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The Role of Tax Auditing in Mitigating the Negative Effects of Creative Accounting

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Abstract:

This study aimed to explore creative accounting in terms of its concept, origins, methods employed, and the motivations of management to use it. It was found that corporate accountants often attempt to reduce the tax base in order to lower the tax burden on the taxpayer. The study also aimed to examine the impact of tax auditing in curbing the practices of creative accounting.

The study concluded that tax auditing plays a significant role in limiting creative accounting practices by uncovering various legal loopholes exploited by accountants. Ultimately, tax auditing reveals the true tax base of the institution and enforces tax payment accurately.

Keywords: Creative accounting; Tax base; Tax burden; Tax auditing; Legal loopholes.

Jel Classification Codes: XN1, XN2.

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1. Introduction

Financial accounting serves as a mirror reflecting the status of any institution through the presentation of its financial statements. Due to the elements of choice and flexibility in the regulations governing these statements, some accounting experts have exploited them for the benefit of management or owners, a practice known as creative accounting. Since accounting is considered a branch of knowledge within the social sciences, incorporating behavioral and ethical aspects, it is crucial for those responsible for accounting to observe these dimensions. They must avoid accounting tools and techniques that mislead financial statement users by presenting a particular situation that serves specific interests. This manipulation of accounting data exploits certain loopholes and treatments, leading to financial outcomes that do not reflect the true reality, often in an attempt to improve the financial.

2. The Theoretical Context of Creative Accounting

Creative accounting is associated with accounting problems faced by institutions, and attempts to find solutions, whether these solutions are seen as innovative or deceptive. Therefore, in this section, we aim to address the essence of creative accounting in the first subsection, the motives behind management's use of creative accounting in the second subsection, and the methods of creative accounting in the third subsection.

2.1 The Essence of Creative Accounting (Definition, Origins, Characteristics)

2.1.1 Definition of Creative Accounting

The definitions of creative accounting vary depending on the perspectives of researchers in the field. Some of the definitions include:

- The use of novel methods, techniques, or procedures by a creative accountant that can be employed to interpret, analyze, or solve an accounting problem faced by management, or to manipulate financial figures and beautify data (Zergouad & Shaabani, 2019, p. 406).
- It is defined as unethical practices in the selection of accounting estimates and policies, allowing opportunities for manipulation and fraud, resulting in inaccurate and misleading financial data (Sahib, 2016, p. 377).
- Creative accounting is the deliberate use of aggressive, deceptive accounting techniques to present an improved image of the company. While these practices may be legal, they violate the spirit of accounting and mislead users of financial statements (Khaneja & Bhargava, 2016/2017, p. 46).
- It is the practice of income smoothing, where management takes steps to accumulate profits during strong financial periods to defer them for use in economically challenging years, or vice versa (Trizanti, 2016, p. 52).

Based on the above definitions, creative accounting can be defined as a planned process carried out by accounting experts who exploit legal loopholes and the flexibility of accounting principles and standards to influence the institution's financial results, primarily to serve management's personal goals.

2.1.2 Origins

Some researchers believe that the emergence of what is known as creative accounting dates back to the 1980s. During this period, the term creative, innovative, or fraudulent accounting, as some refer to it, gained significant attention from many accounting researchers and auditors. Interest in the concept heightened particularly after the events of 2002, which saw the bankruptcy and collapse of four globally recognized American companies: Enron (energy), WorldCom (telecommunications), Xerox (copying devices), and Merck (pharmaceuticals). These companies were either directly complicit with their auditors, particularly the well-known U.S. auditing firm Arthur Andersen, or suffered from gross negligence on the part of their auditors. These incidents led to falsification and distortion of financial results and positions, resulting in significant misrepresentation of their published financial information. Consequently, their stock prices plummeted, causing massive losses to shareholders and creditors alike.

2.1.3 Characteristics of Creative Accounting

Creative accounting is characterized by several key traits, including (Mahmoud & Murad, 2017, pp. 134-135):

- It is a form of manipulation and fraud within the accounting and auditing profession.
- It is a planned process undertaken by the institution's management to achieve its specific objectives.
- It aims to arrive at a particular net profit figure or financial result that benefits the company's management in the short term.
- It is carried out by accounting experts within the framework of selecting between different accounting principles and standards.
- It affects the credibility and reliability of the financial data in the statements.
- Its environment is marked by manipulation of account figures, fraud, distortion, and sleight-of-hand techniques in accounting practices.

2.2 Motives for Management's Use of Creative Accounting

Management's motives for employing creative accounting vary according to the circumstances and factors that provide flexibility and freedom of choice among alternatives. The key motives include:

- Tax evasion.
- Securing necessary funding.
- Professional classification.
- Weak external auditing or collusion with management, which leads to manipulation of financial statements.
- Positively influencing the institution's reputation in the market.
- Gaining the trust of banks to increase borrowing capacity and obtain needed financing.

2.3 Methods of Creative Accounting

To achieve the objectives of creative accounting, certain procedures and techniques are employed. Accounting studies have outlined several methods in this field, including the following (Neqmoush, 2019, pp. 714-715):

2.3.1 Income Statement

This can be divided into two parts:

A. Revenues

Revenue manipulation can occur in several ways:

- Recording revenue prematurely, even when the sale process remains uncertain. According to accounting principles, income is recognized after the exchange of benefits is complete. In this method, income is recorded in the accounting books before the actual sale is finalized or the exchange of benefits has been completed in reality.
- Recording false revenue, which involves the recognition of fictitious or fake revenues.
- Increasing revenues through a one-time gain.
- Shifting current revenues to subsequent accounting periods.

B. Expenses

Expense manipulation can occur as follows:

- Shifting current expenses to previous or subsequent accounting periods.
- Moving future expenses to the current accounting period.
- Recording false expenses, involving the recognition of fictitious or fake expenses.
- Recording purchase expenses prematurely, before the purchase process is finalized or the exchange of benefits has occurred.
- Recording accrued expenses before the payment or disbursement takes place.

2.3.2 Balance Sheet

The balance sheet can be manipulated in several ways:

- Intangible Assets: Overvaluing asset items, particularly intangible assets.
- Tangible Assets: Failing to adhere to the historical cost principle when determining the values listed on the balance sheet.
- Long-term Investments: Changing the accounting methods used for long-term investments, such as switching from the cost method to the equity method.
- Marketable Investments: Manipulating market prices used in valuing the securities portfolio.
- Shareholders' Equity: Reducing shareholders' equity while increasing reserves.
- Inventory: Manipulating inventory accounts by including obsolete or slow-moving items in inventory reports, and altering the prices at which they are valued.

2.3.3 Cash Flow Statement

The accountant may classify operating expenses as investment or financing expenses, and vice versa. Although these practices do not change the final values, they distort the categorization of expenses.

2.3.4 Statement of Changes in Equity

All elements in this statement are vulnerable to creative accounting practices, such as making fictitious changes in the increase or decrease of paid-up capital, earned capital, or calculated capital. These practices also extend to re-evaluating previous errors, losses from past decisions, and previous foreign currency balances.

Additionally, some behaviors and actions management may engage in with respect to creative accounting include (Awadi, Merawi, & Awadi, 2019, pp. 31-31):

- Declaring fictitious profits to entice shareholders into increasing their investment in the company.
- Misleading suppliers about the company's solvency and ability to pay in order to increase purchases without immediate payment.
- Deceiving customers with false guarantees to attract them.
- Offering bribes and commissions to journalists to encourage the dissemination of positive news about the company and avoid bad publicity.
- Misleading the public with fictitious projects and accomplishments financed by the company to reduce profit margins, thus lowering taxable income.

3. The Technical and Conceptual Framework of the Tax Base

The tax base is regarded as a technical framework for taxation, involving the determination of procedures and technical conditions related to the imposition and collection of taxes according to applicable tax legislation. Therefore, in the first subsection, we will address the definition of the tax base, and in the second subsection, we will discuss the methods for determining the tax base.

3.1 The Concept of the Tax Base

The tax base refers to the material, element, or object upon which a tax is imposed. The tax base may pertain to a person, property, capital, income, or goods. It plays a critical role in a country's tax policy, as the fairness and adequacy of tax revenue depend on the proper selection of the tax base (Sahib, 2016, p. 381).

In Algerian law, the tax base is defined as the material, asset, or person subject to taxation, serving as the source from which the state levies various taxes.

Based on these definitions, the tax base can be understood as the material or income on which a tax is imposed, or, in other words, the entity or item subject to taxation.

3.2 Methods of Determining the Tax Base

There are two main methods for determining the tax base: the estimation method by the administration and the direct estimation method. These are detailed as follows (Bouzida, 2007, pp. 31-34):

3.2.1 Estimation by the Administration

- Estimation based on external indicators.
- Lump-sum estimation.

3.2.2 Direct Estimation

- Estimation by the taxpayer.
- Third-party declaration.

4. The Tax Base in Light of Creative Accounting Practices

There is no doubt that creative accounting practices, despite their various motives, primarily aim to influence and reduce the tax base, a practice commonly referred to as tax manipulation. Therefore, we address in the first subsection the concept of tax manipulation, and in the second subsection, the reasons for tax manipulation.

4.1 The Concept of Tax Manipulation (Definition, Types, Causes)

4.1.1 Definition of Tax Manipulation

Many view taxes as an additional burden added to the overall responsibilities they bear, prompting them to try to escape this burden by any means possible.

Tax Evasion in public finance is defined as the partial or complete avoidance of an individual's obligation to pay taxes after the taxable event has occurred (Alimat, 2013).

Economists and tax law scholars have also discussed tax evasion in terms of its economic impact on the public treasury. Some define it as the failure of a taxpayer to pay the due tax on time or avoiding payment altogether, whether through legal or illegal methods.

Based on these definitions, tax manipulation can be understood as the evasion of tax payment through unlawful methods or by exploiting loopholes without violating existing tax laws explicitly.

4.1.2 Types of Tax Manipulation

There are several types of tax manipulation, including:

A. Tax Evasion

Opinions vary regarding the concept of tax evasion, due to the different causes and motives behind it. Tax evasion is defined as (Shbaiki & Kara, 2004, p. 164):

An indirect violation of tax laws through specific methods that allow the taxpayer to avoid paying part or all of the tax.

To achieve tax evasion, taxpayers may use various legal or illegal methods. Based on this, two forms of tax evasion can be distinguished:

- Tax evasion without violating tax law, commonly known as tax avoidance.
- Tax evasion by violating tax law, referred to as tax fraud.

B. Tax Avoidance

Tax avoidance, also known as legal tax evasion, refers to the act of avoiding tax payment without violating tax regulations. It occurs within a legal framework that allows the taxpayer to avoid paying taxes without breaching the law. The complexity of the tax system and poorly drafted laws are the two main factors enabling taxpayers to exploit loopholes that allow them to avoid paying taxes.

Although the taxpayer may act with malicious intent, they are not legally punished for it, as stipulated in Article 01 of the Penal Code: "There is no crime, penalty, or security measure without a law." Nonetheless, tax avoidance poses a threat to the state's

tax revenues. Therefore, lawmakers should address this issue by closing legal loopholes, drafting clear and simple regulations, and granting exemptions or options only through a well-considered and comprehensive plan.

Some of the most common forms of tax avoidance include:

- Avoiding customs taxes by refraining from importing a particular product.
- Discontinuing a production activity that is subject to high taxes, often due to economic or social considerations. For example, individuals may reduce consumption of a specific product or encourage the production of a substitute to protect public interests.
- Evading progressive income taxes by splitting a parent company into legally independent subsidiaries, taking advantage of provisions in commercial law. This type of avoidance is common among individuals.

It is important to note that tax avoidance does not constitute true tax evasion, as there is no material realization of the taxable event. Instead, taxpayers seek to use methods that reduce their tax burden within the limits of the law.

C. Tax Fraud

Tax fraud, also known as illegal tax evasion, refers to avoiding tax payment through unlawful methods that directly violate tax law. It involves evading taxes by presenting false information or interpreting the law in a misleading way. In doing so, the taxpayer commits financial crimes punishable by law. There are several forms of tax fraud, including (Murad, 2010, p. 163):

- Smuggling imported goods by not declaring them to customs authorities, thus avoiding the payment of customs duties.
- Filing a false tax declaration with the tax authorities, where the taxpayer reports lower income or the value of imported goods as less than their actual worth, resulting in a lower tax liability.
- Exaggerating deductible expenses, which reduces the taxable income and, consequently, the amount of tax owed.
- Hiding or transferring assets to evade tax liability, making it difficult for the tax authorities to collect what is owed.

Tax fraud is a serious violation of tax law and involves the deliberate manipulation of financial information to escape tax obligations, often leading to significant penalties and legal consequences.

5. The Impact of Tax Auditing in Uncovering Creative Accounting Techniques Affecting the Tax Base

The tax system of any country works to combat creative accounting methods and practices. Tax auditing plays a key role in detecting such practices, enabling early prevention of tax evasion or rectifying it by reclaiming hidden revenues and imposing penalties.

5.1 Introduction to the Institution Subject to Tax Auditing

5.1.1 Introduction to the Institution

According to commercial register number 0400/28-2836094, the institution is a sole proprietorship specializing in real estate works, located at Lot 401, Mohamed Boudiaf, Unit No. 1, Berhoum Municipality, M'sila Province, within the administrative jurisdiction of the Magra Tax Inspection under subject code 28120941461 and tax number 197728120008631. The institution's file is registered under the preferential system of the National Agency for Investment Development (ANDI).

5.1.2 Tax Liability of the Institution and Accounting Records

A. Direct Taxes

The taxpayer is subject to income tax on total gross income from professional profits in accordance with Articles 1, 2, 3, 85, 104, and 190 bis of the Law on Direct Taxes and Similar Duties. Additionally, the taxpayer is liable for the turnover tax, as stipulated in Articles 217, 219, and 357 of the same law. Since the taxpayer's business employs workers, it is also subject to the income tax on salaries and wages, as per Articles 66 to 75 of the aforementioned law.

B. Turnover Tax

The taxpayer's business is also mandatorily subject to the value-added tax (VAT) due to the nature of its activities, in accordance with Articles 4 and 14, and the applicable VAT rate under Articles 21 and 23 of the Law on Turnover Tax. The institution has the right to deduct VAT on purchases as outlined in Articles 29, 30, 42, and subsequent provisions of the same law.

5.1.3 Accounting Records Maintained by the Taxpayer

- Journal: Certified and signed by the President of the Magra Court on 14/02/2004, containing 47 pages.
- Inventory Book: Certified and signed by the President of the Magra Court on 14/02/2004, containing 46 pages.
- Wages Book: Certified and signed by the President of the Magra Court on 14/02/2004, containing 46 pages.
- Auxiliary Ledgers: These ledgers are maintained electronically and include the purchase ledger, sales ledger, bank ledger, cash ledger, and various transactions ledger.

5.2 The Impact of Tax Auditing on Fixed Assets

Through the examination of tangible fixed assets recorded and declared in the accounting records and the institution's assets, it was found that equipment (a utility vehicle) had been disposed of at the end of 2020, as per the taxpayer's statement. However, the disposal was not declared. In accordance with Articles 172 and 173 of the Law on Direct Taxes and Similar Duties, the undeclared capital gain was adjusted as follows:

Table 1. Undeclared Capital Gain

Description / Year	2020
Investment acquisition cost	1,630,000
Depreciation (accumulated)	570,500
Net accounting value	1,059,500
Sale price	1,250,000
Capital gain	190,500
30% reduction	57,150
70% taxable gain	133,350

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing.

Note: The utility vehicle was held for less than three years, meaning the capital gains are classified as short-term gains.

5.3 The Impact of Tax Auditing on Expenses

5.3.1 Study of Depreciation

Through an examination of the depreciation of raw materials and their comparison with the declared data in the reconciliation reports for each year, the following observations were made:

Table 2. Rejected Expenses Related to Equipment Depreciation and Electrical Supplies

Raw Material	2017	
Equipment and electrical supplies	Opening Inventory	0
	Purchases	1,260,430
	Closing Inventory	0
	Consumption	1,260,430
	Reconciliation Report Consumption	625,000
	Difference	635,430

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing.

Table 3. Rejected Expenses Related to Tile (33×33) Consumption

Raw Material	2018	
Tile (33×33)	Opening Inventory	0
	Purchases (m ²)	25,401
	Closing Inventory	0

	Consumption (m ²)	25,401
	Reconciliation Report Consumption (m ²)	21,305
	Difference in Quantity (m ²)	4,096
	Loss Percentage	15%
	Difference in Quantity after Loss (m ²)	3,482
	Price per m ²	280
	Excess Amount	974,848

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing.

Table 4. Rejected Expenses Related to Cement Pipe Consumption

Raw Material	2020	
Cement Pipes (Diameter 500/300)	Opening Inventory	0
	Purchases	756,439
	Closing Inventory	82,600
	Consumption	673,839
	Reconciliation Report Consumption	261,600
	Difference in Quantity	412,239

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing.

Table 5. Rejected Expenses Related to Iron Manhole Cover Consumption

Raw Material	2019	
Iron Manhole Covers (TAMPON)	Opening Inventory (units)	0
	Purchases (units)	757
	Closing Inventory (units)	0
	Consumption (units)	757
	Reconciliation Report Consumption (units)	630
	Difference in Quantity (units)	127
	Price per Unit (DA)	6,999
	Price per m ² (DA)	280
	Excess Amount (DA)	888,834

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing.

5.3.2 Study of Other Expenses - Other Fines

The consolidation of this expense was carried out in accordance with the provisions of Article 141, Paragraph 6 of the Law on Direct Taxes and Similar Duties. This legal provision pertains to the handling of fines and other related expenses under tax law regulations.

Table 6. Study of Other Expenses - Other Fines

Description / Year	2020	2019	2018	Reason for Rejection
Deducted Expenses	150,782	9,400	30,926	Deducted Expenses
Actual Expenses	0	-	0	Actual Expenses
Difference	150,782	9,400	30,926	/

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing.

5.4 The Impact of Tax Auditing on Turnover

In reviewing the turnover, reliance was placed on bank statements for receipts, work progress reports for invoicing, the information available in the tax file, as well as the correspondence carried out during the investigation. The movement of bank statements approved by the taxpayer, which were obtained from the respective banking agencies, was also tracked. This approach helped ensure that all financial movements related to the company's operations were properly accounted for and verified in alignment with the company's declared turnover.

5.4.1 The Impact of Tax Auditing on Invoiced Turnover

Table 7. The Impact of Tax Auditing on Invoiced Turnover

Description / Year	2020	2019	2018	2017
Extracted Invoiced Turnover	566,013,405	90,094,824	144,588,135	30,014,940
Declared Turnover (TCR)	566,013,405	90,094,824	144,588,135	30,014,940
Difference	0	0	0	0

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing.

5.4.2 The Impact of Tax Auditing on Received Turnover

Table 8. The Impact of Tax Auditing on Received Turnover

Description / Year	2017	2018	2019	2020
Turnover Extracted (9%)	8,482,000	93,043,485	24,483,270	9,567,700
Declared Turnover G50 (9%)	8,482,000	93,043,485	24,483,270	9,567,700
Difference (9%)	0	0	0	0
Turnover Extracted (19%)	16,985,813	56,025,750	64,188,960	49,504,700
Declared Turnover G50 (19%)	16,814,890	56,025,750	64,003,440	49,504,700
Difference (19%)	170,923	0	185,250	0
Total Extracted Turnover	25,467,813	149,069,235	88,672,230	59,072,400
Total Declared Turnover	25,296,890	149,069,235	88,486,710	59,072,400
Difference in Total Turnover	170,923	0	185,249	0

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing.

5.4.2 Undeclared Receipts

These discrepancies represent receipts that were not declared in the monthly G50 declarations. The following table illustrates these differences, based on the examination of bank statements and their reconciliation with the monthly declarations:

Table 9. Undeclared Receipts

Date of Receipt	Bank Branch	Amount Including Taxes (DA)	Amount Excluding Taxes (DA)
07-09-2019	BDL/MSILA	216,742	185,250
30-06-2019	BDL/MSILA	199,980	170,923

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing.

6. Recalculation of Taxes, Fees, and Penalties

6.1 Recalculation of the Professional Activity Tax (TAP)

6.1.1 Recovery of the TAP Reduction for the Period from January to June

In 2018, receipts for the months of January, February, March, April, May, and June were declared in the G50 monthly declarations for November and December. The taxpayer benefited from the 25% reduction in the TAP, as specified in Article 03 of the 2018 Finance Law, which amended Article 222 of the Law on Direct Taxes and Similar Duties.

For the receipts from February, March, April, May, June, and July, the full tax applies, as these amounts do not qualify for the reduction. The following table shows the receipts and their dates according to the bank statements from the Algerian Popular Credit Bank.

Table 10. Bank Statement - Algerian Popular Credit Bank

Date of Receipt	Amount Including Tax (DA)	Tax Rate	Amount Excluding Tax (DA)
14-01-2018	3,050,689	9%	2,776,127
22-01-2018	2,947,850	9%	2,682,544
23-02-2018	4,808,580	9%	4,375,808
02-03-2018	20,430,448	9%	18,594,984
08-03-2018	4,957,810	9%	4,511,607
10-04-2018	2,831,810	19%	2,293,766
26-04-2018	10,804,786	19%	8,751,877
28-04-2018	2,179,260	9%	1,983,127
26-05-2018	7,891,580	19%	6,392,180
03-06-2018	5,356,026	19%	4,338,381
Total	65,262,438	-	56,700,401

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing.

Table 11. Bank Statement - Local Development Bank

Date of Receipt	Amount Including Tax (DA)	Tax Rate	Amount Excluding Tax (DA)
07-01-2018	10,417,720	9%	9,480,125
15-04-2018	9,217,330	9%	8,387,770
26-05-2018	549,315	19%	444,945
18-06-2018	5,984,314	9%	5,445,726
25-06-2018	10,606,050	19%	8,590,900
06-07-2018	2,831,810	19%	2,293,766

Total	39,606,539	-	34,643,232
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Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing

6.1.2 Calculation of the Professional Activity Tax (TAP) on Turnover Discrepancies

Table 12. Recalculation of Professional Activity Tax (TAP)

Statement/Years	2017	2018	2019	2020
Extracted Declared Turnover	25,467,813	149,069,235	88,671,959	59,072,400
G50 Declared Turnover	25,296,890	149,069,235	88,486,710	59,072,400
Non-Reduced Amount (25%)	-	23,685,910	-	-
Difference	170,923	23,685,911	185,249	-
TAP Rate	2%	2%	2%	2%
TAP Amount		3,418	473,718	3,705
Penalty Rate	10%	25%	10%	10%
Penalty Amount		342	118,430	370
Total Penalty	3,760	592,148	4,075	-

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing

Given the nature of the institution's activities, the invoiced turnover for the period under review will be subject to TAP at a rate of 2%, as outlined in Article 217 of the Law on Direct Taxes and Similar Duties, for the period from 02/01/2017 to 31/12/2020. The undeclared portion of the turnover will be subject to financial penalties in accordance with Article 139 of the Law on Direct Taxes and Similar Duties.

A discrepancy between the extracted and declared turnover was observed for three consecutive years, while no discrepancy was found in the last year. This indicates manipulation in tax declarations, which subjects the taxpayer to specific tax penalties as defined by the tax authorities in Article 193, Paragraph 01 of the Law on Direct Taxes and Similar Duties, as reflected in the table above.

6.2 Recalculation of the Total Income Tax

After the tax administration rejected the taxpayer's accounting records, the total income tax is recalculated according to the following table:

Table 14. Re-establishment of Total Income Tax

Statement/Years	2017	2020	2019	2018
Turnover Discrepancy	0	0	0	0
Late Penalties	0	150,782	9,400	30,926
Rejected Expenses	635,430	412,239	888,834	974,848
Rejected Depreciation	0	50,000	0	0
Undeclared Capital Gain	0	133,350	0	0
Deductible Expenses	3,418	0	3,705	473,718
Declared Profit	2,215,701	2,831,926	4,208,716	8,073,381
Extracted Profit	2,847,713	3,578,297	5,103,245	8,605,437
Extracted Tax	864,699	1,120,404	1,654,136	2,879,903
Declared Tax	643,495	859,174	1,341,051	2,693,683
Difference (1)	221,204	261,230	313,085	186,220

Penalty Rate	25%	25%	25%	15%
Penalty (2)	55,301	65,307	78,271	27,933
Total (1+2)	276,505	326,537	391,356	214,152

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing

Since the institution is a sole proprietorship specializing in real estate works, it falls under professional profits as stipulated in Article 12 of the Law on Direct Taxes and Similar Duties. The institution is subject to the total income tax. Following the audit, it was found that the taxpayer's accounting was rejected for the period from 02/01/2017 to 31/12/2020. The total income tax was re-established by the tax authorities, showing the following observations:

- No difference in invoiced turnover: There was no discrepancy in the invoiced turnover during the four years, but the taxpayer delayed reporting the turnover, leading to tax penalties according to Article 194 of the Law on Direct Taxes and Similar Duties.
- Rejected expenses: The rejected expenses increased year after year. In 2017, they amounted to 635,430 DA, rising to 974,848 DA in the following year, and further increasing in 2018 to 888,834 DA. The year 2019 represented the peak, while in 2020, the rejected expenses decreased to 412,239 DA.
- Discrepancy between extracted and declared tax: This discrepancy highlights the taxpayer's attempt to reduce the tax burden by inflating expenses and manipulating them, which led to tax risks. According to Article 194 of the Law on Direct Taxes and Similar Duties, the taxpayer is subject to tax penalties due to this manipulation, as detailed in the table above. This recalculation ensures that the total income tax reflects the true financial situation of the institution, accounting for rejected expenses, penalties, and other discrepancies.

6.3 Recalculation of Value-Added Tax (VAT)

After the tax authority rejected the taxpayer's accounting records, the VAT (Value-Added Tax) is recalculated according to the following table:

Table 15. Recalculation of VAT

Statement/Years	2017	2018	2019	2020	Total
Extracted Turnover (9%)	8,482,000	93,043,485	24,483,270	9,567,700	135,576,456
Declared Turnover G50 (9%)	8,482,000	93,043,485	24,483,270	9,567,700	135,576,456
Difference (9%)	0	0	0	0	0
Extracted Turnover (19%)	16,985,813	56,025,750	64,188,694	49,819,850	187,020,107
Declared Turnover G50 (19%)	16,814,890	56,025,750	64,003,440	49,504,700	186,348,780
Difference (19%)	170,923	0	185,254	315,150	671,327
Total Extracted Turnover	25,467,813	149,069,235	88,671,963	59,387,550	322,596,562
Total Declared Turnover	25,296,890	149,069,235	88,486,710	59,072,400	321,925,235
Total Difference	170,923	0	185,254	315,150	671,327
Unpaid Rights (DA)	32,475	0	35,198	59,879	127,552
VAT on Sales (DA)	0	108,023	165,724	371,956	715,784

Total Penalty Rights	0	0	0	70,081	70,081
Total Unpaid Rights	0	140,498	165,724	407,154	843,336
Penalty Rate (25%)	25%	25%	25%	25%	-
Penalty Amount	-	-	-	210,834	210,834
Total Due (Rights + Penalty)	-	-	-	1,054,170	1,054,170

Source: Prepared by the researchers based on information obtained from the Sub-Directorate of Tax Auditing

It is observed that, over the four years, there was no difference between the extracted received turnover and the declared turnover in the G50 returns for activities subject to the reduced 9% rate. Activities related to the last quarter of 2020, which are subject to the reduced rate, are excluded from the discrepancy.

However, for the turnover declared in the G50 and the extracted turnover subject to the 19% rate, a discrepancy was found. This discrepancy obliges the taxpayer to pay the undisclosed VAT, along with penalties for omitted taxes as outlined in Article 194 of the Law on Direct Taxes and Similar Duties. In the end, the penalty for the unpaid VAT is set at 25% of the amount due.

7. Conclusion

The study aimed to examine the impact of creative accounting on the tax base and how tax auditing helps reduce creative accounting practices when determining the tax base. The research was divided into five sections, with three theoretical sections providing an understanding of various theoretical frameworks and two practical sections focused on a sole proprietorship to identify creative accounting practices within its declared data and how tax auditing helped uncover and correct these manipulations. This was done to establish the tax base with the highest level of transparency.

7.1 Findings:

- Creative accounting is a form of accounting manipulation that does not break accounting laws or standards. Accountants use their knowledge of rules, laws, principles, and standards to manipulate recorded numbers in a way that presents a misleading impression of a company's income and risks. Common techniques include income smoothing, offloading losses from bad years, inflating or reducing profits.
- Reducing creative accounting practices helps recover hidden revenues and enhances tax collections.
- Creative accounting negatively affects the tax base, as increasing expenses leads to a reduced tax base.
- Strict adherence to accounting rules and regulations can significantly reduce tax evasion by enabling tax authorities to track and audit financial data effectively.
- Combating creative accounting practices is challenging and requires skilled professionals with expertise and sharp analytical abilities to detect such manipulations.

7.2 Recommendations:

- Provide tax exemptions to encourage investment and reduce tax evasion.
- Lower tax rates to minimize tax evasion.
- Foster collaboration between the tax authorities and other administrative bodies to gather information and clarifications on taxpayers' activities.
- Close loopholes by updating laws and regulations to limit creative accounting practices.
- Impose strict penalties for financial data manipulation and fraudulent tax declarations.
- Focus on training tax administration staff to identify creative accounting practices and detect manipulations in financial statements and tax declarations.
- Increase tax awareness among all taxpayers.
- Improve the relationship between tax authorities and taxpayers.

- Develop a national electronic tax system using modern information and communication technologies.

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