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“Revenue and expense recognition under IFRS and compare its with tax accounting”

THEME

MASTER THESIS

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BAKU - 2020

Elm andı

I Rüfət Baxşaliyev swear that I have written my master's dissertation on "Revenue and expense recognition under IFRS and compare its with tax accounting" in full compliance with scientific ethics and rules of reference and reflecting all the sources I use in the bibliography.

“MHBS-A ƏSASƏN GƏLİR VƏ XƏRCLƏRİN TANINMASI VƏ VERGİ UÇOTU İLƏ MÜQAYİSƏ EDİLMƏSİ”

XÜLASƏ

Tədqiqatın aktuallığı: Vergi uçotu nəticələri ilə maliyyə hesabatlarının nəticələri arasındakı fərqi anlamaq üçün vergi uçotu və maliyyə hesabatları haqqında hərtərəfli bir fikir əldə etmək lazımdır. Maliyyə hesabatı, maraqlı tərəflərin əksəriyyəti tərəfindən müxtəlif məqsədlər üçün müxtəlif məlumatlar əldə etmək üçün ən çox istifadə olunur.

Tədqiqatın məqsədi: Tədqiqatın məqsədi BMHS-a uyğun olaraq gəlirlərin tanınmasını təhlil etmək və onu Azərbaycanda vergi uçotu ilə müqayisə etməkdir.

müqayisə etmək və əks etdirmək üçün müxtəlif sintez metodlarından istifadə edilmişdir. Sintez metodu şərti sintez, kvalifikasiya sintezi, kəmiyyət sintezi və inkişaf etməkdə olan sintez kimi tiplərə bölünə bilər.

İstifadə olunmuş tədqiqat metodları: Tədqiqatın metodoloji əsasını ətraf fəaliyyətin ümumi elmi metodları tərtib etmişdir. İnformasiyanın işlənməsi və təhlili zamanı elmi biliklərin aşağıdakı metodlarından istifadə edilmişdir: analitik, qrafik, iqtisadi-statistik və s.

Tədqiqatın informasiya bazası: Tədqiqatın informasiya bazası istifadə olunan məlumatlar müxtəlif akademik jurnallardan, kitablardan və onlayn mənbələrdən götürülmüş və bu məlumatlar tədqiqatın məqsədlərinə cavab vermək üçün istifadə edilmişdir.

Tədqiqatın məhdudiyyətləri: Milli şirkətlərlə əlaqədar mövzuda mühasibat məlumatları məhduddur.

Nəticələrin elmi-praktik əhəmiyyəti: Nəticələr praktiki əhəmiyyəti ondan ibarətdir ki, araşdırmanın nəticələri gəlirlərin tanınmasını daha yaxşı başa düşmək üçün yerli müəssisələr tərəfindən tətbiq oluna bilər. Bu da öz növbəsində vergi qaydalarına uyğun olmağa imkan verir və eyni zamanda vergi sistemi kimi qaydalara əsaslanan sistemin çox sərt quruluşundan əziyyət çəkmək üçün BMHS prinsiplərinə əsaslanan yanaşmanı tətbiq edir.

Nəticələrin istafadə oluna biləcəyi sahələr: Azərbaycan şirkətlərinin vergi qaydaları və maliyyə hesabat sistemi haqqında gəlirlərə necə münasibət göstərməsi ilə bağlı mövzuda çox az məlumat olduğu üçün bu araşdırma dəyərli fikirlər əlavə edəcəkdir.

Açar sözlər: vergi, mühasibat, beynəlxalq standartlar, maliyyə, hesabat

“REVENUE AND EXPENSE RECOGNITION UNDER IFRS AND COMPARE ITS WITH TAX ACCOUNTING”

SUMMARY

The actuality of the subject: To understand the difference between tax accounting results and financial statement results, it is necessary to obtain a comprehensive understanding of tax accounting and financial reporting. Financial statements are most commonly used by the majority of stakeholders to obtain different information for different purposes. However, this information is not the only source of information used by stakeholders. The government, for example, cites the results of tax accounting as an important stakeholder and bases its decisions on these results for tax authorities.

Purpose and tasks of the research: The purpose of the study is to analyze the recognition of income in accordance with IFRS and compare it with tax accounting in Azerbaijan.

Various synthesis methods have been used to compare and contrast. The synthesis method can be divided into types such as conditional synthesis, qualitative synthesis, quantitative synthesis and evolving synthesis.

Used research methods: The methodological basis of the research was compiled by general scientific methods of environmental activity. The following methods of scientific knowledge were used during the processing and analysis of information: analytical, graphical, economic-statistical, etc.

The information base of the research: The information used in the research database was taken from various academic journals, books and online sources, and this information was used to meet the objectives of the research.

Restrictions of research: Accounting information on national companies is limited.

The novelty and practical results of investigation: The practical significance of the findings is that the findings of the study can be applied by local businesses to better understand revenue recognition. This, in turn, allows for compliance with tax rules and, at the same time, an approach based on IFRS principles to suffer from the very rigid structure of a system based on rules, such as the tax system.

Scientific-practical significance of results: This study will add valuable insights, as there is little information on how Azerbaijani companies view revenues on tax rules and financial reporting systems.

Keywords: taxes, accounting, international standards, finance, reporting

LIST OF ACRONYMS

AAS	Azerbaijan Accounting System
CGT	Consolidated Groups of Taxpayers
FA	Fixed Assets
GAAP	Generally Accepted Accounting Principles
IAS	International Accounting Standards
IFRS	International Financial Reporting Standards
IT	Income Tax
NFRS	National Financial Reporting Standard
SOCAR	State Oil Company of the Republic of Azerbaijan

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INTRODUCTION

Actuality of the subject: In order to understand the divergence between tax accounting outcomes and financial reporting results, it is essential to gain a comprehensive understanding of tax accounting and financial reporting.

Financial reporting is the most frequently used by the majority of stakeholders to obtain a variety of information for different uses. However, this information is not the only source of information that is used by stakeholders. The government as an important stakeholder, for example, also refers tax accounting results and bases its decisions on these outcomes for taxing businesses.

Despite these differences, there is very little understanding of the differences between tax accounting and financial reporting recognition of revenue and expenses among the public due to several reasons. As tax rules were developed in isolation from many innovations in finance and accounting, the differences between two separate systems with regards to the treatment of revenue and expenses tend to be high.

The topic is actual in Azerbaijan, in particular, because Azerbaijani companies have not been studied in this regard by many researchers. Only general analysis of the differences between tax rules and financial reporting rules has been provided in the literature. However, this is not enough to understand the core principles in an-depth analytical way which makes this research valuable.

The degree of elaboration of the problem: Previously, it was mentioned that there is very little understanding of the divergence in the treatment of revenue and expenses between tax authorities and financial reporting. The studies in this area can be grouped under few categories.

Firstly, books touch on the differences of both systems and how they treat revenue recognition. Secondly, academic journals and reports have published articles that elaborates on the differences between the recognition of revenue and expenses

under tax system rules and IFRS. However, Azerbaijan is not among these examples and therefore, the selection of the country as an example case serves a useful purpose.

Purpose and tasks of the research: The purpose of the study is to analyze revenue recognition under IFRS and compare it to tax accounting in Azerbaijan.

There are several objectives of the study that arise from the purpose of the study. These objectives can be summarized below.

- To provide an in-depth review of the treatment of revenue recognition under IFRS in Azerbaijan
- To provide an in-depth review of the treatment of tax accounting in Azerbaijan
- To compare IFRS and tax accounting recognition of revenues in Azerbaijan.

Object and subject of research: The object of the study are various big businesses in Azerbaijan. The subject of the study, on the other hand, is the theory and principles of tax accounting and financial reporting.

Research methods: Various synthesis methods will be used in order to compare and contrast IFRS recognition of revenue and expenses and Tax Accounting. Synthesis method can be broken down into such types as conventional synthesis, qualitatie synthesis, quantiative synthesis and emerging synthesis. Application of these methods will enable to gain a deep undersdanding of differences and similarities between IFRS and tax Comparative analysis is another method which will be used in this study. This method compares two or more concepts or phenomena in order to discover their similarities and differences. Therefore, this method is deemed relevant for this research project as well and will be applied to compare IFRS and tax accounting regarding their simialrities and differences on the recognition of revenue and expenses.

Research information base: The information used for the study will be taken from various academic journals, books and online resources and this information has been used in meeting the objectives of the research.

Research limitations: The accounting information on the topic regarding national companies is limited.

Scientific-practical results obtained as a result of research: As there is very little information on the subject with respect to how Azerbaijani companies treat revenue under tax rules and financial reporting system, this research will add valuable insights.

Scientific and practical significance of results: The practical significance of the study is that the findings of the research can be applied by local businesses to understand the treatment of revenue recognition better. This will in turn, enable them to be in compliance with tax rules at the same time applying principles-based approach of IFRS in order to suffer from too rigid structure of a rules-based system such as tax system.

I CHAPTER. THEORETICAL REVIEW OF IFRS AND TAX ACCOUNTING

1.1. Basic principles of IFRS

The adoption of IFRS served to create a set of principles that would enable firms all across the world to have a uniform set of standards. Previously to the adoption of IFRS as a basis of accounting in many countries, GAAP (Generally Accepted Accounting Principles) had been used separately for each country in order to guide the preparation of financial reports (Diri M. E.,, 2018: p.21).

Thus, cross-border transactions and the fact that more and more businesses expand abroad to engage in international transactions increased a need for IFRS. Therefore, IFRS provided several benefits as a result. One of them is transparency. Transparency was enhanced as a result of the acceptance of IFRS because a uniform set of standards allowed to have comparable standards which in turn, increased the transparency.

Additionally, accountability was also improved because of the fact that IFRS reduced information gap existing between the providers of capital and their agents meaning that agency problem was ameliorated to some extent.

Furthermore, efficiency of investments for investors has improved as well. Firms that adopted IFRS received higher confidence from investors globally owing to the fact that their financial reports were more trustworthy. This, in turn, increased the efficiency of capital allocation (Cordes J., 2005: p.65).

The Conceptual Framework of IFRS

The Conceptual Framework of IFRS serves as a guidance to the Board engaged in the development of financial reporting standards. This framework sets out the most fundamental principles of financial reporting. The overarching objective of the framework is to ensure consistency and comparability of financial reports of companies so that investors and other stakeholders can have a better overview of the

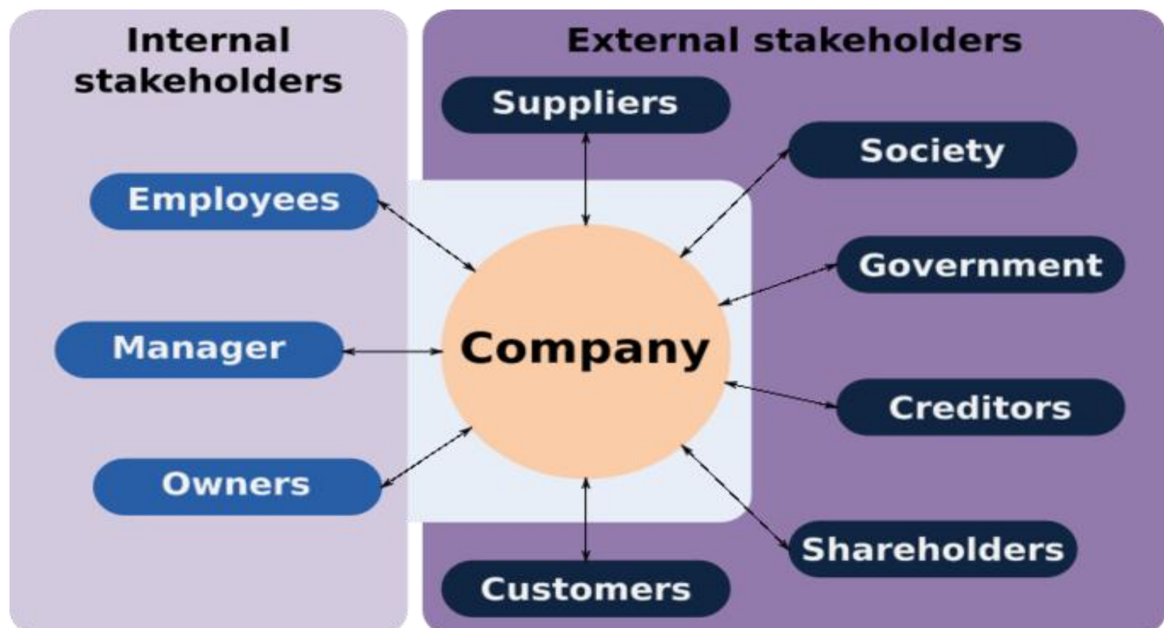
condition and performance of the firm so that they can make more informed decisions.

Status and purpose of conceptual framework of IFRS are to help IFRS Board in preparing financial standards that will help to converge accounting standards around the world. There are many areas in accounting that companies have some choice and in order to eliminate the cases of a misunderstanding and divergence among different businesses, IFRS Conceptual framework gives recommendations on applying a uniform set of policies whenever possible.

Purposes of general financial reporting

The purpose of IFRS is to provide financial information on business entities to a wide range of users who are in need of these reports. For example, stakeholders of the business include such diverse groups as investors, creditors, suppliers, general public and the government and each of these groups have a different information need that are served by financial reporting (Bragg S. M., 2010: p.21).

Diagram 1: Stakeholders of a business who need financial information



Source: Bragg, S. M., (2010). Wiley Revenue Recognition: Rules and Scenarios. London: Wiley.

Qualitative characteristics of useful financial information

Qualitative characteristics of useful financial information that IFRS seeks to present to users of financial reports can be divided into two groups which are fundamental qualitative characteristics and enhancing qualitative characteristics

Fundamental qualitative characteristics

Fundamental qualitative characteristics are relevance and faithful representation.

Relevance

Relevance is one of the most fundamental category that measures the quality of financial information. Accounting information must be relevant in order to make a difference in the decision-making process. If information is not relevant to the users of financial reports, then it is not useful. Therefore, IFRS intends to promote the usage of only relevant information in the accounting reports.

Faithful representation

Faithful representation is another key principle in accounting and this concept assesses whether a business represents its financial condition and performance in a realistic and true way. This concept should encompass all activities of a business such as operational results, financial performance, financial condition, cash flows and so on. Faithful representation can be measured based on the assessment of the three sub-categories:

- Completeness

Completeness is the condition where all useful information for the decision-making of a particular user is present in the provided information. If certain parts of information are omitted that create an incomplete situation and does not allow to evaluate the financial condition, performance or cash flow conditions of the firm, it can be said that the information is not complete for some reason (Bryman, A., Bell, E. A. & Teevan, J., 2012: p.74). Sometimes, incomplete information is provided by the firm in order to mask certain aspects of its business which it intends to hide from the users of financial reports. Therefore, the completeness plays an important role in the provision of financial information in a faithful manner.

- Error-free

Furthermore, information provided must be fair meaning that there should not be errors in the information that might materially affect the quality of information provided. Some errors might result in a biased view of the financial condition of the organization and create a misleading picture for investors.

- Unbiased

Finally, in order to be faithfully represented, accounting information must be free of biases as well. Biases might mean that the preparers of financial reports sometimes intend to present the condition or performance of the firm in a particular way and they can engage in certain practices so that the firm looks more or less attractive. For instance, it is frequent that many businesses crunch their numbers to look attractive for investors or creditors and they might change accounting assumptions in order to look this way which in some cases amounts to manipulation. In other cases, firms might need to show less profit in order to avoid taxes which is another case of a biased representation.

In summary, unbiased information is of high value as without unbiased information, it is impossible for users of financial reports to assess the true condition of the business.

In general, completeness, error-free nature as well as unbiasedness are the main features of faithfully represented information for the users of financial reports.

Enhancing qualitative characteristics

Enhancing qualitative characteristics increase the utility of financial information and therefore, they constitute the foundation of accounting information as well. These characteristics are comparability, verifiability, timeliness and understandability.

Comparability

Comparability is one of the founding principles of IFRS and this principle serves to create more comparable accounting information across the world so that investors are not restricted to invest only domestically. Indeed, when financial information is

comparable, it is easier for the users of reports to compare the results of businesses from different locations and make more informed decisions (Diri M. E., 2013: p.36).

Verifiability

Verifiability is yet another key concept and it states that it should be possible for an objective third party to generate the same financial accounting information given the facts of the business. If there is a divergence in the interpretation of financial information, then the reliability of the information is low and it cannot be accepted as a useful source of information for the business.

Timeliness

Timeliness of information is yet another key concept and it is of high value for the users of financial reports. When information provided is timely, it means it is provided at the right time to inform the decision-making process of the users of financial information. Otherwise, the information is not useful if it is not presented in due time.

Understandability

Despite the fact the users of financial information are deemed to be reasonably well-versed in understanding financial information, IFRS suggests that accounting information should be presented in an easily comprehensible way so that relatively less sophisticated users of accounting information can grasp its content.

Financial statements

Based on the principles that have been discussed up to now, several financial statements have been deemed as useful in terms of summarizing all the useful accounting information needed for the users of financial reports.

It should be highlighted that some users of accounting information, such as managers can access proprietary information or information that are only accessible to the internal users. However, in general, the focus of financial reporting is on publicly available information. Therefore, the following financial statements are deemed as the most important and they are the most frequently used:

- Income Statement/Statement of comprehensive income
- Balance Sheet
- Cash Flow Statement
- Statement of changes in shareholders' equity

Income statement presents the performance of a business for a particular period of time and the most crucial aspects of business such as profitability, revenue and expenses of the firm can be gleaned from this statement.

Balance Sheet, on the other hand, presents a snapshot of the current situation of the business with regards to assets, equity and liabilities. The key balance sheet equation is that the total assets must equal to the sum of liabilities and equity which means that the business finances its total assets with either debt or equity (Christian, D., and Ludenbach N., 2013: p.214). Together with income statement, balance sheet presents an overview of the key aspects of the business and can be used to measure its performance.

Cash flow statement, on the other hand, presents the changes in the cash flows of the business due to the fact that income statement and balance sheet take non-cash items into consideration as well which make their interpretation considerably challenging if the users want to assess the cash flow standing of the firm.

Comprehensive income, in turn, presents total income that are composed of both the income shown in the income statement as well as those income items that are not presented in Income Statement such as changes in the market value of certain assets and liabilities.

Statement of changes in shareholders' equity is yet another useful statement and demonstrates how various segments of equity capital have changed over the period of the time under study.

1.2. Principles of tax accounting

Tax systems vary in each country which creates a divergence in the treatment of this item on the financial reports of businesses. Taxes have a different purpose than financial reporting. Whereas financial reporting serves to provide useful and relevant information to the users of financial reports, taxes are used by the government for such purposes as boosting employment, economic growth and equilibrium.

Main objective of the tax systems are to enhance economic stability, allocate resources efficiently, contribute to economic growth and a fair distribution of wealth. These objectives make tax accounting different from financial accounting. Respective supervisory body in every country is responsible for tax policy.

In order to understanding taxes well, principles of taxation must be reviewed first.

There are several principles that guide a taxation process. One of these principles are legality.

Legality

Legality principle states that taxes are not enforceable without the relevant law that establishes them. Thus, without a law there are no taxes.

Equality or equity

This principle states that all taxable persons must be treated on an equal footing which means that tax authorities must not commit discrimination in terms of such factors as race, gender, religion and so on. Hence, if similar are conditions are present, then all subjects of tax laws must be treated equally without discrimination.

Neutrality

Neutrality is another principle of taxation which argues for a neutral impact of taxes. This means that taxes must be levied in such a way that they have little interference in the natural functioning of the markets. Therefore, taxes have been one of the most debated issues in terms of their effect on the functioning of free markets. Taxes create a deadweight loss which reduces efficiency. However, taxes are a useful

means for the government to achieve such conditions as equality and fair allocation of resources which are achieved at the expense of efficiency.

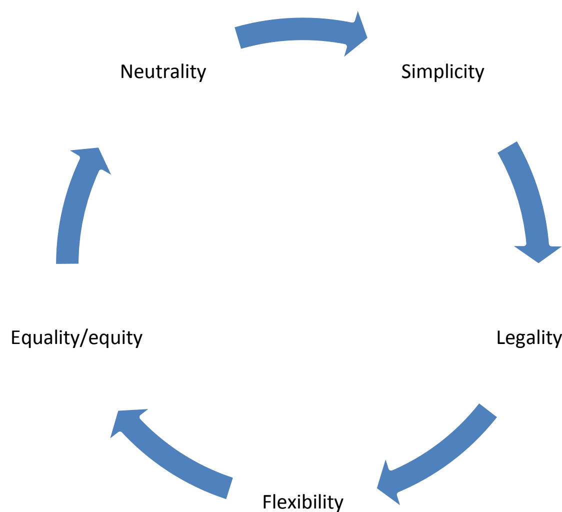
Simplicity

Tax system must also be simple meaning that complying with tax system rules and regulations must not create a heavy cost for tax subjects.

Flexibility

Tax system must also be flexible in order to operate effectively and efficiently by the government. To demonstrate, the needs of the government might differ and therefore, it might choose to change taxes from time to time to meet various economic objectives. Taxation therefore must be flexible enough so that the government uses it effectively and efficiently.

Diagram 2: Principles of taxation



Source: Epstein, B. J. & Jermakowitch, E. K., (2008). IFRS Policies and Procedures. London: Wiley.

Tax accounting differs from accounting for general reporting purposes. Therefore, tax amount reported to tax authorities and taxes reported on the financial statements differ.

There are two types of differences between the amount of tax on financial statements and amount of tax reported to tax authorities. These two differences are grouped under temporary and permanent differences.

Temporary differences

Temporary differences occur when the carrying amount of asset or liabilities are different on the books of the company and for tax purposes. These differences reflect themselves on the statements as temporary differences which later converge.

Permanent differences

However, some differences might persist and even be permanent owing to the fact that treatment of some income and expense items are different under two bases (accounting and tax).

Deferred taxes accounting methods

Deferred taxes can be treated differently in accordance with the method selected.

Deferred tax accounting method

In this method, when temporary differences originated, the deferred income tax amount is based on the tax rates in effect. The deferred form is a strategy based on income statement.

Asset-liability method

Deferred income tax sums are based on the expected tax rates for the periods in which the temporary discrepancies change in the asset-liability process. It is an approach based on a balance-sheet approach.

Loss carry backs

Loss carryback is an accounting term that describes a case where a company has net operating loss and decides to add the loss to the tax return of a previous year.

This resulted in a lower tax bill for the year this "carried over" loss was applied to as it reduces the tax liabilities for the previous year. Thanks to this newly reduced tax obligation, the loss carryback will create a tax refund for the company for the previous year.

Loss carrybacks are similar to loss carryforward, with the exception of firms transferring their net operating losses to results from previous years rather than subsequent years. A loss carryback can only be extended to the two years preceding the year the net operating loss occurred, unless certain conditions are present.

It will be as if the corporation overpaid its taxes for that year after the carry back loss is applied. Usually, just two years before the year in which the net operating loss occurred can be carried back losses. Special circumstances make it possible to endure a three-year deficit.

Loss carry forwards

Loss carryforward refers to an accounting strategy that adds the net operating loss of the current year (NOL) to the net income for future years to reduce tax liability

For example, if a business experiences negative net operating income (NOI) in year one but positive NOI in subsequent years, it may reduce the amount of future profits it records using NOL carryforward to record some or all of the first year loss in subsequent years.

For good NOI years, it results in lower taxable income and reduces the amount that the company owes the government in taxes. Carryforward loss can also apply to carry forward a capital loss.

1.3. Revenue and expense recognition under IFRS and how recognition is related to tax accounting

There are certain differences in the treatment of revenue and expenses under IFRS and tax accounting. These differences are related to the differences in the objectives of the two systems (financial reporting and tax accounting).

One of the main things that has to be noted is that financial reporting recognition of revenue and expenses should be viewed as a principles-based approach. IFRS promotes a principles-based approach as this approach is a better suited to meet the needs of a wide range of users who have different objectives and realities. There cannot be precise rules that can be enforced to all companies. Therefore, principles-based approaches are a better reflection of the financial condition and performance of a wide range of businesses. For this reason, IFRS bases new standards on principles rather than rules.

The use of judgment is an essential element of IFRS and financial reporting GAAPs. Businesses use a variety of judgments in preparing their reports. For example, the useful life of long-lived assets is one of these judgments that companies apply and these useful life assumptions might be different based on the reality of different companies. Therefore, it can be expected that applying a subjective judgment is an important part of financial reporting.

Taxes, on the contrary, are based on rules which means that all businesses must adhere to pre-determined set of rules by tax authorities.

Diagram 3: Financial reporting vs tax reporting

Source: Diri, M. E., (2018). Introduction to Earnings Management. Cham: Springer.

It is recommended by experts that accounting rules or taxes determined for financial reporting purposes under IFRS should be taken as a basis for the application of tax rules as well.

Historically, tax rules have been developed in relative isolation from accounting principles which resulted in a wider divergence of the two systems in regards to how

they treat taxes. Therefore, it is advised that financial reporting based financial information is taken as a basis for the preparation of tax rules as well (Diri, M. E.,, 2013: p.85). Upon the calculation of deferred taxes based on financial reporting information, it is then recommended that this information is fed into the creation of effective and efficient tax systems.

According to IFRS, as accounting documents the impact of income tax, they will represent the financial statements ' current and future fiscal consequences.

As we budget for the income tax due each year (also known as "current tax"), the current tax implications are expressed.

On the other hand, deferred tax registration represents the potential fiscal implica tions.

Deferred taxes can be of two types which are:

- Deferred tax assets;
- Deferred tax liabilities.

Deferred tax assets

In general, a deferred tax asset represents a tax deduction in future fiscal years (through tax conciliation), a result of the recovery of an asset or the liquidation of a liability.

To explain the functionality of the deferred tax assets, and how they allows full compliance with IFRS and tax regulations simultaneously, let us consider a practical example.

The account “loss due to deterioration of inventory value” is an expense account in the income statement; and the account “accumulated deterioration of inventory value” is a corrective asset account (valuation account). In this way, the users of the financial statements obtain reliable and timely information, useful for the economic decision-making (https://www.iasplus.com/en/standards).

However, if, for example, the country's tax legislation establishes that this accou nting expenditure (corresponding to a partial deterioration of the inventory's value) is

not deductible for income tax purposes, but until such time as such deteriorated invent ory is sold or self-consumed.

We have noted that deferred taxes arise from the differences in the financial and tax treatment of the same economic transaction. In the particular case of deferred tax assets, these may be generated mainly by the fact that in the application of IFRS there are certain accounting expenses (or losses) that are the product of estimates based on principles (use of professional judgement and the best information available), as was the recent example of the impairment loss of the inventory value. Because it is an estimate (although it may be accurate or very good), a tax regulation could consider such expenditure or loss as non-deductible from the income tax so far-and to the extent that such estimates are end up becoming the reality (that is to say, when the facts become accomplished).

Another situation that may generate a deferred tax asset (i.e., a right to future tax deduction) is the fact that under IFRS there may be an accounting record of an expense (or a loss) without necessarily having a related countable income.

Table 1: Main causes of the existence of deferred assets

Assets currently registered that will generate income taxed in the future but no deductible expenses.
Countable income currently registered (accrued) that will be taxed in the future when they match the tax definition of income.

Source: Cordes, J., Ebel, R. D. & Gravelle, J., (2005). The Encyclopedia of Taxation & Tax Policy. London: The Urban Insitute.

Deferred tax liabilities

In general, a deferred tax asset represents a tax deduction in future fiscal years (through tax reconciliation), resulting from the recovery of an asset or the liquidation of a liability. We have indicated that deferred taxes arise from the differences between the financial and the tax treatment of the same economic transaction. In the particular

case of deferred tax liabilities, these may be generated mainly by the fact that in the application of IFRS there are certain countable income (or earnings) that do not constitute an income for tax purposes, as was the case from the recent example of measuring the biological assets at their "fair value minus sales costs".

This type of countable income could be taxed for tax purposes in another fiscal period; For example, when the related asset is sold. This will generate a taxable temporary difference (i.e., a value to be added later in the tax conciliation), and consequently, a deferred tax liability.

II CHAPTER. CRITICAL COMPARISON OF IFRS AND TAX ACCOUNTING

2.1. Divergences between IFRS and tax accounting regarding revenue and expense recognition

Today, consolidated financial statements compiled in accordance with IFRS are no longer rare and an increasing number of domestic companies wishing to attract foreign investors are becoming confident users of reporting transformation tools.

Despite a well-developed transformation algorithm, domestic firms still encounter difficulties directly related to the interpretation of the provisions of international standards (IFRS).

Problems arise in a wide variety of topics. Nevertheless, we would like to focus on the problems of accounting for income tax (here in after referred to as NNP), which raise serious questions in the reporting process.

In order to timely identify and correctly reflect key transactions related to obligations under income tax (IT), you need to clearly understand the requirements of international reporting requirements, and the distinguishing features that are found in comparison with local rules.

We give an interpretation reflecting the provisions of Azerbaijan generally accepted accounting principles in relation to this issue. Temporary differences are income / expenses recorded in profit for accounting and tax purposes in different periods. At the same time, the latest edition of IFRS indicates that temporary differences arise due to the difference in the carrying amount of the asset / liability and the tax value of this asset / liability.

It is worth explaining that this discrepancy in definitions does not bring with it differences in the results of the calculation of deferred taxes, since these methods do not conflict: if they are used correctly, the same results will be obtained.

Nevertheless, the profit and loss ratio method is considered less effective in comparison with the balance sheet. This is due to the fact that it does not make it possible to timely monitor all the temporary differences that appear during the course of the company's economic activity.

The most obvious example for our purposes is a positive revaluation of fixed assets, not affecting the company's profits, but attributable directly to changes in the amount of capital. As a result of such a revaluation in accounting, the amount of depreciation deductions will change, the expense will increase, which will not happen in tax accounting. In the end, the company will pay tax calculated on a larger income than it actually has. It will not be possible to identify the difference between accounting and tax accounting that appears during the revaluation process using the profit and loss method, which consists in comparing income and expenses.

The balance method enables these changes to be recorded at a time directly during the execution of the operation. Returning to the example of the revaluation of non-current assets, the use of the income statement method in this case leads to the identification of differences at the time of depreciation (i.e. on a monthly basis), while the balance sheet is often formed once a year. Thus, the SDA method splits the resulting difference into several parts, increasing the number of operations to account for these differences and, as a result, increasing the probability of errors in collecting data for annual reporting.

We must say that in national standards any increase / decrease in the amount of deferred taxes is shown exclusively in the FIU, and international rules recommend deferred taxes in the same part of the reporting, which reflects the reason for their occurrence. In the end, deferred tax will be reflected in the financial result, other comprehensive income or in equity (Водолазко Н. С., Трунина В. Ф., 2015).

According to Azerbaijan law, permanent differences are recognized as income / expenses that are included in accounting profit, but not taken into account in

calculating the tax base for income tax or forming the tax base for income tax, but not recognized for accounting purposes in either current or subsequent periods.

In international standards, the concept of “permanent difference” is absent, however, other differences bear this name, which are special cases of taxation of the current year, not included in the tax base for income tax and at the same time not related to temporary differences.

Permanent differences in Azerbaijan generally accepted accounting principles often turn out to be temporary for the purposes of IFRS, since the definition of “temporary differences” in IFRS, as we described earlier, is wider than that in Azerbaijan generally accepted accounting principles.

Consider, as an example, the accrual of reserves for the depreciation of inventories (inventories). In tax accounting, there is no reserve, and, consequently, no expense in fact, which gives the accountant a false basis for classifying the difference as permanent, but in reality this difference will be restored in the future by writing off the reserve at the time of using the Inventories, from which it can be concluded That is a temporary difference. Returning to a comparison of approaches for determining temporary differences, it is worth noting that with the balance method, the temporary difference would be recognized immediately, avoiding this classification error.

In addition to differences in the methods of classification and accounting for tax differences, there are inconsistencies in the depth of detail of some conceptual aspects of accounting for deferred taxes.

The key characteristic of deferred taxes in international standards is temporary certainty, analysis of the conditions for the further sale of tax assets (liabilities).

In accordance with paragraph 47.51 of IFRS 12, the amount of deferred tax assets (liabilities) is estimated based on: (Гринкевич Л.С., Баянова К.А., 2014)

• the proposed method of implementation - reimbursement of an asset or repayment of an obligation; and

• the tax rate that will be applied in the period in which the deferred tax assets (liabilities) will be realized.

It should also be taken into account that if the tax rate varies depending on the distribution of profits, the deferred tax is calculated based on the rate applicable to retained earnings.

In many states, the tax rate differs depending on how the company intends to replace the carrying amount of the asset in question or to liquidate a specific liability. Then, when calculating the amount of deferred tax, it is advisable to evaluate the intentions of management. If the company's intentions for this asset are of a dual nature (that is, it expects to derive economic benefits from the use or disposal of the asset, and subsequently sell it without waiting for the end of the JFS), then it follows that the carrying amount of the asset will be recovered in two ways, and deferred tax calculation time such a "dual" intention cannot be excluded from the field of analysis.

In domestic legislation, differentiation of rates, based on the intentions of the enterprise regarding profit (meaning whether it will be distributed in whole or in some part) is not provided. Also, in Azerbaijan there is a fixed tax rate, and in practice there is often a discrepancy with international standards when a differentiated rate is provided in the country.

At some points, Azerbaijan standards do not contradict international ones.

When studying IAS 12, you may find that deferred tax assets are accounted for only to the extent that there is a high probability of actual taxable profit from which deferred tax assets and liabilities can potentially be rolled up (offset). The same is true for Azerbaijan generally accepted accounting principles.

It is worth noting that the standard does not give a direct concept of "high probability", however, according to paragraphs 28-29 of IFRS 12, within the framework of procedures for assessing the probability of future taxable profit, the company has the opportunity to use the possibilities of tax planning. In the domestic

standard, this aspect is not covered in any way, and remains a “gray” regulation zone. (Bragg, S. M., 2010)

There are fewer requirements for a deferred tax liability in both standards than for a tax asset.

In accordance with paragraph 15 of IFRS 12, for taxable temporary differences, a deferred tax liability always arises, except in cases that arise as a result of:

1) recognition of business reputation (initial);

2) the initial recognition of an asset and liability as a result of a transaction that does not affect either accounting profit or profit calculated for tax accounting purposes (except for transactions involving business combinations).

3) investments in subsidiaries, associates and joint ventures in the presence of a high probability that temporary differences will not be realized in the future.

In this aspect, there is a significant discrepancy between accounting standards: there are no exceptions to the recognition of deferred tax liability / asset in respect of temporary differences in Azerbaijan generally accepted accounting principles. However, due to the peculiarities of using this method, which is based on the fact that income / expenses are taken into account differently depending on time, deferred tax does not arise subject to consideration of business combinations and, to some extent, with regard to revaluation OS objects.

Let us consider in more detail what deferred taxes are in essence in the framework of business combination transactions.

When it is necessary to reflect a business acquisition transaction using the acquisition method, the principles of recognition of deferred taxes in relation to unused tax losses and loans of the acquired company, as well as in respect of temporary differences between the tax base of identifiable assets and liabilities acquired as a result of the transaction, are usually used their sizes, which is carried out in the account.

As for taxable temporary differences arising on the initial recognition of goodwill as a result of a business combination, it must be said that deferred tax liabilities are not taken into account. In addition, it must be understood that a deferred tax asset must be accounted for (if it fits the relevant criteria) within the framework of a cost that exceeds the goodwill tax base over its carrying amount for the time a business combination transaction is completed.

The Azerbaijan generally accepted accounting principles does not specify the specifics for recording deferred taxes in the accounting and reporting of consolidation and transactions in business combinations. Typically, business combinations do not recognize additional deferred taxes. If, as a result of a business combination transaction, the buyer is able to realize additional tax benefits, they will be recognized in the income statement in the usual manner; however, no adjustments are made to the amounts initially recognized in a business combination (acquisition of a subsidiary), which is consistent with the requirements of IFRS.

At the same time, changes in the amount of the deferred tax assets of the buyer, including a change in the assessment of their feasibility that arose as a result of a business combination transaction, are recognized separately from the results of the reflection of this transaction by the acquisition method.

As for goodwill, recognition of deferred tax is only possible in relation to that goodwill that is "recognized in the buyer's financial statements when acquiring an enterprise as a property complex" (Diri, M. E., 2018). Goodwill is amortized for accounting purposes and for determining the tax base for income taxes, but over different periods, which leads to temporary differences in respect of which the customer recognizes a deferred tax liability.

Other discrepancies in tax accounting in the two standards include accounting for deferred taxes regarding foreign exchange differences, investments in subsidiaries, associates and joint ventures, share payments and transactions in hyperinflationary

conditions, mainly because Accounting Provision 18/02 is not detailed and illustrative in part its application to specified situations.

It is also necessary to describe the reflection of deferred taxes in the financial statements.

Azerbaijan generally accepted accounting principles enable companies to make decisions regarding the offsetting of deferred taxes on their own, with the exception of those points that are prohibited by law (for example, in transactions with shares and bonds). Regarding the offsetting of deferred tax assets and liabilities, no specific explanations are provided in Azerbaijan generally accepted accounting principles.

In accordance with IFRS 12, deferred tax liabilities and assets are offset in cases where the firm has duly executed rights to this, and deferred tax liabilities and assets are directly related to income tax, which is levied by a specific tax authority:

- from a specific company;
- from various companies, however, they have plans to settle their tax relations on a net basis, or their tax assets will be realized simultaneously with the repayment of tax obligations (Cihan, B. & Suleymanov, E., 2011).

The net deferred tax credit scheme provided by IFRS 12 is quite relevant in light of the relatively recent practice of consolidated tax payments. At this moment in Azerbaijan there are 16 consolidated groups of taxpayers (CGT), most of them formed in 2011-2012.

The formation of CTG allows you to reduce the consolidated tax base by the size of the net losses of CGT enterprises, and classify transactions between KGN participants as uncontrolled for applying transfer pricing control rules.

Since CGT enterprises have an officially registered (legal) right to offset current tax liabilities and are ready to use it, it is also possible to offset deferred taxes within the framework of the whole CGT.

To summarize the above, it is necessary to say that contrary to the general trend of accounting standards, there are still irreconcilable differences between them, for example, in respect of deferred income tax.

These discrepancies mainly arise due to various methods in IFRS and Azerbaijan Accounting Standards: the first considers deferred taxes from the perspective of their possible future implementation and presentation to users, and the second makes the initial assumption that the deferred tax account exists rather for the mechanical adjustment of the gap between accounting and tax accounting.

2.2. Revenue and expense recognition under IFRS and book-tax differences of income

International Standard IAS 18 “Revenue” defines the conditions for recognition of revenue, i.e. the receipt of economic benefits from the core business of the enterprise, which leads to an increase in equity (except for shareholders' contributions). This standard separates the concepts of revenue and revenue. According to IAS 18, revenue is the receipt of economic benefits for the period arising in the ordinary course of business of the company, the result of which is an increase in equity other than capital gains from shareholders 'deposits, and income is any income that increases equity (except for shareholders' deposits) , both in the ordinary course of business (revenue), and other income. In the practice of Kazakhstani accounting, the concept of "revenue" has traditionally been replaced by the concept of "income from the sale of products and the provision of services."

In accordance with IAS 18, revenue from the sale of goods is recognized if all of the following conditions are met: (American Institute of Certified Public Accountants, 2019)

1. the seller transferred to the buyer the risks and rewards associated with the possession of the goods. In most transactions, the transfer of risks coincides with the transfer of ownership and ownership;

2. the seller no longer participates in the management of the goods (does not control the goods) on the basis of ownership;

3. The amount of revenue can be reliably estimated;

4. there is a probability of receipt of economic benefits (payment);

5. Transaction costs can be measured reliably.

Transactions with a significant risk of ownership (for example, when the buyer is highly likely to cancel the transaction) are not considered sales and do not form revenue - for example, any sales to the retail network in which the seller commits himself to take unsold goods from the network at his own expense. Transactions in which the risk of termination is negligible (for example, with mass retail sales), generate revenue immediately, subject to the assessment of the seller's future risks and obligations.

Income from the sale of goods is recognized when the goods are shipped, while ownership has passed to the buyer, i.e. at the stage of completion of the transaction at the reporting date.

In accordance with Section 5 of the National Financial Reporting Standard No. 1 dated June 21, 2007, income recognition criteria are:

1. the transfer to the buyer from the seller of significant risks and benefits of ownership of goods;

2. the seller is no longer involved in management and does not control the goods sold;

3. the amount of income can be reliably estimated;

4. there is a likelihood that the economic benefits associated with the transaction will go to the organization;

5. The costs incurred or expected in connection with the transaction can be reliably estimated.

Thus, in IFRS and in the NFRS, the criteria for recognition of income in accounting are almost identical.

Despite the fact that there is no special standard for expenses among IFRS, there are international standards that indirectly regulate the principles of accounting for expenses of an enterprise. For example, International Accounting Standard No. 2 “Inventories” (IAS 2. Inventories), which operates in the field of inventory accounting system, refers to such standards. This standard rigidly establishes the methodology for transferring indirect production costs to the cost of finished products, intersecting with the field of production management accounting. The standard establishes requirements for the annual inventory procedure and revaluation of stocks. (Collings S., 2013)

This standard approved the methodology for the distribution of indirect production costs. In addition to direct production costs, indirect (variable and fixed) costs (overheads) are also included in the cost of inventories, distributed among products on a systematic basis. The standard requires the distribution of fixed indirect costs by the standard-cost method, in which the relative norm for the distribution of overhead costs is fixed for the normal capacity of the production capacity. The international standard does not strictly define the principles of the distribution of indirect costs between different types of products - the main thing is that the methodology is applied consistently and reasonably.

The principles of accounting for income and expenses also include the rules for providing information on the income and expenses of the enterprise in the financial statements. When presenting financial statements, an entity shall disclose in an explanatory note:

- accounting policies adopted for income recognition, including methods for determining the stage of completion of a transaction for the provision of services;

- the amount of each significant type of income recognized for the reporting period.

In the accounting policy, in the "Revenue Recognition" section, an entity shall indicate the principle of revenue recognition. According to IAS 18, such a principle is

the recognition of income when the goods (finished products) are shipped and the ownership is transferred to the buyer. Recognition of revenue by the stage of completion is called the "as soon as possible" method.

The second principle is the separation of the amounts of each of the significant types of income. Moreover, the accounting policies determine the main types of enterprise income. Most often, these include:

- income from the sale of goods, the provision of services,
- interest income, royalties,
- dividend income.

Interest income is accrued on a temporary basis, with reference to the principal amount of the debt and the applicable interest rate.

IAS 18 "Revenue", in this case, by interest means the fee for the use of cash or cash equivalents or amounts due to the entity. In the Republic Azerbaijan, if an enterprise carries out activities that are not licensed in accordance with banking legislation, it may receive interest in the form of interest, granting a commodity loan. Therefore, interest under IFRS should be considered as interest on investments in securities.

Dividend income is recognized when the right of shareholders to receive them is recognized.

The recognition of expenses in accordance with IFRS largely depends on the recognition of revenue in accordance with the principle of comparability of income and expenses. Therefore, the costs associated with obtaining the related income are recognized in the financial statements at the time the income is recognized.

All income and expense accounts received for the year are closed at the end of the year and reflected in the income statement.

Information provided by the entity directly in the income statement itself should include, at a minimum, aggregated indicators of the following amounts: (Epstein, B. J. & Jermakowitch, E. K., 2008)

- income;

- financing costs;

- the share of profit or loss from investments in an associate and joint venture accounted for using the equity method;

- tax expenses;

- a single amount, representing the total amount of profit or loss after taxes from discontinued operations and other income or loss after taxes recognized in measuring fair value, less the costs of the sale or disposal of assets or group (s) of disposal, which are discontinued activities in accordance with section 34 of NSFO No. 1;

- profit or loss.

An entity shall disclose the following items directly in the income statement itself as a distribution of profit or loss for the period:

- profit or loss attributable to minority interests; and

- profit or loss attributable to owners of equity instruments of the parent organization.

Additional articles, headings and subtotals should be presented directly in the statement of profit and loss when this presentation is appropriate for understanding the financial results of the company.

An entity should also present an analysis of expenses using a classification based either on the nature of the expenses or on the function of expenses, depending on which of them provides reliable and more relevant information.

Under the "analysis by nature of expenses" method, expenses are consolidated in the income statement in accordance with their nature (for example, depreciation of fixed assets, procurement of materials, transportation expenses, employee benefits and advertising costs) and are not redistributed between different functional areas within subject (https://www.iasplus.com/en/standards).

Within the framework of the "analysis by cost function" method, classification of expenses is generalized by their function in accordance with their functional areas

(for example, sales costs, administrative costs). In accordance with this method, the entity, at a minimum, discloses the cost of sales separately from other expenses.

The presentation of such an analysis by enterprises directly in the income statement is welcome.

At the end of the calendar reporting year, the final amount of corporate income tax due to the budget at the established rate taking into account adjustments to the taxable income to the budget is finalized as a matter of priority from the amount of actual accounting income received by the enterprise for the reporting year.

In addition to the current legislative acts in the field of accounting, the procedure for recognizing the income and expenses of an enterprise is regulated by tax legislation.

The Tax Code defines the cases of attributing deductions from the total annual income of expenses within the limits of norms. Deductions are made only if there are documents confirming the costs associated with obtaining the total annual income. These expenses are deductible in the tax period in which they are actually incurred, with the exception of deferred expenses. Deferred expenses are deductible in the tax period to which they relate.

Tax legislation sets forth its requirements for recognition, disclosure and measurement of financial categories in financial statements. As a result of this, differences arise in the estimation of income and expense accounts, and as a result, differences in the amounts when assets and liabilities are reflected in financial statements, in most cases, such differences arise in the period of occurrence of expenses and recognition of the corresponding income. There are differences permanent, temporary, mixed (temporary-permanent). The procedure for determining income differs in accounting from tax accounting. In the first case, income from sales is defined as the difference between revenue without value added tax and excise taxes and expenses on production and sales determined by regulatory accounting documents. In tax accounting, income is calculated as the difference between total

annual income (excluding indirect taxes) and deductions determined by tax legislation. Table 2. shows the distinguishing features between taxable income and accounting income.

Table 2: The difference between taxable income and accounting income

Indicator	Taxable income	Accounting income
Definition	The amount of income (loss) for the reporting period, determined in accordance with tax legislation	The amount of net income or loss for the reporting period before taxes; calculated as the difference between income and expenses
Formation order	It is formed in accordance with tax legislation, which does not provide for alternative tax accounting methods.	It is formed on the basis of accounting policies adopted by the organization, on the basis of principles and accounting standards that provide for various alternative methods of accounting and measurement
Susceptibility to change	Change is subject to tax policy.	Less affected by consistency and comparability

Source: Christian, D. & Ludenbach, N., 2013

The vast majority of financial instruments of an enterprise are interpreted in the same way in both accounting and tax accounting. The effect of certain events or operations, however, will have a different reflection in tax and accounting. The tax effect of most events reflected in the financial statements for the period is taken into account when determining the amount of corporate income tax payable.

Temporary differences are differences between taxable and accounting income for the reporting period, which arise because the period in which certain items of expense and income are included in taxable income does not coincide with the period in which they are included in accounting income. Temporary differences arise in one period and are canceled in one or more subsequent periods. Some temporary differences may not be directly associated with certain assets or liabilities, but, nevertheless, are the result of economic events reflected in the financial statements and will have a tax effect in future periods.

Permanent differences are differences between taxable income and accounting income for the reporting period that arise in the current reporting period and are not canceled in subsequent reporting periods. (Beardsley R., 2017)

Usually, temporary differences arise as a result of using different methods of depreciation in tax and accounting, drawing up a plan of compensation payments to employees, when drawing up a plan that reflects time-based payments upon completion of a certain percentage of work in capital construction.

The temporary difference is canceled at the moment when the related asset is restored or the corresponding liability is settled. Deferred tax revenues or expenses represent an increase or decrease in taxes payable or reimbursable in future periods as a result of temporary differences and offsetting tax losses for a future period at the end of the current year.

Deferred corporate income tax is included in the category of so-called estimated liabilities, the exact amount of which cannot be determined before a certain date. In the case of income tax, its amount, as you know, depends on the financial results of the enterprise, which remain uncertain until the end of the year. Taxes, however, must be paid during the year before the final amount of obligations is calculated.

In modern accounting in Western countries, the concept of temporary differences is interpreted more broadly than by our standards. Temporary differences include all types of differences between accounting and tax records of assets and liabilities, which are expressed as a result of temporary differences payable or deductible.

A temporary deductible difference is the sum of the differences to be deducted in determining taxable profit when the carrying amount of the related asset is restored or the related liability is settled.

Temporary difference to payment is the amount of differences between tax payments, which is determined when calculating taxable profit in future periods at the time of restoration of the book value of the corresponding asset or repayment of the corresponding liability.

There are four main types of temporary differences, namely:

1) recognition of income in accounting precedes the period of recognition of it in tax accounting (example: profit from investments, recognized as income in accounting, is recognized as such in tax accounting only after receiving / paying it as dividends). Temporary differences of this type lead to an increase in the amount of the liability / expense for deferred tax and are, therefore, temporary differences for payment;

2) the recognition of income in tax accounting precedes the period of its recognition in accounting (example: for tax accounting, income from funds transferred to a construction company in advance for a contract for repair work is recognized in full for the entire amount; in accounting, income is recognized according to the terms of the contract portioned, depending on the percentage of work performed). Temporary differences of this type lead to an increase in the amount of asset / income for deferred tax and are, therefore, temporary differences for deduction;

3) the recognition of an expense that reduces taxable profit precedes the period of its recognition in accounting (example: in accounting, a straight-line method of depreciation is used that increases the useful life of an asset, whereas in tax accounting only an accelerated method of depreciation is used that reduces the life of an asset) Temporary differences of this type lead to an increase in the amount of the liability / expense for deferred tax and are, therefore, temporary differences for payment;

4) recognition of an expense in accounting is ahead of its recognition as a factor that reduces taxable profit in tax accounting (example: this relates mainly to estimated or estimated expenses, such as expenses for the provision of warranty services or accrued expenses by court order. Such expenses are not subject to accounting in taxation until they are fixed, i.e. they do not move from the rank of evaluative to the rank of valid). Temporary differences of this type lead to an increase in deferred tax asset / income and are, therefore, temporary deductible differences.

The principles of accounting for income and expenses include: (Bakker, A., Berg, T. v. d. & Janssen, B., 2015)

-the procedure for the recognition of income and expenses in accounting;

-the procedure for determining taxable profit;

-principles of reflection of income and expenses in the financial statements of the enterprise.

2.3. Impact of differences between IFRS and tax accounting regarding revenue/expense recognition on financial reporting quality

In connection with the intensification of the process of globalization of the world economic system, Azerbaijan, by reforming the economic sector, went to the implementation of IFRS. One of the main problems in the field of the economy of the Azerbaijan is the problem of overcoming the differences between IFRS and AAS in accounting principles and the purpose of presenting financial statements (Bulaev A.V.. 2015: 11). The relevance of studying the differences in IFRS and AAS (Azerbaijan Accounting System), affecting the analysis of financial statements, due to the fact that the financial statements, like a mirror, reflects the results of the company. Analysis of the financial condition of the enterprise allows you to assess whether the business entity is able to finance its production activities, constantly maintain at an acceptable level its solvency, liquidity and investment attractiveness. The process of successful functioning of a business entity is an interconnected, balanced and multi-structured system. The main task of the financier-analyst and manager is a reliable assessment of the assets and liabilities of the enterprise at the reporting date, carried out using the analysis of financial statements (Syrovatsky E.Y., 2012: p.11). Analysis of financial statements should be based on real, reliable data on the activities of the enterprise. American science fiction writer, journalist and literary critic Bruce Sterling argues that "information itself is not power, otherwise the most powerful people in the world would be librarians" (http://aforizmer.ru/aforizmi/bryus-sterling). Financial statements are

the final result of the financial and economic activities of an economic entity. Therefore, based on the data presented in it, internal and external users make economic decisions.

International Financial Reporting Standards (IFRS) are a set of documents (standards) governing the rules for the preparation of financial statements necessary for external and internal users to make economic decisions regarding the enterprise. The list of organizations that present and publish IFRS financial statements is expanding annually. According to the "On Consolidated Financial Statements", IFRS financial statements are prepared by:

1) credit organizations;

2) insurance organizations (with the exception of medical insurance companies operating exclusively in the field of compulsory medical insurance);

3) non-state pension funds;

4) management companies of investment funds, mutual investment funds and non-state pension funds;

5) clearing organizations;

6) state unitary enterprises, the list of which is approved by the Government of the Azerbaijan;

7) open joint stock companies whose shares are in federal ownership and the list of which is approved by the Government of the Azerbaijan;

8) other organizations whose securities are admitted to organized trading by their inclusion in the quotation list.

(http://ipp.spb.ru/index.php?page=news_archive&list=3&id=3251)

An increasing number of Azerbaijan enterprises need to prepare financial statements not only according to Azerbaijan accounting rules, but also according to international standards. Understanding the fundamental differences between AAS and IFRS will allow companies to switch to accounting according to international standards with minimal costs, as well as analyze the financial statements in the

highest quality. The main differences between IFRS and AAS, affecting the analysis of the financial statements of the organization, are presented in table 2.3.

Table 3: The main differences between IFRS and AAS

Comparative feature	**AAS**	**IFRS**	**Assessment of the impact on the analysis of financial statements**
Purpose of Using Financial Information	Reflection of property status	Reflection of real financial position	IFRS has a higher degree of compliance with the real state of things of information in the statements
Asset recognition framework	Availability of supporting documents	The possibility of obtaining economic benefits from the object	Unlikely receivables may be recognized in AAS as assets, which will distort subsequent financial analysis.
Initial cost of the FA	The amount of actual costs is recognized. Discounting in determining the initial cost of the FA is not applied.	Recognized at cost. If the payment for fixed assets is postponed for a considerable period of time, then the initial cost of fixed assets is equal to the discounted value of future payments.	The absence of discounting distorts the objectivity of reporting under AAS, but increases the reporting indicators: accounts receivable, profit and so on.
Cost Recognition	The expense is recognized in the account, if a contract is concluded, documentary confirmation is required	Expenses are recognized on a matching basis. No documentary evidence required.	IFRS reporting is based on higher quality information than RAS. However, the data on expenses in AAS are reliable, since there is documentary evidence.
Revenue recognition condition	Income from ordinary activities is recognized in the financial statements on the basis of legal confirmation (contract or other document)	Revenue recognition is associated with the moment of transfer of significant risks and rewards due to ownership of goods	The moment of transfer of significant risks and rewards due to the ownership of the goods, in the general case, may differ from the date of transfer of

			property rights indicated in the contract (or other document)
Balance sheet equation	Assets = Liabilities	Assets - Liabilities = Equity	The effectiveness of the organization in accordance with IFRS is measured by profit. AAS allows for both profit and loss.
Inflation adjustment	Azerbaijan Accounting Standards Compiled Without Adjustment For Inflation	Non-monetary items of the balance sheet should be recalculated for inflation in hyperinflation	Analysis of IFRS data gives a more realistic picture of the state of affairs in the organization

Source: http://www.klerk.ru/buh/articles/376670/

The differences between IFRS and AAS are due to historical goals for using financial information. IFRS aims to reflect the real financial situation of the enterprise, AAS - property position. The main users of financial statements prepared in accordance with IFRS are investors and financial institutions. The preparation of the Azerbaijan financial statements primarily pursues fiscal goals, this information is necessary for tax authorities, statistical agencies.

Azerbaijan reporting organizations is aimed primarily at minimizing taxes. IFRS - primarily aimed at meeting the interests of investors and other users who are not connected and do not have access to reporting. It is the interests of investors to a greater extent reflect the needs of other users. Since they are the suppliers of capital and to a greater extent do not affect the decisions taken on reporting. Therefore, meeting their needs will also help meet the needs of other users.

AAS is rather tightly connected with the legislative and regulatory system in the Azerbaijan, and IFRS are supranational standards that are independent of laws. In practice, financial statements focused on the requirements of tax legislation often contain distorted financial information, based on which it is difficult to determine the

actual capitalization of an organization and establish its actual financial position. And this, in turn, does not at all contribute to the influx of investments into the Azerbaijan economy, increases the price of incoming capital and, therefore, negatively affects the expansion of the tax base. However, this does not mean that IFRSs are fully capable of reflecting the actual financial condition of an enterprise that meets all the requirements of users, while AAS is not capable of. This is evidenced by the practice of their application. Distortion and falsification are present both in IFRS and in AAS. Therefore, without control and responsibility for compliance with certain rules, it is impossible to implement both IFRS and AAS. As can be seen from table 3, the main principle of recognition of assets in accordance with IFRS is "the possibility of obtaining economic benefits from the object", in AAS - "availability of supporting documents". If a company acquires fixed assets with deferred payment, then in accordance with IAS 16 "Fixed Assets" the initial cost of such fixed assets is formed at a discount, since in fact the organization made the purchase cheaper. The choice of the discount rate is determined by professional judgment. AAS does not use the principle of discounting and determines the initial cost of an object by the nominal value of payments. The absence of such a method distorts the objectivity of reporting under AAS, but raises such reporting indicators as accounts receivable, profit, and so on. In AAS, unlike IFRS, it is not established that "assets" are acquired for the purpose of obtaining economic profit (profit) and that economic operations reflected in financial accounting as income and expenses must meet the definition of elements "income", "expenses", and each of them is also at the same time defining the "assets" element, since expenses are incurred in order to make profit in the future (economic benefit due to excess of income over expenses) (Moshchenko N.P., 2007: p.71).

Another fundamental difference is the recognition of costs. The compliance requirement, according to which expenses are recognized in the period of expected income, is central to IFRS. Expenses are recorded as they fall due, and not upon payment or receipt of money. Consequently, there may be accruals in the financial

statements (when expenses have already been incurred, and the corresponding amounts are not yet payable and prepayable, when the amounts have already been paid or liabilities have been recorded, even if the costs associated with them relate to the subsequent reporting period). In 10/99 “Organization expenses” an additional condition is included that the expense is recognized if an agreement is concluded. That is, in contrast to IFRS, the expense cannot be recognized only on the basis of the professional judgment of the accountant to reduce economic benefits and must necessarily be documented. For example, the costs of bonuses to employees. As a rule, premiums for the year are approved in May of next year. In Azerbaijan accounting, costs are recognized after accrual of premiums, that is, in the cost of the next reporting period. Consequently, the financial statements in accordance with IFRS reflect financial results more real than in accordance with AAS (http://ipp.spb.ru/index.php?page=news_archive&list=3&id=3251).

According to Accounting Provision 9/99, the condition for recognition of revenue is an approach in which income from ordinary activities is recognized in the financial statements on the basis of a specific legal confirmation (contract or other document). IAS 18 relates revenue recognition to the moment that significant risks and rewards arising from ownership of the goods are transferred. The indicated time may differ from the date of transfer of property rights indicated in the contract (or other document). The main differences in revenue recognition according to AAS and IFRS are presented in table 2.4, compiled on the basis of AAS 9/99 “Income of the organization” and IFRS 18 “Revenue”.

Table 4: Differences in revenue recognition in IFRS and AAS

Comparative feature	AAS	IFRS
Revenue Recognition	There is confidence that there will be an increase in economic benefits. The amount of revenue can be determined.	There is a possibility of obtaining the estimated economic benefits. The total contract revenue can be measured reliably.
Revenue recognition moment	Revenue is recognized when the transfer of ownership takes place on the basis of a specific legal confirmation (contract or other document).	Revenue is recognized when the transfer of significant risks and rewards arising from ownership of the goods occurs.
Revenue estimate	The amount of revenue is determined based on the price specified in the contract.	Revenue is measured at the fair value of the consideration received, taking into account the trade discounts and rebates presented
Legal regulation	Different types of operations are regulated by one normative act (Accounting Provision 9/99)	Different types of operations are governed by general principles.
Recognition of shareholder contribution as revenue	Deposits of LLC participants that are not registered as contributions to the authorized capital or contributions to property are recognized as income of the organization	Deposits received from existing shareholders are not recognized either as income or as revenue

Accounting Provision

The central place in the Azerbaijan financial statements is the balance sheet, in IFRS - the profit and loss statement. Compiled in accordance with IFRS, the profit and loss statement in its structure is more analytical and substantial than the Azerbaijan report on financial results. This report is central to IFRS, and the procedure for compiling it is rather laborious. It well reveals all the economic activities of the company for the reporting period, and also serves as the main source of indicators for financial analysis.

The basis for the construction and understanding of the balance sheet is considered to be the balance sheet equation - an equation that reflects the relationship between assets, liabilities, liabilities and equity. The Azerbaijan balance sheet is characterized by the equation "Assets = Liabilities", that is, the balance sheet is considered as the correct entries on the accounts during the reporting period. The balance sheet prepared in accordance with the requirements of IFRS is characterized by the equation “Assets - Liabilities = Equity”, that is, equity is the share in the assets of the company remaining after deducting all of its liabilities. A measure of the effectiveness of the enterprise is its profit. Capital in IFRS is considered not so much as the result of assessments of past events, but as the result of today's assessments of the current state of the organization, which to a greater extent (compared with assessments of past events) can serve as the basis for future-oriented investment decisions. In addition, articles in the Azerbaijan balance sheet are strictly assigned to sections. In IFRS this is not.

IFRS gives the opportunity to study a variety of indicators of many time periods, however, according to AAS, most organizations, as a rule, reflect data for the last two reporting dates. Lack of information for in-depth analysis of reporting and trending is a disadvantage of AAS. It should also be noted that AAS reporting is compiled without adjusting for inflation. In IFRS, non-monetary items of the balance sheet should be translated into inflation in a hyperinflationary economy. Analysis of IFRS data gives a more realistic picture of the state of affairs in the organization.

III CHAPTER. DEVELOPMENT OF OPTİMAL APPROACH TO RECONCİLİATİON OF İFRS AND TAX ACCOUNTİNG

3.1. Correct approach to determining an optimal divergence between IFRS and Tax Accounting. Application of best practices to Azerbaijan

The integration of the Azerbaijani economy into the global economy is one of the priorities of the state economic policy pursued in recent years in the Republic.

Reforming the national accounting system in accordance with international standards is one of the main state accounting policies as an integral part of the above policies.

Accounting reform in Azerbaijan involves the following steps:

1. Adoption of a package of legislative acts regulating the activities of accounting entities in the preparation and presentation of financial statements in accordance with international standards;

2. Development and implementation of a set of measures reflected in the relevant regulatory legal acts on the submission by the accounting entities of new financial statements within the deadlines established by the legislation of Azerbaijan;

3. The implementation of the continuous learning process in order to acquire the necessary, fundamental knowledge on the preparation of new financial statements by accounting entities, the implementation of external and internal audits for the quality and timely presentation of these reports within the framework of the approved relevant program documents.

It can be said that at present, in accordance with certain provisions and requirements of the Law "On Accounting", which entered into force by Decree of the President of the Republic of Azerbaijan on September 2, 2004, the main package of regulatory legal acts regulating the activities of accounting entities has been approved in the republic on the application of the new financial statements.

The terms of application of international accounting standards specified in article 17 of the law require that all commercial enterprises, with the exception of small business, be required to apply International Financial Reporting Standards (IFRS) and National Accounting Standards based on IFRS starting January 01, 2008. At the same time, municipal authorities, budgetary organizations and extrabudgetary state funds are obliged to apply the National Accounting Standards in accordance with the International Accounting Standards for the Public Sector starting January 1, 2009 (Bağırov D., 2010).

At the same time, in order to ensure a set of measures for the targeted application of this law, by a decree of the President of the Republic of Azerbaijan on February 7, 2005, the Ministry of Finance had powers to implement state regulation in the field of accounting.

The main objective of this regulation is to develop a set of measures with the aim of coordinating the provision of coordinated actions for the presentation of more transparent and high-quality new financial statements by accounting entities prepared on the basis of financial accounting and in accordance with international requirements.

Within the framework of the legislative powers of state regulation received by the Ministry of Finance, the following results were achieved, which are provided for at the first stage of the said reform:

• Organized work on the translation of International Financial Reporting Standards (IFRS), as well as the approval of these transfers as official texts in the Fund of the Committee on International Accounting Standards;

• Developed and approved National Accounting Standards for commercial organizations on the basis of IFRS according to the version of 2006;

• Comments and recommendations on the implementation of the approved National Accounting Standards for commercial organizations have been developed and approved;

• Developed and approved National Accounting Standards for municipal authorities, budgetary organizations and extrabudgetary state funds in accordance with the International Accounting Standards for the Public Sector;

• A program for transition to IFRS for structures of public interest was developed and approved in accordance with the Resolution of the Cabinet of Ministers of the Republic of Azerbaijan dated July 18, 2005. The list of these structures includes commercial enterprises with the most powerful production potential, namely: enterprises with two indicators that exceed the criterion values of indicators (annual income, average number of employees for one year and the balance sheet) established by the Resolution of the Cabinet of Ministers of the Republic of Azerbaijan dated 20.06. 2005 year (Cihan, B. & Suleymanov E., 2011).

The program identified the following specific steps that ultimately ensure the earlier application of financial statements based on IFRS, in contrast to the application deadlines set for other similar structures:

- Creation of a working group on the implementation of IFRS;

- Translation of specific IFRS at the expense of own funds into the Azerbaijani language;

- Training of accounting staff in order to acquire fundamental knowledge of IFRS and the application of the conversion methodology in connection with the preparation and presentation of financial statements;

- Analysis of the traditional and modern accounting system;

- Development of accounting policies in accordance with IFRS;

- Development of a working chart of accounts in accordance with adopted accounting policies;

- Development of basic accounting records (entries) in accordance with the adopted work plan of accounting accounts;

- Development of instructions for the preparation of financial statements;

- Implementation of conversion procedures for the preparation of financial statements based on IFRS;

- First time adoption of IFRS.

In accordance with this program, structures of public interest began work on the transition to IFRS.

At present, the Republic has begun to carry out the tasks of presenting new financial statements provided for in the second stage of the reform.

In order to provide effective assistance to organizations in connection with their transition to international accounting standards, with the subsequent strengthening of the functions of monitoring the implementation of these

By a decree of the President of the Republic of Azerbaijan dated December 19, 2007, the Ministry of Finance was instructed to conduct systematic monitoring at enterprises that apply new accounting standards within the time frames established by law.

Given the earlier deadlines for the submission of financial statements by entities of public interest in accordance with the list approved by the Decree of the Cabinet of Ministers of the Republic of the Ministry of Finance as a result of monitoring, a significant part of these enterprises was covered for the implementation of IFRS in the transition period.

Summarizing and analyzing the results identified during the monitoring, the following results were obtained:

1. At present, a number of enterprises compose financial statements in accordance with IFRS;

As a result of targeted work, the AzərCell Telecom MMM enterprise achieved certain successes in the implementation of the main block of measures for the transition to IFRS, including the work on acquiring the necessary knowledge and skills on the application of these standards by specialized service employees

(accountants, programmers), as well as providing these employees with necessary technical means (materials for the preparation of financial information).

At the same time, some of the measures taken (including the development of accounting policies in accordance with IFRS, the development of instructions for the preparation of financial statements and the development and implementation of conversion procedures for the application of IFRS), in our opinion, were not presented at a high level, without appropriate scientific methodological substantiation or did not cover all the methodological and practical aspects adopted and applied at the present stage of accounting reform.

However, this does not detract from the positive results achieved by AzerCell Telecom MMM in implementing IFRS, which since 2006 AzerCell Telecom MMM has been submitting financial statements based on IFRS.

The State Oil Company of the Republic of Azerbaijan (SOCAR) and the enterprises subordinate to this company as a result of targeted activities to implement the program document gained some experience in preparing financial statements based on IFRS.

Here, first of all, the role of SOCAR in organizing translations of IFRS into the Azerbaijani language should be noted. So, out of the total number of IFRS adopted by the Fund of the Committee on International Accounting Standards in 2006, 14 standards were transferred at the expense of the company.

In addition, some work was carried out to train relevant personnel in order to acquire fundamental knowledge on the application of IFRS and the presentation of new financial statements. So, in order to achieve this goal, SOCAR from January 1, 2006 to July 1, 2008, a significant number (over 1000) of accounting specialists participated in the courses on the implementation of IFRS (IBP, 2017).

Technical assistance in preparing and presenting these reports was provided by Price Waterhouse Coopers.

Currently, this reporting has been submitted to the Ministry of Finance in accordance with the requirements stipulated by the legislation of the Azerbaijan Republic.

2. Enterprises mainly carried out activities to apply IFRS;

Aztelecom Production Association, Azeriqaz closed joint-stock company and a company subordinate to this company, Azərsu open joint-stock company, Azərenerji open joint-stock company, Azerbaijan State Railways carried out the activities of the program document on the preparation of financial statements based on IFRS, with the exception of measures for the implementation of conversion procedures for the preparation of financial statements based on IFRS, as well as for the first application of IFRS.

3. Partial implementation of measures to prepare financial statements on the basis of IFRS, as well as the absence of any actions on the implementation of this program by some organizations was revealed.

Bakı Metropoliteni, Azərkimya State Company and the company subordinate to this company carried out only three activities of this program (creation of a working group on the implementation of IFRS, translation of specific IFRS at the expense of own funds into Azerbaijani, as well as training of accounting staff with the purpose of acquiring basic knowledge of IFRS and the application of the conversion methodology in connection with the preparation and presentation of financial statements).

In addition, it can be said that the Organization "Dövlət Xəzər Dəniz Gəmiçiliyi" did not carry out these work on the preparation of financial statements based on IFRS.

The causal dependence of the results, in our opinion, can be characterized by the following conclusions:

1. Currently, with the entry into force of the new law "On Accounting", financial accounting based on IFRS has been separated from tax accounting based on the principles and provisions of the tax legislation of the republic.

In turn, the traditional national accounting system, which has lost legal force and brought into compliance with tax legislation, has essentially turned into an integral part of tax accounting, without which it is no longer possible for taxpayers to correctly and impartially submit relevant tax reports.

Given the existing problems with the application of IFRS in the opinion of the author, in the context of the transition of accounting to international standards, it is necessary to restructure the financial service with the creation of appropriate accounting structures based on IFRS and tax legislation. These structures will carry out financial and tax accounting, as well as present financial and tax reporting.

In other words, in relation to existing conditions, instead of having lost the legal force of financial statements approved in accordance with the requirements of the old Law "On Accounting", which entered into force on July 01, 1995, we are talking about transforming these financial statements into tax ones or developing and adoption of the Tax balance, the Report on tax results, the Report on the movement of capital and funds of the enterprise, respectively (The Tax Code of the Republic of Azerbaijan, 2016).

2. Currently, there is a great need in the republic for the training of relevant specialists in introducing financial accounting.

Therefore, measures for the targeted mastery of financial service specialists by the necessary, fundamental knowledge about the application of IFRS using various methods of promotion and incentive should be the focus of attention of the governing body of the accounting entity.

In other words, one of the necessary factors for the implementation of IFRS is the creation of an appropriate intellectual potential capable of the conversion and transformation procedures for the transition to new financial statements.

3. The development of appropriate software to automate the introduction of financial accounting is one of the paramount tasks for the successful implementation of IFRS.

Thus, conditions will be created for coordinating the activities of tax and financial accounting specialists, as well as the effective application of internal control methods audit using the methodology of the tax bridge or the transition of financial accounting to tax accounting.

Achieving this goal involves the allocation of significant financial resources in connection with the acquisition of appropriate technical means and technologies, as well as education and training services for the implementation of software to automate the introduction of financial accounting, which naturally makes for an accelerated solution to this problem.

4. In the context of the transition to IFRS, including also work in the initial phase of implementation of these standards, the successful preparation and presentation of new financial statements depends on the degree of involvement of enterprises in this work by professional accounting organizations.

In accordance with article 4.3.6. The Law “On Accounting” in order to improve the national accounting system, the Ministry of Finance cooperates with professional accounting organizations.

At this stage of the reform of the accounting system, there is a weak involvement of such enterprises. This is due to objective and subjective factors of their disinterest in the provision of such consulting services, including, of course, work related to the automation of the process of introducing financial accounting.

If the influence of objective factors can be explained by registration in the prescribed manner of professional accounting organizations and, accordingly. the intensification of their activities in the provision of consulting services for the introduction of financial accounting after the approval of the new law “On Accounting”, namely, since 2005, the influence of subjective factors in the opinion of the author is determined by the absence of any coordinated actions to implement IFRS between the authorities executive authorities, supervising, within the framework of

the relevant powers delegated by the legislation, to present high-quality and timely new financial statements.

The absence of the indicated conceptual approach or the atmosphere of impunity existing at the enterprises pushes almost to the last plan all the necessary measures related to the application of IFRS.

Meanwhile, the Accounts Chamber, the Chamber of Auditors, as well as independent auditors conduct audits or provide audit services (present an audit opinion) for the preparation and preparation of financial statements in accordance with IFRS within the framework of the authority delegated to them established by the legislation of the republic ..

In addition, in accordance with article 247-1 of the Code of Administrative Violations of the Republic of Azerbaijan, which entered into force by Decree of the President of the Republic of Azerbaijan dated September 20, 2005, a system of penalties was established for official legal entities guilty of violating legislation on the preparation and submission of financial and the combined (consolidated) financial statements, as well as the storage of accounting documents.

If these violations are detected, the penalties established by law will be applied to credit organizations by the National Bank of the Republic, and for other accounting entities by the Ministry of Finance of the Republic.

Thus, the creation of an effective system for the implementation of external and internal audit involving all interested parties that oversee the presentation of financial statements on the basis of IFRS, within the framework of the authority delegated by the legislation to these parties, in the opinion of the author, will dramatically accelerate the resolution of existing problems in the field of accounting Since June 1, 2018, the Law of the Azerbaijan Republic on Amendments to the Law of the Republic of Azerbaijan on Accounting has entered into force (hereinafter - the Law).

Major changes to the law can be classified into several categories.

According to the amendments, enterprises are divided into 4 groups - micro, small, medium and large businesses. The criteria for the above groups are determined by the Cabinet of Ministers. Accounting standards for enterprises also differ by these criteria.

New accounting rules have been established, and accounting organizations are required to comply with these rules. Thus, entities must create a separate accounting section within the organization or maintain a separate accountant.

Under the new rules, the chief accountant must be involved in the business, and senior accountants must be professionals in large legal entities, budgetary organizations and legal entities that publish annual financial statements or consolidated financial statements. If the accountant is associated with the contract, these persons must sign an employment contract with at least two professional accountants. If an accountant participates in these enterprises under a contract, an employment contract must be concluded with at least two professional accountants.

Financial reporting standards will also be amended. The International Financial Reporting Standards, the International Financial Reporting Standards for Small and Medium Enterprises and the International Public Sector Accounting Standards will be translated into Azerbaijani by the Ministry of Finance and will come into force on the publication of official texts. National financial reporting standards and accounting policies will be repealed from this date.

As new standards are introduced, standards are also defined that will be used by business entities. Thus, for micro, small and medium enterprises, the Ministry of Finance sets specific rules according to which these organizations can keep records in this form or in accordance with International Financial Reporting Standards and International Financial Reporting Standards for Small and Medium Enterprises.

Large enterprises can prepare their financial statements in accordance with the International Financial Reporting Standards for small and medium-sized enterprises

or the International Financial Reporting Standards established by the Ministry of Finance (Gashenko I., 2018).

It should be noted that the Ministry of Taxes of the Republic of Azerbaijan will also study the above requirements during state financial control and tax audits. Lack of financial reporting in accordance with the requirements will result in administrative liability. Responsibility will be borne by the head of the accounting entity, the chief accountant or a legal entity or an individual providing accounting services.

3.2. Future prospects of the impact of differences between revenue/expense recognition and tax accounting on Azerbaijani companies

Despite the fact that the procedures for accounting for income and expenses are strictly regulated by law, accounting for this process requires a conscious choice of priorities: focusing on the economic function, expressed in the correlation of income and expenses in one reporting period, or on the legal function, when income and expenses are not reflected in the accounting for several reporting periods, which leads to a distortion of the reporting information on the income of investment entities for these periods.

One of the ways to solve the problem of recognition of income and expenses in construction is the availability of reliable information support for acceptance and delivery of construction products.

Regardless of the option of handing over the construction project for accounting and tax purposes, the primary accounting document will be the acceptance and transfer of work results signed by the parties, which in essence is the calculation of the cost of work performed for the reporting period. This document justifies the costs of the builder, who must keep track of the volume of work, and the time of their implementation. Based on the data of the Acceptance of Completed Works Act, a Certificate of the cost of work performed and costs is filled out, in which the work performed and costs are reflected on the basis of the contractual cost, taking into

account the total amount of work performed from the beginning of the construction of a particular object. On the basis of these primary documents, accounting of revenue, expenses for construction and installation works and their write-off, and determination of the value of fixed assets is kept (Bakker A., Berg, T. v. d. & Janssen B., 2015).

All expenses associated with the construction of the facility, which are recorded in the Journal of accounting of completed work separately for each construction object on the basis of uniform standards and prices for each structural element or type of work, are the basis for filling out the General Journal of the work performed.

As for the acceptance of the completed construction facility when it is fully ready, in this case, the determining conditions for the recognition of income in the accounting of the developer in accordance with the standards of accounting standards are:

a) the right to receive proceeds arising from a specific contract or otherwise confirmed accordingly;

b) the ability to determine the amount of revenue;

c) there is confidence that as a result of a particular operation there will be an increase in the economic benefits of the organization;

d) transfer of ownership, possession, use and orders for the acceptance of work by the customer, the provision of services;

e) the ability to determine the costs that have been or will be incurred in connection with the receipt of revenue.

According to “Accounting for Construction Contracts”, the contractor can apply two methods for determining financial results, depending on the form of determining income adopted by him.

There are two forms of determining income (IFRS, 2019):

1) “Income at the cost of the construction project”;

2) "Income at the cost of work as they are ready."

In the event that the income is determined after completion of all work at the construction site, the method of "Revenue at the cost of the construction site" is applied.

In this case, the financial result is the difference between the contractual value of the completed construction object and the cost of performing work on this object.

When applying the method “Income at the cost of works as they are ready”, the financial result of the contractor is revealed for a certain reporting period of time after the complete completion of individual works on structural elements or stages stipulated by the project. It is defined as the difference between the volume of work performed and their costs.

The scope of work is determined in the prescribed manner based on the contract value and the methods used for its calculation. The costs attributable to the work performed are determined by the direct method and (or) by calculation.

Costs are accumulated in account 203 and participate in the process of determining the financial result only after completion of work at the construction site (IFRS, 2019).

Thus, a properly organized process of initial observation in a construction organization allows one to form a reliable professional judgment on a focused perception of facts, the completeness and reliability of accounting information depend on the quality of which.

Expenses are recorded in accounts of classes 2 “Inventories”. Class 2 accounts take into account direct production costs, first collect the debit of the account, and then assign them to the production cost of production in the debit of account 203 in the order of their distribution.

Class 7 accounts (accounts 701,711,721,731) are designed to display information on the economic elements of costs. On debit, they accumulate expenses, and on credit - write off as intended.

Account 202 "Production costs" is intended for the accumulation of information on the cost of sales of finished products, goods, work performed, services rendered. It reflects the production cost of sales of finished products, works, services, the actual cost of goods sold (without trade margins).

Administrative costs include those associated with the management and organization of the enterprise. The composition of administrative expenses is determined by account 721 “Administrative expenses”. Administrative expenses include:

a) general corporate expenses (organizational expenses, expenses for holding annual meetings, hospitality expenses, etc.);

b) expenses for business trips and maintenance of the enterprise management apparatus and other administrative personnel;

c) expenses for the maintenance of fixed assets and fixed assets for administrative purposes (operating leases, property insurance, depreciation, repairs, heating, lighting, water supply, water management, security, etc.)

d) remuneration for professional services (legal, audit, property valuation); e) communication costs (postal, telegraph, telephone, telex, fax, etc.);

f) costs of resolving litigation;

g) taxes, fees and other mandatory payments prescribed by law (except taxes, fees and mandatory payments included in the production cost of products, works, services);

h) payment for settlement and cash services and other services of banks;

i) other administrative expenses.

Costs of sales - the costs associated with the sale (sale, sale) of products, goods, works, services. The composition of sales costs is determined by account 701 "Sales costs", according to which the sales costs include:

a) the cost of packaging materials for packing finished products in warehouses;

b) the cost of repairing containers for storing products;

c) remuneration and commissions to sellers, sales agents and employees of sales units;

d) expenses for advertising and market research (marketing);

e) the costs of pre-sale preparation of goods;

f) the costs of business trips of employees engaged in marketing; there are expenses for the maintenance of fixed assets related to the sale of products, goods, works, services (operational rent, insurance, depreciation, repairs, heating, lighting, security);

g) the cost of transportation, transshipment and insurance of finished products (goods), freight forwarding and other services;

c) the costs of warranty repairs and warranty services;

i) other expenses associated with the sale of products, goods, works, services.

Distribution costs do not include expenses that, according to the supply contract, are made by the supplier for a fee (packaging cost, selling price of delivery of values to the consumer, etc.). Other operating expenses include:

- expenses for research and development;

- the cost of sales of foreign currency;

- the cost of inventories sold, for accounting purposes, consists of their carrying value and costs associated with their implementation;

- the amount of bad receivables and deductions for doubtful debts;

- losses from operating exchange rate differences;

- losses from depreciation of stocks;

- shortages and losses from damage to values;

- recognized fines, interest, penalty;

- expenses for the maintenance of social and cultural facilities;

- other operating expenses.

Other expenses include research and development costs, cost of sold foreign currency, cost of sold inventories, doubtful and bad debts, losses from operating

foreign exchange differences, losses from depreciation of inventories, shortages and losses from damage to property, fines, housing and utility services , children's to school facilities, holiday homes, resorts and other health and cultural facilities.

Financial expenses include expenses related to the payment of interest on the use of loans received, on issued bonds, financial leases and other expenses of the enterprise related to raising borrowed capital.

Accounting for the financial activities of the enterprise is carried out on account 751 "Financial expenses". The debit of account 751 reflects the amount of recognized expenses, the credit - write-off to "Financial Results". According to the "Income Tax" account, income taxes are recognized as expenses and are recorded on account 901 "Income Tax".

Extraordinary event - an event or operation that differs from the ordinary activities of the enterprise, and is not expected to be repeated periodically or in each subsequent period.

The costs of emergency events include (IFRS, 2019):

a) direct costs resulting from these events;

b) expenses for the implementation of measures related to the prevention and elimination of the consequences of emergency events.

Extraordinary expenses are recorded on account 761 "Extraordinary expenses". The debit of account 761 reflects the amount of recognized expenses on the loan of the asset account, and for the loan - write-off to financial results.

Recognition of income and expenses. When the result of the construction contract can be reliably estimated, the revenue and costs thereof should be recognized as revenue and expenses, respectively, by reference to the stage of completion of work under the construction contract at the reporting date. The expected loss under the construction contract should be recognized immediately as an expense.

Contracts are broken down into the following stages:

1) determination of the costs of the construction contract incurred to perform work on the date of the report in proportion to the estimated total costs of the construction contract (the method is called "based on costs");

2) monitoring the amount of work performed by an expert method (the method is called “revenue-based”);

3) the actual calculation of the physical share of work performed under the construction contract.

Recognition of income and expenses by determining the percentage of completion is called the percentage of completion method.

With the method of completing work on the basis of income, the cost of work accepted by the customer on the reporting date is compared with the price of the contract, and with the method based on costs, the costs incurred at the date of the report are compared with the total costs of the contract.

If the total costs of the contract exceed the total revenue under it, the expected loss should immediately be recognized as an expense and should be immediately written off to the costs.

To determine revenue under a contract, you must determine the type of contract. Information disclosure requirements The company must disclose:

- the amount of revenue under the contract recognized as revenue over the period;

- methods used to determine revenue from the contract;

- methods used to determine the stage of implementation of contracts in progress.

For unfinished contracts, the company must disclose the total costs incurred and recognized gains (net of recognized losses) at the current date, the amount of advances received and the amount of deductions.

When accounting for construction contracts, a number of problems arise related to the peculiarities of the construction industry. Moreover, given that the construction

work requires several years to complete, the reporting period is also delayed by several years and this creates certain difficulties in accounting.

The range of issues associated with the application of accounting rules in different enterprises differs from each other. For example, some enterprises prefer the earliest recognition of profits, while others, on the contrary, try to delay recognition of profits. Due to the fact that it is impossible to determine the actual profit made under construction contracts, during the term of the contract the recognition of profit can be based on estimated indicators. Enterprises may use various methods to conduct this assessment. For example, individual enterprises calculate the cost of the completed part of the work relative to the total volume of work, others calculate the income after all the work has been completed, some recognize income at the cost of invoices received or on payments paid by customers.

Construction contracts Construction contracts are contracts concluded for the construction of individual facilities and for the construction of a complex of facilities that are close in design, technology and function, as well as for purpose or use. One of the important properties of construction contracts is that the start and end dates of construction occur in different reporting periods. Construction contracts are usually very complex.

Stable price agreements are construction contracts (often including articles providing for cost increases) based on stable prices or the contractor’s consent for a stable payment on commodity units.

These contracts reflect the full value of the building. Such contracts are usually beneficial to sellers because the contractor is responsible for controlling costs. If the costs of the contractor increase, this does not affect the contract prices. In case of excess of the contractor's expenses over the agreed prices, it is possible to talk about losses.

In case of unstable prices, contracts are concluded on the basis of “expenses plus”.

An “expenses plus” agreement is a construction agreement that provides for reimbursement to the contractor of the expenses stipulated by the agreement or determined in other ways, plus amounts as a percentage of these expenses or the amount of stable fees.

Amounts recoverable under these agreements are related to expenses. For the amount of expenses incurred, the so-called profit of the contractor in the form of interest. This type of contract is beneficial to the contractor; they are not interested in controlling costs, and at the same time, profit is ensured.

Contract income

Article 13 of the standard defines the elements of income under a construction contract. According to article 14 of the standard, the income from a construction contract is usually considered to be a fair amount for the amounts received or estimated. At the same time, the amount of income may increase or decrease with the transition from one reporting period to another. The income under the contract consists of the following (IFRS, 2019):

(a) the initial amount of income agreed upon under the contract; and

(b) discrepancies, claims, and incentive payments that meet the following criteria:

(c) the estimated income from them; and

(d) with reliable assessment.

Contractual construction costs

Article 18 of the standard defines the main components of construction costs under the contract.

The costs of the contract consist of the following:

(a) expenses directly attributable to a specific contract;

(b) expenses attributed to the activity provided for in the contract and at the same time to the specific contract; and

(c) other expenses stipulated by the terms of the contract and requiring payment by the customer in a special manner.

Article 19 of the standard defines the main components of construction costs under a specific contract. These costs consist of the following elements:

(a) costs associated with monitoring the construction site, as well as the salaries of employees;

(b) the cost of materials used in construction;

(c) depreciation of machinery and equipment used under the contract;

(d) expenses related to the delivery to the construction site and the export of machinery, equipment, goods and materials;

(e) the cost of renting machinery and equipment;

(e) costs directly related to design work and technical support;

(g) the estimated costs of the work arising from the warranty, including the costs of correcting errors, as well as the estimated costs of the warranties; and

(h) claims of third parties.

Article 20 of the standard defines the costs attributable to the activities stipulated by the construction contract and specific contracts:

(a) insurance payments;

(b) expenses related to technical support and architectural work not related to a specific contract; and

(c) additional (overhead) construction costs.

The distribution of costs corresponds to the normal level of construction activity.

Insurance costs can be allocated according to the cost stipulated by the construction contract, and the amount of expenses for the maintenance of workers by the number of employees.

Article 21 of this standard defines the costs that are not related to the activities provided for by the construction contract and specific contracts:

(a) general administrative expenses for which reimbursement is not provided for in the contract;

(b) selling expenses;

(c) research and development costs, the reimbursement of which is not provided for in the contract; and

(d) depreciation of idle machinery and equipment not used by a specific contract.

So, articles 18-21 of this standard can be summarized as follows:

Cost Items	Included	Excluded
Employee costs	X	
The cost of materials used in construction	X	
Construction overhead	X	
Insurance (including insurance assigned to the contract and distribution of the total amount of insurance payments)	X	
General administrative and selling expenses		X*
Depreciation of machinery and equipment used under the contract	X	
Depreciation of machinery and equipment not used under a specific contract		X
Costs of delivery and removal of structures, equipment and materials to the construction site	X	
The cost of renting machinery and equipment	X	
Costs of restoration and improvement of the territory at the end of the contract	X	
Research and development costs		X*
Debt expenses (must comply with the requirements of Article 23 of IAS)	X	
Technical assistance and construction costs directly attributable to the contract	X	
Estimated cost of correcting	X	

errors, as well as arising from insurance obligations and expected work		
Third Party Claims	X	
* except in cases where compensation is not provided for by the contract		

According to Article 23 of this standard, the costs of the contract can be calculated only after signing this contract. So, all expenses incurred before signing the contract (notary, accounting, research costs) cannot be attributed to the costs of the contract.

Recognition of income and expenses under a construction contract

In Art. 23 of this Standard defines the general accounting requirements for recognition of income and expenses. The income and expenses of the contract shall be recognized as follows (Beardsley R., 2017):

1. with a reliable assessment of the results of the construction contract;

2. according to the stage of completion of work under the contract at the reporting date;

3. The expected loss under the construction contract should immediately be recognized as an expense.

The rule of checking the reliability of evaluating the results of a construction contract differs under stable price agreements and “expenses plus”. Based on this construction contract is distributed under two contracts.

According to Art. 24 standard contract at stable prices can be reliably evaluated only in the following cases:

(a) the total amount of contractual income can be reliably calculated;

(b) upon probabilistic entry into the enterprise of economic effects under the contract;

(c) in the reliable assessment of the costs required to complete the contract, as well as the stage of completion of work under the contract at the reporting date; and

(d) when accurately determining and evaluating contractual expenses to compare actual contractual costs incurred with previous estimates.

If one of these conditions is not observed, contractual income cannot be recognized sequentially. According to Art. 25 of the standard, the contract “expenses plus” can be reliably evaluated only in the following cases:

(a) upon probabilistic entry into the enterprise of economic effects under the contract; and

(b) in the precise determination and evaluation of contract costs, regardless of the reimbursement of their amount.

Clause (b) noted in the “expenses plus” agreement is very important because the income under the agreement is based on the expenses under the agreement, and if the expenses are uncertain, then, accordingly, the income will also be uncertain.

Disclosure The following points should be disclosed in the notes to the financial statements:

(a) the total amount of expenses incurred at the reporting date and recognized profit (minus recognized losses);

(b) the amount of advances received;

(c) the amount of deductions (deductions is the sum of interim accounts not paid without fulfilling such conditions stipulated in the contract or eliminating deficiencies. The amount of deductions and their conditions is specified in the contract accordingly).

(d) the total amount, as an asset, provided to be received from customers for work under a contract. To calculate this amount, it is required to subtract the amount of recognized expenses and interim accounts from the expenses incurred plus recognized profits.

(e) the total amount, as an obligation, provided for payment to customers of contractual work. To calculate this amount, it is required to subtract the amount of

recognized expenses and interim accounts from the expenses incurred plus recognized profits.

(e) other contingent assets and contingent liabilities.

The contractor completed the operations foreseen in the first year. All expenses incurred under the agreement by them are paid in cash and all invoices and advance payments are also received in cash. Expenses under contracts B, C and E were received to fulfill the contract, but include material costs not used at the reporting date. Under contracts B, C and E, advance payments were received from customers.

CONCLUSIONS AND RECOMMENDATIONS

The organization's expenses represent the basic category of accounting, are one of the main elements of financial and tax reporting and serve as the basis for management decisions. In this regard, the content of expenses as a specific object of accounting is disclosed in the work. The study of scientific ideas about the nature and content of expenses showed that new definitions of expenses that appeared at the stage of accounting reform contain a number of contradictions and are not built into a clear system. To resolve the identified contradictions in the work on the basis of a systematic approach, it was proposed, firstly, to trace the interpretation of this category in various subsystems: financial, managerial and tax accounting, and secondly, to consider expenses in the following areas: the concept of expenses, classification, recognition and evaluation.

Considering that the concept of "expenses" as an important category of accounting began to be considered relatively recently, the work summarized the current experience of Azerbaijani and foreign scientists on this issue and established differences between the concepts of "costs", "costs", "costs" , "Cost price." For this, a systematization of the conceptual apparatus was carried out according to more than 60 domestic and foreign sources. Each category is considered in chronological order: first of all, the concept was interpreted in accordance with normative documents, secondly, the conceptual apparatus developed by Azerbaijani (Soviet) economists was used, and thirdly, definitions proposed by foreign researchers were analyzed.

Considering the concept of expenses in tax accounting, it should be noted that here has developed its own definition of expenses, which lawmakers interpret exclusively for their fiscal interests, not fully taking into account their economic nature, as well as the experience gained over decades by domestic and international accounting. Expenses in tax accounting are identified with costs, and the emphasis is placed only on their economic feasibility and documentary evidence.

In management accounting, the concepts of costs and costs are often identified. The paper considers the difference between these categories and the comparative characteristics of expenses in financial, managerial and tax accounting. Attaching particular importance to the issues of terminology that are key at the stage of reforming the Azerbaijan accounting system, the work substantiates and argues for the need to reflect the definition of costs and expenses in regulatory documents, limiting the scope of these categories and providing the possibility of their unambiguous qualification.

The identified shortcomings and contradictions in the interpretation of the concepts of "costs" and "costs" necessitated the justification of the facts of economic life, leading to the formation of costs. An important theoretical prerequisite for this was the separation of the facts of economic life by the degree of influence on the balance sheet currency on modifications and permutations. Business operations that form expenses were considered both in the static and in the dynamic interpretation of the balance sheet. It was revealed that it is the dynamic model that most adequately forms the category of expenses. Carrying out such a study gave grounds to assert that there are 16 basic types of facts of economic life that relate to modifications of the first and third types and permutations of the second type and lead to costs.

International financial reporting standards have made a significant contribution to improving and harmonizing financial reporting worldwide. The application of IFRS enhances the transparency of financial information about market participants and promotes the unification of economies of different countries.

At present, when preparing financial statements in accordance with international standards, organizations can conduct two types of accounting (conversion) in parallel or, much more often, transform financial statements prepared in accordance with Russian accounting standards into IFRS. During the study, criteria were developed for choosing the transition of the Azerbaijan Construction Organization to international financial reporting standards. When choosing the method of transition to international

financial reporting standards, the management of the construction organization should remember that the proposed methodology for the transition of the organization to the presentation of financial information in accordance with IFRS should be analyzed and processed, if necessary, depending on the level of knowledge and experience of the employees who carry out the transformation or conversion.

When transitioning Azerbaijan construction organizations to international financial reporting standards, it is necessary to carefully study the differences in the organization of accounting in accordance with the Azerbaijan accounting standards and international financial reporting standards.

The application of IFRS in Azerbaijan construction organizations requires the solution of a number of organizational and technical issues, the unresolved of which "slows down and makes it difficult to transfer accounting to IFRS. The role of the state in the process of transition of Azerbaijan construction organizations to international financial reporting standards should be the most active. It should not be reduced only to the adoption of relevant legislative acts, it is necessary to provide practical support to construction organizations that are moving to the application of IFRS, to resolve issues of training and methodological support for the transition.

The Azerbaijani financial market cannot effectively develop separately from the international market. Due to the increased transparency of financial statements of construction companies, investments will become less risky for investors. This will be a very important step in establishing mutual trust between Azerbaijan and other countries. As a result of the application of IFRS, Azerbaijani construction companies will become full partners in the global construction market and will effectively use the opportunities offered by international capital markets.

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