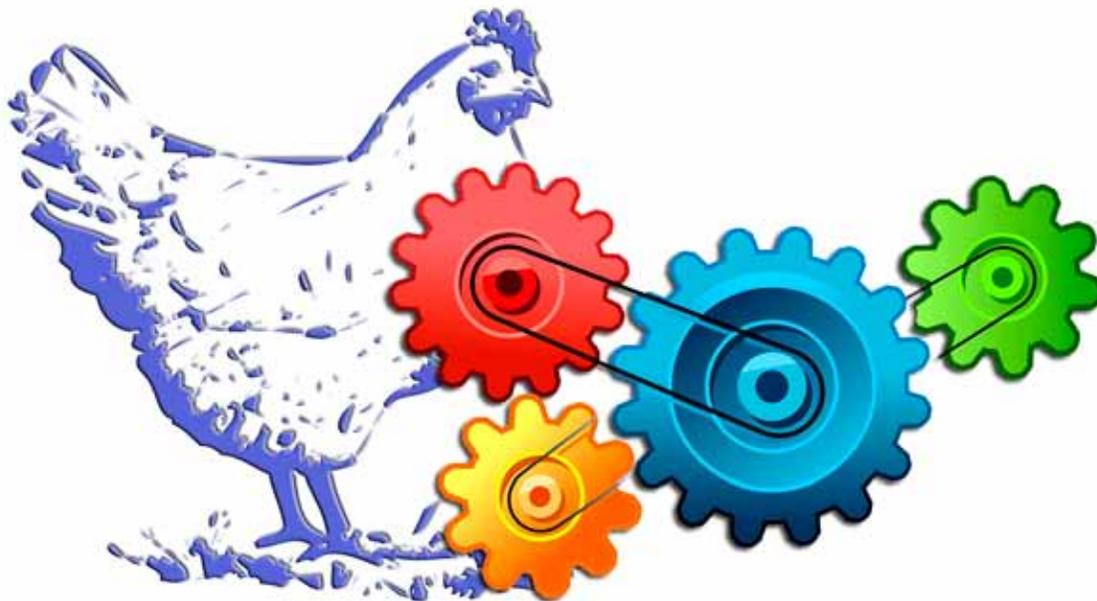


Audits in the Poultry Sector: Productive Stage

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Summary

This paper analyses the producer stage of the poultry sector, educating on tax benefits and the accounting regulations applicable to this sector. In addition, it establishes a risk matrix showing the inconsistencies that might arise in the sector. In addition, it provides an operational control strategy for poultry meat producers which may be extended to the rest of the marketing chain of the poultry sector (including both meat and eggs) to enable enhanced compliance by the sector's supplier chain.

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INTRODUCTION

Contenido

- Introduction
- 1. Background
- 2. Sector analysis
- 3. Proposal for audits
- 4. Conclusions
- 5. Bibliography

In the 80's and 90's, tax administrations implemented controls to combat taxpayer non-compliance. Although initially successful, over time these controls showed falling performance. With the purpose of redressing the situation and meeting public interests, administrations should re-think their control strategies.

Deep knowledge of the sectors and the use of technology allow tax administrations to make less intrusive, more effective and much timelier controls to enable the monitoring of sector compliance and more efficient targeting of audit efforts. This type of control may be supported by traditional mass controls, which have low operational costs.

Auditing activities pose on-going challenges to the work of tax administrations. Most administrations' operations are usually conducted in a context of legal, financial and HR restrictions which compel them to seek alternative audit methods that will not impose significant restrictions while allowing them to maximize their results.

In many cases, conventional auditing fails as a result of the operating conditions of the taxpayer sectors, which affect the auditability of their transactions. Operational controls are proposed as a means of improving compliance by sectors like poultry production, whose characteristics enable controls on their production and marketing.

1. BACKGROUND

Overall controls tend to show falling performances. This is usually the case because the restricted context in which tax administrations operate prevents them from sustaining the feeling among taxpayers that there is high risk of non-compliance detection and debt enforcement.

Operations control is a desirable goal for those responsible for developing control strategies. Good operational controls enable enhanced taxpayer compliance of taxpayers with low or medium risk aversion, who will tend to improve their

self-assessments if they believe that the tax administration knows about their transactions and if they perceive that their non-compliance will not be tolerated.

One of the sectors that lends itself well to efficient operational controls by virtue of its specific characteristics is poultry raising. In subsequent paragraphs we provide an analysis of the tax advantages which make it feasible to implement less intrusive, less costly and more effective operational controls.

If, as in the Peruvian case, the sector is highly informal, an initial control at the level of the farmer and a subsequent expansion to the whole sales chain could not only improve collections of all the sales chain with interesting ramifications for controlling the transactions of suppliers of go-

ods and services in the industry but also improve competitiveness in the sector, given that the Administration could reduce the unfair competition created by evasion in the sector.

2. SECTOR ANALYSIS

2.1 Applicable tax system

The system that is currently in effect for taxes under central government administration includes:

- General Sales Tax at an 18% rate¹ over total sales.
- Income Tax² at a general 30% rate, which given the relevance of the poultry sector, is reduced to 15% provided the conditions in the norm are met.
- Agricultural Sector Promotion Act - Act N°27360³. Individuals or corporations may apply for the benefits granted by Act N° 27360, when they conduct the following activities:
 - Agriculture and/or breeding activities, except for forestry;
 - Agro-industrial activities;
 - Aquiculture.

It is understood that the beneficiary's core business is the agricultural, breeding and/or agro-industrial activity when net income from other activities is not comprised in the benefits established by Law and do not exceed, overall, twenty-percent (20%) of the overall net income estimation. The validity of the benefits granted by Act N° 27360 has been extended by Act N° 28810 as of 31 December, 2021.

2.1.1 Agricultural sector application

In order to apply for the benefits of the Agricultural Sector Promotion Act, the businesses of the sector shall file form No. 4888 with the Tax Administration as of 31 January of each fiscal year, during the effective term of the benefit.

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1. *Text of the General Income Tax and Selective Excise Act – Executive Order N° 055-99-EF (published on 15 April, 1999 and effective as of 04.16.1999) and its Regulatory Executive Order N° 29-94-EF (published on 03.29.1994, effective as of 03.30.1994).*
 2. *Text of the Income Tax Act, Executive Order N° 179-2004-EF (Published on 8 December, 2004),*
 3. *Article 1 of Executive Order N° 065-2002-AG, published on 12-30-2002, indicates that the agro-industrial activity under the scope of this Act, is the productive activity included in the Annex to Executive Order N° 007-2002-AG, even when it is conducted by an individual other than the beneficiary.*

As provided for in Executive Order N° 007-2002-AG, the agro-industrial activities included in this benefit correspond to CIIU 1511-4, 1513-0, and 1542-0. By virtue of the provisions in article 3 of Act N° 28852 on the promotion of private investment in reforestation and agroforestry; for the purpose of enforcing Act N° 27360, reforestation activities shall be deemed crops.

2.1.2 Sector benefits

The Benefits established by Act N° 27360 are summarized hereunder:

Benefits	Agriculture	Agro-industry
15% rate on third-category income from the Income Tax	Yes	Yes
Exemption from the Extraordinary Solidarity Tax ⁴ (1) applicable on remunerations for individuals employed in the agricultural sector.	Yes	Yes
Agricultural Health Insurance (receiving all the services from the Social Security and a 4% contribution from the salary).	Yes	Yes
Special 20% annual depreciation rate on investments in hydraulic infrastructure and irrigation works undertaken by beneficiaries during the effective term of the Law.	Yes	Yes
Beneficiaries with investments in the pre-productive phase shall recover the General Sales Tax and the Imports' Tax paid for imports and/or local purchases of capital goods, supplies, services and construction contracts, provided they apply in the pre-productive phase, which shall not exceed a 5-year term.	Yes	Yes

2.1.3 Beneficiaries' obligations

In order to qualify for the tax benefits set forth, individuals or corporations shall be up to date with their tax obligations. Otherwise, they shall lose the benefits extended, when during the effectiveness of the Law, they fail to meet 3 current, consecutive or alternate tax obligations in the fiscal year they applied for the benefit. To such end, the payments made effective within 30-calendar days subsequent to maturity shall not be deemed noncompliance.

The loss of the tax benefits extended by Act N° 27360 shall apply upon determining noncompliance with tax obligations with the SUNAT. This is an automatic process, without requiring a notification by the Administration (Refer to [Report N° 227-2005-SUNAT/2B0000](#)).

Upon losing the benefit, the taxpayer is required to pay an income tax advance within the general system, as from the month subsequent to the loss.

2.1.4 Auditing of the benefit

In order to audit the benefit granted, the SUNAT files a request with the Ministry of Agriculture for the pertinent technical qualifications of the beneficiaries' activities, which shall be delivered within thirty (30) working days subsequent to the date of the request.

Should the information submitted in the process to apply for the benefits of the Law be false or, if at the end of the fiscal year the taxpayer has failed to fulfill the requirements in item 1 of Article 2 of the regulation, the taxpayer shall not be deemed a beneficiary. To such end, the SUNAT shall issue the corresponding resolution.

In such cases, taxpayers shall be required to file the statement and make the payment of the taxes they failed to file in the fiscal year, plus interest and fines applicable, as provided for in the Tax Code.

4. Extraordinary solidarity tax, annulled as from 12/01/2001 by Act N° 28378 in its single article, published on 11-10-2004.

2.2 Analysis of the accounting standards for the poultry sector

Biological assets: In the poultry sector, biological assets apply to birds in the breeding and production phase, which produce birds for future sale, as well as chickens in the breeding phase as of 31 December each year. The businesses of the sector record their biological assets according to the following accounting practice:

- Birds in the breeding phase (from zero days to week 22 in the case of chickens) are valued at the cost. This practice is adopted in the absence of an active market that determines their fair value, considering the short life-span.
- Birds in the completed breeding phase. The bird moves into the productive phase (egg-laying), such as the case of broiler chicks, and they are valued at the fair value less the costs estimated at the point of sale; in Peru it is estimated on the basis of the prices published by the Ministry of Agriculture.⁵
- Birds in process (live birds) bred for sale (up to 34-days), are valued at the cost in the absence of an active market that determines the fair value. In the subsequent phase, they are valued at the fair value less the costs estimated at the point of sale. In Peru, it is determined on the basis of the prices published by the Ministry of Agriculture.
- On their financial statements, the businesses of the sector account for the income or expenses obtained upon applying the variation

in the fair market value of the assets, at the Balance Sheet date. Considering the application of the IAS 41, any future variation resulting from production, such as prices or other factors, shall be accounted for on the income for the year in which such change is made. In other words, the operating profits or losses shall include an adjustment for the change in the fair value of such assets in the applicable period.

- Birds in the reproductive phase (in the breeding and laying phase) are deemed to have a 69-week productive life; after 69 weeks, they are discarded and carried over as inventory applying the fair value minus the costs estimated at the point of sale.

2.2.1 Accounting estimates applicable to the sector

In the poultry sector, in compliance with Accounting Standards, businesses undertake estimates and assumptions for the future.

Accounting estimates do not reflect actual performance.

Estimates and assumptions with the risk of producing a material adjustment may imply:

- Determining the recoverable Value of biological assets⁶:
- Reviewing the book value and the depreciation provision⁷.

5. <http://www.minag.gob.pe/boletin-diario-de-precios/boletin-diario-de-precios-2010/index.html>

6. *In this case, the sector's businesses apply the criteria established in IAS-41, which sets forth that the asset shall be measured in the initial recognition on the financial statements as well as at the date of the balance sheet at their fair value less the estimated costs at the point of sale.*

Such Fair Value is determined according to their quoted market price in the active market. In the absence of a market, the applicable principle shall be the prices of transactions at the assessment date or market prices for similar assets or present value of the net cash flows expected from the asset, discounted at a rate before taxes defined by the market.

7. *Businesses in the poultry sector apply the provisions in IAS-36 in order to determine whether a permanent asset has been impaired and a provision is required. Reproductive birds are depreciated as of the date on which the reproductive activity starts. The breeding process extends over 180-days, during this period, the consumption in these species are accounted for together with the value of chickens in the cost of the biological agent, which is subsequently amortized (depreciated, according to our tax regulations).*

2.3. Sector importance

The poultry sector forms part of the livestock sector and together with the agricultural sector, constitutes the agricultural-livestock sector. The poultry sector includes the production of meat as well as eggs. In Peru, the agricultural-livestock sector is one of the most important, as presented hereunder:

Such restrictions to substitute products favored the development of the poultry industry for meat and eggs, making bird meat the one in highest demand¹⁰. According to data from the National Institute of Statistics and Information Technology (INEI, as per the Spanish acronym), the production of chicken meat went from almost 462 Million metric tons in 1997 to almost 938 Million metric tons in 2009.

Concepto	PBI 2006 *	Participación
Total	160,383	100.0%
Agropecuaria	13,344	8.3%
Pesca	808	0.5%
Minería e Hidrocarburos	9,349	6.1%
Manufactura	24,150	15.1%
Otros Servicios	61,736	38.5%
Construcción	8,348	5.2%
Electricidad y Agua	3,320	2.1%
Comercio	23,227	14.6%
Otros	15,500	9.7%

Fuente: INEI y BCRP

Concepto	IGV	Renta, Iva Cel y Reg-Adiccionario	Total Recaudación	Participación
Total	11,081.7	1,899.8	12,981.5	100.0%
	32%	39%		
Agropecuaria	181.3	31.5	212.8	1.7%
Pesca	18.7	63.3	82.0	0.7%
Minería e Hidrocarburos	1,329.7	6,731.6	8,061.3	62.2%
Manufactura	2,592.1	1,587.1	4,179.2	32.2%
Otros Servicios	1,827.1	3,105.2	4,932.3	38.0%
Construcción	552.6	241.4	794.0	6.1%
Comercio	2,214.8	1,213.2	3,428.0	26.4%

Fuente: Superintendencia Nacional de los Impuestos Internos (SUNAT)

In spite of the importance of the sector in terms of revenue, it does not match its GDP contribution, as presented on the table at the end of paragraph. In this area, such lack of consistency arises from the high level of tax expenditure in the sector⁸ as a consequence of State tax policies; the other component is explained by the high level of production consumption by the inhabitants in rural areas; finally, the high level of informality that prevails in the sector explains the difference.

Broilers are the inputs for other activities such as cold cut factories, restaurants, chicken meat outlets, hospitals, among others; but it is also an end product. The largest share of broiler chickens are aimed at end consumers (households) through supermarkets, general markets or mini-markets.

In Peru, the production of poultry meets the largest share of the demand for animal protein⁹; this explains the lack of important pastures in the country that promote livestock breeding. The lack of a quality cold-storage change prevents the fish from the Peruvian sea, rich in species for direct human consumption, from reaching consumption centers in sufficient amounts.

Retail sales is the most informal stage, chicken is sold alive by weight in the storage centers of broiler chicken producers or in large wholesale markets; from that point, control of the product is lost.

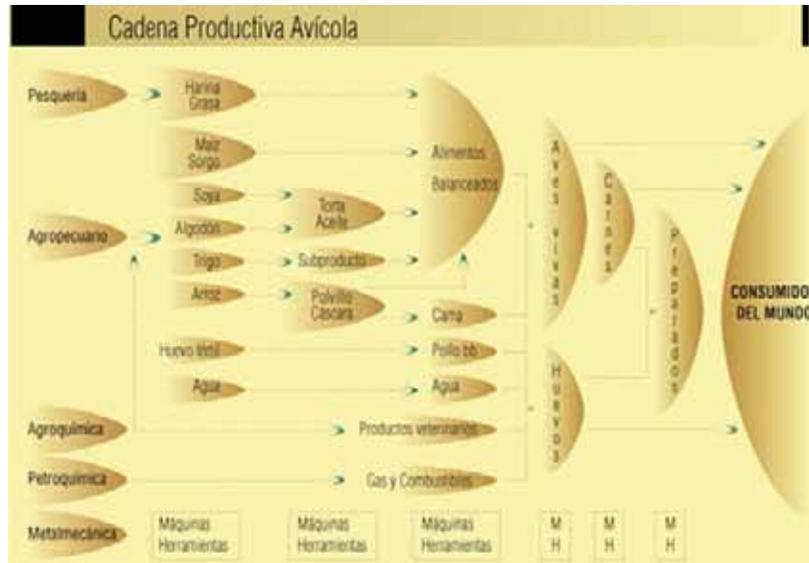
2.4. Description of the sector's operation

The poultry productive chain involves a diverse series of goods and services, including: inputs such as corn, soy, micro-elements, fish meal, vitamins, etc. In the following chart, we present the information prepared by the Poultry Breeders' Association of Peru:

8. In 2009, the estimated total Tax expenditure, understood as: the quantified amount of tax base exemptions, authorized deductions from gross income, tax credits drawn from payable taxes, reductions in tax rates and deferred taxes, amounted to USD 2,648 MM, out of which 22% was aimed at the Agricultural Sector <http://idbdocs.iadb.org/wsdocs/getdocument.aspx?docnum=1780035> as of 04-08-2011.

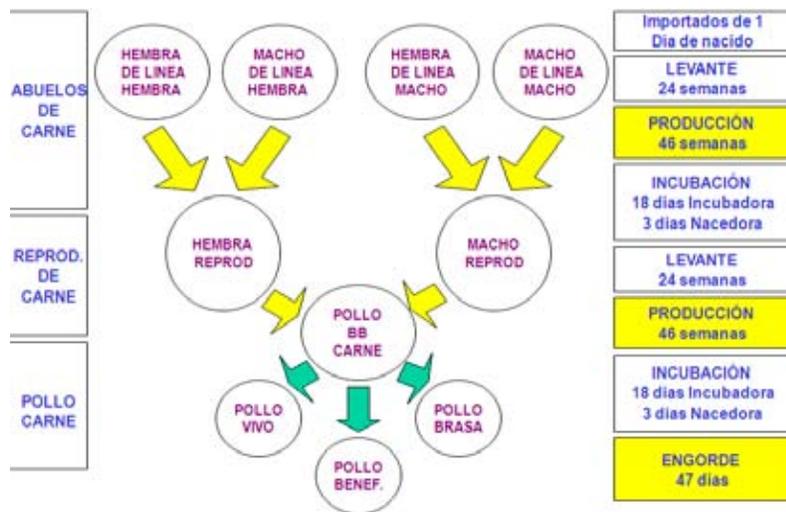
9. <http://www.inei.gob.pe/web/aplicaciones/siemweb/index.asp?id=003>

10. Available at http://www.apavic.com/html/sections/cuadros/cuadro_11.asp



At the level of the broiler chicken producer, we find producers of broiler grandparent stock, broiler producers (parent stock), and finally, producers who purchase eggs for incubation of parent stock or chicks for fattening and subsequent sale. Each production phase is headed by spe-

cialized producers. The largest producers in the country start their production from the grandparent level. The following chart has been prepared by the Ministry of Agriculture (MINAG) and distinguishes the different levels of producers:



2.5. Informality in the sector

The poultry industry requires great capital investments and this stands as a market access barrier. According to the information from the Peruvian Agriculture Association (APA¹¹), supported by the statistical information from the INEI, industrial poultry and egg production is concentrated in the departments of Lima, La Libertad and Ica and large producers account for over 80% of the total production.

The rest of the production comes from small or semi-industrial ventures, the latter by a significant number of small and medium-sized producers in specific areas, which, taking advantage of the access barriers or transportation surcharges, control a significant portion of the commercial meat and egg production.

The tax behavior of the latter group tends to be deficient, and the collection of the debts it generates is low, since they normally lack sufficient resources to operate and use the General Sales Tax (VAT) as a permanent working-capital financing mechanism, and, in many cases, as the single source of business profit.

In an auditing process, the work of the auditor is based, among others, on the knowledge regarding the operations of the business and reviews on accounting documents and records; the latter, naturally, account for past events. Given the dynamic and complex nature of the poultry sector, it is difficult to assert that such records are complete and

reasonably reflect all the economic events of the business, particularly when the purpose is to systematically conceal production and sales, as in the case of informal actors (partially or totally)¹².

Consequently, such situation renders the auditing efforts and methods based on historic records ineffective in controlling informality in the poultry sector.

On the other hand, for years, producers in the poultry sector have developed information and auditing methods and means enabling them to efficiently manage their productive and marketing operations, even before they are reflected on an accounting document or record, since this is vital for the efficient operation of their business.

Nevertheless, there are no tax regulations demanding the enforcement of audits based on records or the content thereof. This is due to the fact that tax regulations provide for the use of general documents by taxpayers, without distinctions by sector or types of taxpayers (beyond their size). Therefore, innovative control and auditing programs are required, focused on current events of the productive units and more aligned with the dynamic nature of economic sectors or activities such as poultry breeding, in order to attain better efficacy in audits and collection.

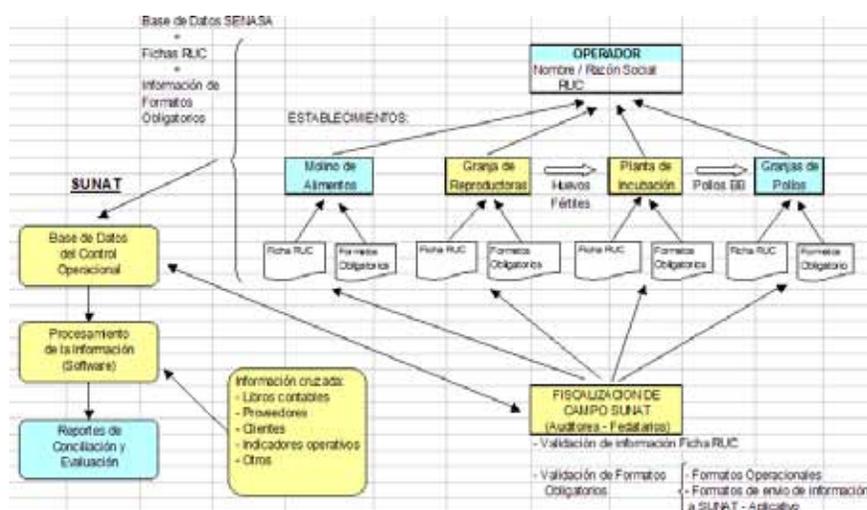
11. The association's web page is: <http://www.apavic.com/index2.asp>

12. This is a feature of the economic sectors whose operation and type of productive chains require deep knowledge of the productive processes, the production-marketing chain, etc.

3. PROPOSAL FOR AUDITS

3.1. Business model

The business model set forth is summarized in the following chart, in order to avoid false selections, it suggests using the information on the purchase of feed, as a supplemental indicator enabling to distinguish a producer from a simple seller.



3.2 Sector risk table

Following is a risk Table that describes the sector:

CONCEPT	Individuals	Small	Medium	Rest of PRICOS	MEGAS TOPS
No records of feed purchases for poultry breeding.	H	H	M	L	L
No records of poultry sales	H	H	M	M	L
False inventories	H	H	H	M	L
Accounting estimations applicable to the sector	-	-	M	H	H
Under-valuation of the bird sales' record	H	H	H	M	M
Failure to issue invoices	H	H	M	L	L
Inconsistencies in bird transportation	-	-	M	M	L
High index of write-offs and losses.	L	L	M	H	H

H= High M= Medium L= Low

This table shows how risks are presented as a function of the type of taxpayer. Audits shall be defined according to the type of taxpayer and the risks observed in each one.

The type of taxpayer is classified according to income, by which individual taxpayers and small taxpayers feature lower income. This group includes MYPES –micro and small taxpayers–, many of them created as subsistence businesses, and few to accumulate capital and grow. This group of taxpayers is large; therefore, the results of their audits are not positive. They present great inconsistencies and high risk; owing to their number, massive audits apply in this group.

Medium-sized taxpayers and the rest of Large taxpayers (PRICOS, as per the Spanish acronym) are subject to audits. Nevertheless, owing to their audit history, noncompliance in this group ranks in the middle level. The level of income and number of taxpayers in this group is not high.

Taxpayers classified under TOPS and MEGAS feature high income and equity levels, but are few in number.

Actions are aimed at HIGH-risk cases and, the type of procedure and the enforcement time depends on the taxpayer group and size.

3.4 Operations' traceability: informative statements and direct audits.

The tax administration, among other powers, may require taxpayers to file informative statements of their transactions. Based on this power, it may mandate producers to report on their operations electronically (PDT¹³), from imports of grandparent stock, which has to go through customs, to the final benefit from the assets and the statements from the farms in which broilers'

breeding or fattening process has been conducted.

The SUNAT may enforce the informative statement not only through random or ongoing audits¹⁴, but also with additional controls by the SENASA, the public animal health authority. This could supplement the regular audits not only with the regular visits to the production centers, but also by the recording and verification of exceptional mortality cases.

3.4. Bancarization¹⁵ of transactions as a supplemental auditing mechanism for taxpayers

In order to guarantee the traceability of transactions and avoid the rejection of the purchase and/or sale transaction reported, Peruvian legislation requires using payment means when transactions exceed S/. 3,500 or USD 1,000. The payment means defined by legislation enable to identify the parties without any doubt.

On the other hand, the informal production of broilers requires lots of at least 5000 units of broiler chicks, and over 50,000 eggs for incubation of chicks, for a profitable operation. Producers would be mandated to use means of payment to complete their transactions. This mechanism would avoid rejection of transactions and prevent the disruption of operations' traceability.

3.5 Sales tax to guarantee the payment of tax obligations

As mentioned above, approximately 20% of the total chicken production is informal in this context. To the extent parent stock egg and meat producers are more reliable, it is possible to establish the obligation of a General Sales Tax

13. PDT: *Electronic Statements' Programs*

14. *Visits to the production facilities may be scheduled in order to verify the physical existence of chickens prior to the chicken status process. (chechar esta llamado debe ser 14)*

15. *Act No. 28194*

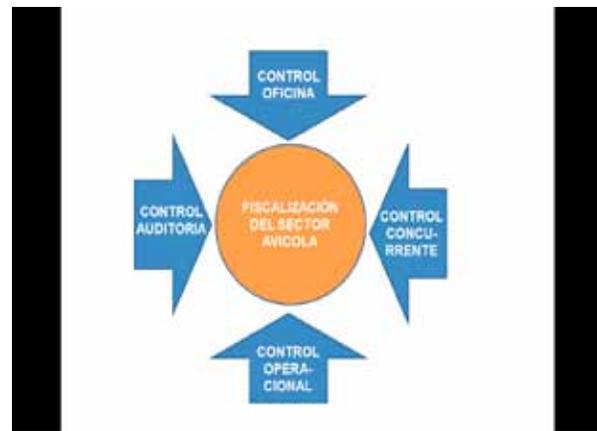
withholding on sales of goods; a tax advance that would guarantee (depending on the rate) at least a share of the tax obligations from less formal producers.

3.6 Compliance control: monitoring transactions and selection of taxpayers subject to audits

3.6.1 Sector auditing

According to the taxpayer group and the risk level, diverse auditing actions shall be applied, all of them with the purpose of enforcing compliance with tax obligations.

- Concurrent Audits. - They are conducted regularly in order to determine compliance with formal obligations, verify the transportation of goods with waybills, or verify the issue of invoices for the products sold.
- Operational Audits. - It consists in audits conducted regularly in order to induce the taxpayer to comply. This audit is conducted on the basis of information from concurrent audits.
- Notifications from the Administration. - These are expeditious and massive actions to promote taxpayers' compliance with tax obligations. The Administration sends notices to the taxpayer upon detecting inconsistencies that require rectification. Should the taxpayer not comply within the term defined, he shall be summoned to the offices of the Tax Administration in order to submit the documentation and regularize or explain the reasons for the inconsistencies.
- Audits.-This action requires more time. The taxpayer's accounting books are inspected in order to determine gaps in terms of sales as well as purchases with tax relevance and omissions on the statement record and the tax payment.



3.6.2 Selection of taxpayers

Taxpayers shall be eligible for audits when they meet the following conditions:

1. Businesses in the sector with inconsistencies in the transportation of birds.
2. Taxpayers in the sector who, according to inspections, failed to issue invoices.
3. Suppliers from poultry businesses, who fail to file their General Sales Tax statement.
4. Customers from poultry businesses who fail to file their General Sales Tax statement.
5. Suppliers of poultry businesses who, based on third-party information, understate sales.
6. Customers from poultry businesses, with mismatches between the purchases filed and the effective purchases from their suppliers.
7. Customers from poultry businesses who are not registered with the Tax Administration.
8. Poultry businesses who do not file sales and/or purchases according to the information delivered by their customers and/or suppliers.
9. Businesses in the poultry sector that file estimations by sector.

The following types of audits are suggested:

3.6.3 Concurrent audits:

Mobile control: The area of massive actions and audits shall be based on mobile controls, which consist in procedures by the massive operations' unit based in strategic geographical areas for the purpose of controlling entry and exit of trucks carrying cargo; for the poultry sector, they would control the transportation of birds. During each audit, they shall request waybills, whose information shall be entered on the internal systems, providing the data of the carrier, driver, related invoice, and delivery address.

Invoices' procedures: The system shall identify taxpayers who are traders in the poultry sector, identifying those based in the markets or places where birds are stocked, and a massive audit shall be conducted in order to verify whether they issue invoices.

Administrative control: An induction audit shall be conducted with the purpose of promoting taxpayers' voluntary compliance.

Audits: A General audit shall be conducted, consisting in a review of documents with a specific scope. Subsequently, the omission shall be determined and the applicable assessment Resolutions shall be issued, when the taxpayer fails to rectify the situation.

3.6. 4 Applicable audits' procedures

3.6.4.1 Internal tax administration requirement

- Statements filed with the Tax Administration.
- Audits' reports presented by the taxpayer.
- Result of the interventions conducted in the Mobile Audits.
- Results of the interventions in procedures to verify the issue of invoices.

Information provided by other agencies in the sector

- Information delivered by the Ministry of Agriculture regarding prices.

Information provided by taxpayers

- Detail of the sales in the poultry sector.
- Detail of the purchases in the sector.
- Detail of the prices for sales.

Review of documents

Upon reviewing the documents, the auditor shall assess the obligation according to two methods, based on:

- an actual basis
- a presumptive basis

3.6.4.2 Specific procedures on an actual basis applicable to the sector:

3.6.4.2.1 Verify that purchase transactions are recorded according to the detailed accounting by suppliers.

The administration shall identify whether purchases qualify as inventory or fixed assets, considering the definitions in IAS 2 Inventories and IAS 16 Property, Plant and Equipment. The following calculations shall apply for the assessment:

The Average Gross Profit Margin (Pm) shall be determined as follows:

The purchase and sale price from the invoices filed by the taxpayer shall be considered.

Determination of the Pm by product. The purchase and sales invoices' filed by the taxpayer shall be accounted for. The unit purchase price and sale price shall be stated, respectively.

$$Pm = (USP/UPP) - 1$$

Where: USP is the Unit Sale Price and UPP is the Unit Purchase Price.

In order to assess the omitted sales, the amounts of the assessed omitted purchases shall be entered, and the assessed Pm applied; based on this procedure, we may draw the following formula:

$$\text{MOS} = \text{MOP} + \text{VA}$$

Where: MOS is Monthly Omitted Sale; MOP is Monthly Omitted Purchase, VA: Value Added, which is calculated as:

$$\text{VA} = \text{Pm.} * \text{MOP}$$

3.6.4.2.2 Verify the accounting and filing of the total sales transactions.

It is worth verifying whether the taxpayer accounts for and files the total sales transactions.

The auditor shall gather all the information relative to the sales made by the taxpayer. To such end, he shall obtain the information delivered by customers as well as the detail of all the purchases reported by the main poultry businesses summoned.

3.6.4.2.3 General audit for understatement of sales

Pursuant to the provisions in Article 42° of the General Sales Tax Act, approved by Executive Order N° 055-99-EF and Article 10° section 6 of the Regulations in the General Sales Tax Act, as approved by Executive Order N° 136-96-EF, the amount of a transaction is deemed inaccurate when, in spite of the issue of an invoice, the following situations arise:

1. that such amount is lower than the regular market value, for other goods and services of equal nature, unless otherwise determined.
2. that reductions in prices arising from write-offs and similar reasons, are off the normal ranges for the business.
3. that the discounts do not meet the provisions in the law or Regulation.

In order to enforce article 1, it is necessary to determine whether the taxpayer's **accounting records feature the inconsistencies mentioned above, among others, the following procedures:**

- Verification that the sales prices are in line with the market; that prices do not vary among customers and the value is not under the prices to the public, unless the taxpayer applies a special prices' policy based on volume and/or customer loyalty.
- Verify that the taxpayer has conducted sales at actual values. In other words, that the sales of goods are accounted for at normal market values. In order to determine a potential understatement of sales, a comparison is required between the sale price of a sample of sales transactions for the same taxpayer and the market value of assets. The taxpayer shall be required to present supporting documentation of the inconsistencies detected.
- In this type of situation, taxpayers may argue that the difference is based on the fact that they establish the prices of assets according to the following criteria; in such case, they shall be required to file a report explaining the price determination procedures¹⁶.

16. *Dominating and free competition position; Free market in terms of product prices, considering discounts without impairing the cost thereof; Fulfillment of their financial obligation, which impacts the reduction in profits; Special customers who pay cash or immediately (within 2-day minimum and 7-day maximum term); Purchase/sale contracts at similar prices; The case may be that a business sells its products under the cost, provided the market value is lower; Greater cost owing to technology factors; Greater financial burden borne by one business with respect to another; Access to second-quality inputs' markets.*

- In this sense, a comparison shall be conducted among the customers who were granted special prices, according to the sales volume and payment terms, since with different customer segments, different sales prices may apply.
- Supporting documentation is required to determine that such values were lower than the normal market value for other goods or services of equal nature.
- It is necessary to determine the percentage of the taxpayer's income that accounts for sales in each level, stating volume and profit margin; the percentage of sales in each level that matches the sales invoices and the percentage of income that represents transactions conducted with buyers who received the invoices, moreover when such details show that in certain cases, the alleged understated sales are one-time sales.
- For the discounts granted, the Administration shall verify whether the taxpayer meets or fails to meet the provisions in section b) of Article 14° of the General Sales Tax Act and item 13) of Art 5° in the Regulations of the General Sales Tax Act.
- The taxpayer shall be informed of the criterion that the auditor shall apply in establishing the assessed market value.
- Upon determining an understatement, the assumptions in the Tax Code shall be the basis to define the need to apply the applicable presumptions.
- In Peru, section a) in item 6 of Article 10° of the General Sales Tax Act Regulations, sets forth that in order to assess the sale price of an asset, a service or a construction contract, as referred to in the first paragraph of Article 42 of the General Sales Tax Act, the SUNAT shall assess it officially based on the market value, and it may apply the procedure set forth in Article 32 of the Income Tax Act. It also sets forth that in the absence of a market value, the sale value shall be determined based on the background information held by the SUNAT (for example: information crossed with customers, audits to taxpayers of the same sector, information from institutions, etc.).
- Additionally, the data and amounts from the invoices whose values are deemed inaccurate shall be accounted for, that is to say, in cases of sales' understatements.
- Based on the invoices, the unit sale price and the sale price for the product shall be accounted for.
- The sale value shall be assessed by the SUNAT, by multiplying the units of the asset sold according to the invoice, by the unit sale price obtained from the invoices for other customers.
- The sale price is determined by comparing the sale price from the invoices and the sale price assessed by the SUNAT; when the latter is higher, a price understatement applies.
- In the case of sales' understatement, the omitted sale price is assessed as the lowest sale price outstanding, and the 18% General Sales Tax rate shall be applied to such amount.
- In the case of a general audit from which differences arise, the procedures applicable are those defined in the Tax Code.
- When the assumptions established in the Tax Code may not be applied, the taxpayer shall be induced to admit the omissions through the induction process described above.

3.6.4.2.4 Fair value accounting estimates

Based on the provisions in IAS 41, the medium and large-sized taxpayers' sectors account for estimates to present the fair value of their inventories. In this sense, it is worth considering that the highest value attributed shall be accounted for as income for the fiscal year. Nevertheless,

for tax purposes, this amount shall be deducted, since in Peru, the annual Income Tax is assessed on an accrued basis. In other words, such income is calculated and shall be considered income when the products are sold. Therefore, it is necessary to verify that the deduction effectively matches the fair value assessment, with the precaution not to deduct the items that constitute actual sales in the fiscal year.

3.6.4.2.5 Write-offs and losses

The deduction of write-offs shall be accepted provided that they are reasonable and verifiable in the productive process.

Regarding losses, the technical report of the losses in the sector shall be filed, as well as veterinarian's reports, etc.

3.7 Impact administration: price increases and impact on the basic shopping basket. management mechanisms

In our country, consumption of chicken meat is high and bears a relevant influence on the makeup of the basic shopping basket. It is foreseeable that informal producers are pressed to

shift to the end consumer the higher cost implied by the auditing mechanism, which would compel them to reveal not only the amounts from the transactions they perform, but also to accurately assess their tax obligations.

Notwithstanding, we deem this a temporary effect, since, the largest share of production is concentrated in a small group of large businesses, who feature an integrated operation that extends to the end consumer, with chicken at more beneficial prices directly in their stores, or indirectly, through sales in large markets and/or supermarkets.

We consider that although the initial pressure to shift the price to the end consumer could end in inflationary effects, such pressure would drop and disappear in the short-term owing to the regulating effect of the formal marketing chain in the market, since they would have zero pressure to increase their prices as a consequence of the auditing mechanism. This is empirically reasserted as a consequence of the application of General Sales Tax withholdings on certain sensitive products (such as fishmeal), whose volatile prices in the beginning owing to the expectation, became normal in less than 15 days.

4. CONCLUSIONS

Operating audits shall enable to: Broaden the tax base: (Taxpayers who file and pay); Keep the RUC registry updated (poultry businesses); Promote the documentation of transactions and reduce understatement of income (accuracy gap) from omitted sales/understatement of sales; Encourage taxpayers to carry a record of their transactions through operations' forms; Facilitate administrative controls by the SUNAT and the early detection of noncompliance; increase the risk sensation and promote voluntary compliance. Operating audits constitute an effective anti-evasion and informality measure in certain sectors.

Owing to its inherent features, the poultry sector qualifies for the implementation of operating audits to control the main risks in terms of Income/ Costs.

Operating audits are perfectly supplemented by traditional field audits.

The implementation of such a measure requires the support of the formal sector to reduce resistance.

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