



## Analysis of the Incidence of the Tax on Profits in a Credit and Service Cooperative

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### ABSTRACT

*The examination of tax compliance expenses is becoming more relevant, revealing a complex challenge that involves both national and international fiscal policies. This matter is closely linked to tax evasion and avoidance, and its consequences could distort taxpayers' economic choices. Against this background, the study focuses on the impact of profit tax on the operational outcomes of the 'Fortalecida Abel Santamaría Cuadrado' Credit and Services Cooperative, which operates within the sugarcane sector in Camagüey, Cuba. The research uses both qualitative and quantitative methodologies to investigate this issue. The study aims to provide a detailed understanding of how tax compliance costs affect the cooperative in question by implementing a tripartite procedure that uses mathematical techniques and relative frequency analysis. A key finding from this investigation is the negative impact resulting from the exclusion of advance salary payments as deductible expenses in tax calculations. This finding highlights a critical area for fiscal policy reform as the policy oversight is identified as a source of financial strain for the cooperative. The implications of this discovery are far-reaching, indicating that similar cooperatives and businesses within Cuba (and possibly in comparable economic contexts) may also be experiencing analogous fiscal burdens. Based on these insights, the study recommends the creation of customized methodologies to accurately measure tax compliance costs in the Cuban context. These methodologies should consider the distinctive socio-economic and regulatory features that define the Cuban economy, allowing for more precise evaluations of tax-related burdens on businesses. Furthermore, this research invites broader contemplation on the intersection of tax policy and business sustainability, particularly within sectors that are crucial to national economies but may be vulnerable to strict tax regimes. It emphasizes the need for a balanced approach to tax legislation that protects revenue interests without impeding economic vitality.*





## INTRODUCTION

The Tax Administration in Cuba is immersed in a process of improvement, in order to guarantee sufficient levels of collection to support the sustainability of the growing social investments, whose changes obey a project of greater scope and dimension, aimed at updating the economic and social development model of the country.

Raising the standard of living of Cuban society to ensure prosperous and sustainable development is a basic principle expressed in the Guidelines of the Economic and Social Policy of the Party and the Revolution for the period 2021-2026 (Central Committee of the Communist Party of Cuba, 2021), to which responds the need to gradually apply the tax policy in line with the economic and social changes taking place in the country, where a key purpose of this policy is to protect the increase in social investment, expressed in the universal and free access to social services, where education and health stand out.

In this context, we agree with Torres and Morales (2018, p.15), when they state "public revenues and among them tax revenues we must frame them as a category linked to the fulfillment of the functions of the State". These authors highlight the role of tax revenues to the state budget, conformed by for taxes, fees and contributions required by the tax laws of each country.

The conformation of taxes contemplated in the tax laws of each country is based on tax principles, where these are recognized as the fundamental precepts or guidelines that constitute the normative basis for the organization of taxes aimed at achieving certain state or social objectives. Authors such as Calderón (2013) highlight the use of these principles as the basis for the design of tax laws that allow the implementation of justice and economic efficiency as two key elements of a tax system.

There is no homogeneous authorial treatment in the statement of tax principles contemplated in the tax laws of each country. However, most authors (Albi, et al., 1996; Calderón, 2013; Macedo, 2018; Torres and Morales, 2018, among others) highlight the principles of capacity to pay, fairness and equity, efficiency, sufficiency and finally administrative simplicity as important in the design of tax rules. It is with this last principle that the present study is related.

The principle of administrative simplicity is based on the recognition that there are associated costs linked to the taxation process, where there is authorial consensus that taxation costs can be classified generically into three types:

1. The most obvious cost is the cost of paying the tax itself.
2. Distortion costs arising from the changes that taxes produce in the prices of products and factors of production, which in turn alter the share of economic behavior.
3. Operating costs, which are the resources used to operate the tax system (or a given tax) that could be saved if the tax system (or the given tax) did not exist. (Macedo, 2018, p.31)

The most important of these are the operating costs of the tax system, which are perceived from two points of view:

1. The costs to the Treasury related essentially a the costs of the administration, including the costs of enactment of the tax law, which include the The tax legislation to the expenses of all the agencies in charge of the enforcement o these laws, including those linked to tax evaders.
2. The taxpayer's costs or tax compliance costs, which are represent the cost to the taxpayer of complying with his tax obligations.

The latter according to Macedo (2018, p.31-32) can be classified into three types:

1. Monetary costs: These include everything from the expenditure for the payment of the tax itself, such as the expenses of the personnel dedicated in the entities or companies to taxation in all or part of their time, to the payment of tax advisors according to the complexity of the system.
2. Time costs: These are incurred when filling out tax returns, collecting the necessary data for these purposes, as well as any other action that takes time away from the taxpayer's economic activities and is related to the fulfillment of his tax obligation.
3. Psychic costs: These include stress and anxiety, located both in honest taxpayers who try to comply with their tax obligations and have difficulties in understanding tax laws and regulations; or even tax evaders who suffer when they are discovered or because of the latent fear of being discovered.





## LITERATURE REVIEW

### A. Tax Compliance Cost

The importance of tax compliance costs is recognized due to their impact on taxpayers' attitudes towards compliance with tax obligations, being a cause of tax evasion and avoidance. However, despite this recognition, there are insufficiencies in the availability of the source of information on the taxpayer's costs, since the pertinent information channels are not available in all cases. This situation is a factor to be considered in the analysis of tax evasion and avoidance, since, as Gómez and Morán (2020) state, the statistical limitations when analyzing tax evasion and avoidance are numerous and raise the need to work in a coordinated manner in the elaboration, processing and filtering of the information used as input from different sources and entities.

According to Gómez and Morán (2020), in the analysis of tax avoidance and evasion it is necessary to understand not only the magnitude of tax avoidance and evasion, but also its causes and This is crucial when designing tax policy and anticipating its possible effects on different groups of taxpayers. Traditionally, tax administrations have influenced tax non-compliance behavior through the use of penalty-oriented instruments, with emphasis on the size of the penalty and the increase of the tax rate. This situation has caused taxpayer compliance costs to become a determining factor in their compliance with tax obligations, which implies the need to be observed and studied.

In recent years there has been a worldwide trend on the part of the governments to transfer costs from the public or state sector to the private sector or population, thus reducing the costs of the treasury by increasing taxpayer compliance costs, in their eagerness to curb public spending and avoiding the implementation of more taxes that are unpopular. This tendency to increase taxpayer costs can lead to anti-social behavior, with increased tax evasion, informality, due to the fact that taxpayer costs have a more arbitrary incidence and weigh with disproportionate intensity on companies and individuals (United Nations - CIAT, 2014).

Compliance costs tend to increase as the complexity of the tax system and the complexity of each tax increases. Lewis (1982) highlighted, as a fundamental principle to be considered by any tax administration, the simplicity of its system, due to the impact it has on maintaining very low levels of both the administrative costs of the tax authorities and the taxpayers' compliance costs, when he stated: the first principle [of a good tax regime] is simplicity, where both the administrative costs of the tax authorities and the costs incurred by the taxpayer in complying with his tax obligations are kept to a minimum. [and] what appears to be a saving in administrative costs sometimes contributes to an increase in the personal costs of tax compliance and vice versa. (p.151- 152).

To manage these costs it is essential to measure and characterize them. However, in the Cuban business context they are not measured and consequently are not analyzed. Law 113 of the Tax System (National Assembly of the People's Power, 2012) establishes new guidelines in the special tax regime for the agricultural sector, where it is established in Article 359 that natural and legal persons engaged in agricultural activities, without prejudice to the payment of the remaining taxes in whose taxable event they incur, pay taxes on personal income, on profits, on sales, on the ownership or possession of agricultural land, on the idleness of agricultural and forestry land, on land transportation, on the use of labor force, as well as the contribution to social security.

For the payment of the tax on profits for Credit and Service Cooperatives (CCS), the Law establishes some specificities, consisting of:

1. The CCS pays this tax at a rate of 17.5% of the total amount of the tax. Taxable net income, provided that more than 50% of its income comes from the commercialization of agricultural products and/or the rendering of services related to this sector.
2. Otherwise, they apply the tax rate of up to thirty-five percent. (35%), established in general for the payment of this tax.

In this context, the Cooperativa de Créditos y Servicios Fortalecida Abel Santamaría Cuadrado is the product of the voluntary and express union of landowners and/or usufructuaries and their families who jointly work the land and do not belong to any other cooperative. Its main line of production is to produce and commercialize agricultural, livestock, forestry, sugarcane and other productions.





This cooperative has a total area for collective use of 66.43 hectares, of which 40.26 hectares are dedicated to cattle raising and 26.17 hectares to sugarcane. For the development of its activities it has a total of 14 workers as cooperative members, who have adequate preparation and training for the performance of their duties, including 4 graduates of higher level, 7 technical level and 1 skilled worker, in addition to 260 members linked to productive activities.

In this cooperative, the impact of the tax policy on its results is not determined, based on the recognition that this type of organization has particular characteristics that distinguish it. Therefore, the objective of the present study is to analyze the incidence of the tax on profits in the results of the Cooperative of Credits and Services Fortalecida Abel Santamaría Cuadrado belonging to the sugarcane sector in Camagüey. There are antecedents of similar studies in the national context in the National Office of Tax Administration (ONAT) of Camaguey jointly with the University of Camaguey by Torres and Fernandez (2004) where a study of the compliance costs of taxpayers in the municipality of Camaguey was carried out, but from the perspective of the ONAT in the search for possible causes of tax evasion and avoidance.

## METHODS

The study presented here is an applied research, with a mixed approach, where a three-step procedure was developed. Determination of the financial result according to the affidavit, in order to visualize the taxable base of this tax according to tax regulations.

A table consisting of three columns and 12 rows Columns:

- A. Concept
- B. No of row
- C. Unit of Measure (UOM)
- D. Import Rows:
  - 01. Gross Income
  - 02. Returns
  - 03. Net income
  - 04. Other income
  - 05. Total income
  - 06. Cost of sales
  - 07. Cost of sales
  - 08. Other expenses
  - 09. Total Expenses
  - 10. Net income
  - 11. Deductions
  - 12. Taxable net income.

Step 2. Analysis of the incidence of salary advances in the determination of the tax on profits, where we seek to quantify the incidence of this item in the amount to be taxed of this tax.

A table is made up of five columns and six rows Columns:

- A. Concept
- B. Unit of Measure (UOM)
- C. Amount per affidavit
- D. Amount considering salary advances
- E. Variation Rows:
  - 01. Total income
  - 02. Total Expenses
  - 03. Net income
  - 04. Deductions
  - 05. Taxable net income.
  - 06. Profit tax





Step 3. Determination of the weight of the tax on profits within the cooperative's contributions, the purpose of which was to quantify through the relative frequency the weight of this tax on the total contributions made for taxes.

A table is made up of three columns and seven rows Columns:

- A. Concept
- B. Amount
- C. %

Rows:

- 01. Sales tax
- 02. Tax on labor force
- 03. Tax on land transportation
- 04. Profit tax
- 05. Territorial contribution to local development
- 06. Social security contributions
- 07. Total taxes

### RESULTS AND DISCUSSION

The period analyzed corresponds to the end of the accounting period in 2021, from July 1, 2020 to June 30, 2021. The results achieved are shown below.

**Table 1. Determination of the financial result according to the affidavit**

Concept	No From Row	UM	Amount
A	B	C	D
Gross income	01	Weights	1 000 205,28
Returns	02	Weights	0.00
Net income	03	Weights	1 000 205,28
Other income	04	Weights	0.00
<b>Total income</b>	05	<b>Weights</b>	<b>1 000 205,28</b>
Cost of sales	06	Weights	217 936.06
Cost of sales	07	Weights	389.04
Other expenses	08	Weights	82 550.33
<b>Total expenses</b>	09	<b>Weights</b>	<b>300 875,43</b>
<b>Net income</b>	10	<b>Weights</b>	<b>699 329,85</b>
Deductions	11	Weights	34 966.49
<b>Taxable net income</b>	12	<b>Weights</b>	<b>664 363.36</b>

Table 1 shows that for tax purposes the cooperative shows a net profit as taxable income for the calculation of the profit tax of \$ 664,363.36, given that the salary advance is not considered a deductible expense for the calculation of the net taxable income, this is deducted after the profit tax is paid, so the cooperative shows a fictitious result at the end of the fiscal year for tax purposes.



**Table 2. Analysis of the incidence of salary advances on the determination of the profit tax**

Concept	UM	Amount per affidavit	Amount considering advances of salaries	Variation
A	B	C	D	E
Total income	Weight s	1 000 205,28	1 000 205,28	0.00
Total expenses	Weight s	300 875,43	687 923. 73	387 048.30
<b>Net income</b>	<b>Weight s</b>	<b>\$ 699 329,85</b>	<b>312 281,55</b>	<b>(387 048.30)</b>
Deductions	Weight s	34 966.49	34 966.49	0.0
<b>Taxable net income</b>	<b>Weight s</b>	<b>664 363.36</b>	<b>277 315. 06</b>	<b>(387 048.30)</b>
<b>Profit tax</b>	<b>Weight s</b>	<b>116 264,00</b>	<b>48 530,00</b>	<b>(67 734,00)</b>

Table 2 quantifies a decrease in the taxable income for profit tax purposes of Ps. 387,048.30 by considering advances on salaries as a deductible expense.

The accounting treatment of the monthly payroll for this type of business organization establishes the debit to the account "Payment on account of profits" because the advances are considered to be remittances made on account of profits and are credited at the end of the fiscal year against the Profit and Loss account. This situation causes that during the fiscal year in the CCS the expenses related to salary are not charged to any expense account and, therefore, for tax purposes they are not considered deductible.

The failure to consider the advance payment on salaries as a deductible expense for tax purposes causes losses to this cooperative in the amount of 67,734.00 pesos, since the amount to be contributed to the budget would have been 48,530.00 pesos.

**Table 3. Determination of the weight of the profit tax within the cooperative's contributions**

Concept	Amount	%
A	B	C
Sales tax	389,04	0.2
Tax on labor force	18 502,22	9.4
Tax on land transportation	372.00	0.2
<b>Profit tax</b>	<b>116 264,00</b>	<b>59.0</b>
Territorial contribution to local development	4 809,98	2.4
Social security contributions	56 853,73	28.8
<b>Total taxes</b>	<b>197 190. 97</b>	<b>100.0</b>

Table 3 shows the significant weight of the tax on profits in this company, where 59 percent of the amount contributed to the state budget from taxes corresponds to this tax, so the economic impact caused by not considering advances on salaries as deductible expenses is of greater relevance.

As a consequence of this situation, the entity was affected in the months of January to March 2022, where there was a delay in the payment of salaries to workers, as well as not being able to comply with the payment of the corresponding taxes. This last situation meant that CCS had to request a deferral from the Tax





Administration Office with the corresponding payment of a commission, as required by law, for the deferral request presented for the items detailed below.

- a. Social security contributions
- b. Special employee social security contribution withholdings
- c. Labor Force Utilization Tax
- d. Territorial contribution to local development

The non-consideration of the advance payment for salaries as a deductible expense for tax purposes generates a fictitious result and causes a payment of tax to the budget above the real results of the entity, since actually the cooperative incurred in an expense and cash was disbursed for this concept, which has a productive backing. This type of affectation corresponds to tax compliance costs and is in total correspondence with what is expressed by Macedo (2018) when he considers that monetary compliance costs, which include the tax payment itself, when they significantly reduce the taxpayer's income can alter the economic behavior, discouraging the efforts of the companies to obtain higher levels of sales or profits.

This situation coincides in part with the results obtained by Torres and Fernández (2004) in the study carried out in the municipality of Camagüey, where it was found that elements such as the form of accounting that increased the base The taxable income and the progressivity of the rates had an impact on taxpayers' behavior, which had a discouraging effect on productivity and, in the case of the self-employed sector, an increase in tax evasion or avoidance.

For their part, the studies by Gómez and Morán (2020) recognize the multicausal nature of tax avoidance and evasion, where in the opinion of the authors of this article, for the current Cuban context, tax compliance costs are an element to be considered in studies on the subject.

## CONCLUSION

Tax compliance costs are a factor to be taken into account by the Tax Administration in any analysis of tax evasion and avoidance. The analysis carried out raises the need for the ONAT to assess the consideration of salary advances as deductible expenses for the purpose of calculating the tax on salaries for the sugarcane cooperative sector. Finally, the need to design methodologies for determining tax compliance costs contextualized to Cuban particularities is evident.

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