Albania the accounting and fiscal regulation are dependent. These regulations (fiscal and financial) are drafting from the same structure: the

Ministry of Finance. The relationship between tax and accounting is strong but taxation dominates most of the cases. Therefore, based on Lamb theory, our country is categorized at the fifth category: *Tax dominates.* It means that the tax rule/regulation is followed for tax and financial/accounting reporting purposes, where there is a conflicting reporting rule.

The Development of accounting regulations in Albania

After the 90s, in order to be involved in a democratic and free market, the Albanian society has had its own oscillations trying to search for the best opportunities. The international experiences, especially the Italian, Soviet and recent decades it mainly French and European mainland are considered valuable during the long historical path accounting development and modernization. These experiences have been adopted into the Albanian economy. Albania, during the transition period towards a market economy, successfully managed to implement a number of important elements of the institutional and legal framework of the financial reporting. However, our country should take further steps in order to achieve its goals for a strong reporting framework created specifically to fulfill the needs of our economy and to converge with "acquiscommunautaire" and international standards and practices.

At the beginning of the second decade, the internationalization of Albanian business activity presented the necessity to develop the accounting regulations. The new accounting law (nr. 9228, date 29.04.2004) has the objective to improve the quality of financial reporting in Albania. This law aims to fulfill the gaps inherited from the previous accounting and financial reporting. Accounting requirements in previous accounting law, the General Plan of Accounting and the Banks Accounting Manual, do not provide a good financial reporting quality for entities with public interest, therefore the users hesitated to make economic decisions. The new Accounting Law, as an organic law for accounting and financial statements, introduced the spirit of accounting standards, making it more efficient and flexible. It is simple, concise and modern, which appear only in fundamental and necessary regulations in accounting/financial statements.

From the first of January 2008, in Albania are made effective 15 National Accounting Standards, which are applied by all entities private and public, in compliance with IFRSs. Shortly, the new law presents an increasing of harmonization of the Albanian legislation with EU regulations. The correct presentation and implementation of National Accounting Standards, updated according with the IFRS, will lead to a significant improvement of the quality and purposes of financial reporting in public and private entities. This will give the possibility to improve decision making, management efficiency and of course will increase transparency and reduce the informality.

The development of tax regulations in Albania

Albania operates under the system "code law," which means a country where accounting and financial standards are regulated by law, for fiscal issues. Tax legislation consists of a package of laws, regulations, guidelines and tax agreements (according to taxes), manners and procedures of establishment these taxes, procedures for collecting taxes, as well as the methods of tax control.

The tax legislation contains rules on how financial reporting should be done for fiscal issues, which are applied by entities as well as by the tax authorities.

The main objective of the tax reform was the adoption of the tax practices from the developed countries based in two topics: the introduction of tax legislation and the creation of tax authorities. This project was drafted by the Ministry of Finance in collaboration with International Monetary Fund. The most important and fundamental laws of taxation are as follows:

- *Law nr.7758, date 12.10.1993 "Documenting and keeping tax accounts";*
- *Law nr.9920, date 19.05.2008 "On Tax Procedures in Republic of Albania" (this law was drafted with support of international experts);*
- *Law nr.8438, date 28.12.1998 "On Tax Income".*

During these two decades of democracy and free market, the implementation of further changes, aimed to establish a favorable macroeconomic development, sustainable economic growth and creating a good, fair and transparent relationship between business and fiscal authorities.

Beside the introduction of electronic filling and the assessment of the anticorruption structures, the main objective of these huge changes was to simplify, specify and clarify many practices, uncertainties and questions pointed out from the Law "On Entrepreneurs and Companies".

CONCLUSIONS

During the last two decades, tax regulations and accounting regulations in Albania have made huge changes due to internal and external, national and international pressures. In summary, all mentioned above can be emphasized into four important conclusions:

- The connection between accounting and taxation is one of the main reasons that the implementation of IAS/IFRS has become a point of debate in EU based on legislative and cultural diversity.
- Over the two decades, European regulations have given their impact on accounting and taxation in Albania, in order to be close to European standards. Albania, as other

developing countries, has strengthened its accounting regulations, in order to be adopted and involved in the global market economy. The reform on taxation is still in process and has faced with many challenges that require more effectiveness and efficiency, led by the aspiration to be close to European standards.

- Fiscal issues and accounting objectives are different, in conceptual level as well as in optical level, as a regulatory structure that operates in any jurisdiction and that depends on local circumstances. Accounting rules and tax rules are two concepts that are drafted by two different authorities, which have two different purposes.
- Based on the taxonomy of Lamb (1998), in Albania the accounting and fiscal regulation are dependent. The relationship between tax and accounting is strong but taxation dominates most of the cases. Therefore, our country is categorized at the fifth category: *Tax dominates.* A tax rule/regulation is followed for tax and financial/accounting reporting purposes, where there is a conflicting reporting rule.

REFERENCES

Alley, C. and James, S. (2005). "The interface between financial accounting and tax accounting: a summary of current research", Working Paper Series, no.84, University of Waikato, NZ.

Blake, J., Amat, O., Fortes, H. (1993)."The Relationship between Tax Regulations and Financial Accounting: a comparison of Germany, Spain and the United Kingdom", Economic Working Paper, 46, UniversitadPompeuFabra, Barcelona, available at: http://www.econ.upf.edu/docs /papers/downloads/46.pdf

Blake, J., Amat, O., Gowthorpe, C., Pilkington, C. (1998) "International accounting harmonization", European Business Review, vol. 98, pp. 144–150

Bollano, J. (2010). "Albania through implementation of financial reporting and auditing standards", Proceedings of International Scientific Conference of NAC of Albania

Cela,H. (2004)."Towards application of new standards on accounting and auditing – Albanian challenge on implementing IAS/IFRSs and ISAs", Albanian Institute of Authorized Chartered Auditors.

Cuzdriorean, D. (2012). "The relationship between accounting and taxation insight the European Union: The influence of the international accounting regulation", Working Paper, AnnalesUniversitatisApulensis, Series Oeconomica.

Freedman, J. (2008)."Financial and tax accounting: transparency and truth", University of Oxford Faculty of Law Legal Studies Research Paper Series, Working Paper No 2.

Gielen, F., and Hegarty, J. (2007)."An accounting and taxation conundrum: a pan european perspective on tax accounting implications of IFRS adoption", Paper prepared for the World Bank Centre for Financial Reporting Reform, Vienna, Austria.

Lamb, M., Nobes, C., Roberts, A.(1998)."International Variations in the Connections Between Tax and Financial Reporting", Accounting and Business Research, vol. 28, no. 3, pp. 173-188

Official journal of the Republic of Albania (1992-2011). Edition of the Official Publications Centre[available at http://www.ligjet.org/].

Nobes, C. (2003)."A conceptual framework for the taxable income of businesses and how to apply it under the IFRS", ACCA, London.

