



## **Proposed Methodology for Tolling Operations in Maintaining Accounting Records in Industrial Enterprises**

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### **Abstract**

This article is devoted to the issues of regulating tolling operations implemented in the process of receiving raw materials supplied by the customer, their processing and subsequent return of products to customers. In addition, the article investigates the procedure for document flow, obligatory requisites of source documents drawn up at the customer and during processing, as well as the procedure for their compilation, acceptance, and storage.

**Keywords:** tolling party; raw materials supplied by the customer; tolling; costs, processing; external tolling; internal tolling

### **Introduction**

Further liberalization and development of the economy of our republic, formation of new economic legislation, as well as the increase in the independence and responsibility of accounting entities entail the need to investigate the methodological and organizational aspects of enterprise management in reliance upon a new approach.

The President of the Republic of Uzbekistan Sh.M. Mirziyoyev has mentioned: “Under market conditions both the product supplier and the consumer must entirely fulfill their contractual obligations. The management system in the economy is outdated, efficient mechanisms for supporting innovative ideas have not been introduced on time, and it still remains a serious problem. In addition, technological backwardness, resource and energy-saving technologies, slow implementation of alternative energy sources represent obstacles to economic development. The demand of the market economy is such that access to resources and opportunities, that is, the scope of business, should be equal to everyone. From this point of view, it is not fair that the import of products required for the needs of the population into our country is accumulated in the hands of only certain groups and has become the source of their income”[2].

The Decree №4947 of the President of the Republic of Uzbekistan “On the Action Strategy for further development of the Republic of Uzbekistan” adopted in 2017 sets the task of “ensuring the balance and stability of the national economy, raising the share of industry in its structure”[3]. In this regard, further development of the industry, production of high value-added finished products based on deep processing of local raw materials, modernization and diversification of the industry, reduction of production costs, as well as creation of a competitive environment are of

particular importance in terms of solving problems. Moreover, one of the main objectives is to attract foreign enterprises to carry out processing (tolling) operations within the territory of the Republic of Uzbekistan in order to effectively use the idle production capacities of the industrial enterprises of the republic.

The Regulation “On the procedure for reflecting operations related to raw materials supplied for processing in accounting” was adopted according to the order of the Minister of Finance of the Republic of Uzbekistan [4]. This Regulation sets the procedure for accounting operations related to raw materials for processing in accordance with the Law of the Republic of Uzbekistan “On Accounting”. This fact justifies the relevance and practical significance of the topic of this article in terms of the implementation of the tasks defined in these statutory acts.

### **Literature Review**

Tolling is a widespread production in world practice, where the name is used as “raw materials supplied for processing”. Supplied raw materials are raw materials that are exported to another country for processing and then brought back to the country in the form of finished products. In a broad sense, “tolling” and “tolling operations” determine the method of organizing the processing of the supplied raw materials and the various methods of manufacturing the products from the processed raw materials and settlements made for such products. Tolling operations are classified as export services. Tolling agreement is an agreement concluded between the customer and the enterprise that provides services for the processing of a certain amount of raw materials within a certain period of time. Raw materials supplied for processing are exempted from customs duties, including value added tax, and the value added tax paid is refunded when the finished product crosses the border during export.

In the opinion of L. V. Postnikova, tolling represents one of the forms of using raw materials under special customs control. Furthermore, she defines tolling operations as “foreign economic cooperation between enterprises of various countries, in which raw materials and semi-finished products of one enterprise are supplied to another enterprise for further processing, and then a finished product is obtained from the raw materials provided” [5].

According to A.G. Burkova, tolling is a relationship between economic entities, in which the owner of raw materials transfers it to a partner enterprise for processing, as a result of which he receives a finished product and covers the costs of processing and a certain part of the revenue [6].

N.N. Parasotskaya describes tolling as the transfer of raw materials and consumables to a third party for processing, and related operations are defined as operations of processing raw materials and consumables [7].

In reliance upon the foregoing considerations, we should emphasize that processing of the raw materials supplied by the customer and tolling are considered the same in the economic literature. As a result, it entails the fact that enterprises organize accounting and tax reporting of economic activities not in the right way. These concepts have the following aspects in common: that is, the customer and the contractor are considered as two economic entities, while the ownership of the processing plant is retained and the finished product is provided to the customer as a legal result during the performance of the contract. These operations mainly serve to perform certain types of activities.

There are also a number of differences that significantly affect accounting and tax reporting. In terms of tolling, not only raw materials, consumables, but also goods and services (repair, restoration, replacement of parts) are considered as objects for processing. Tolling carries out operations under customs control and under special taxation procedure.

Nevertheless, as a result of the analysis of a number of research papers and educational literary sources, as well as practical manuals, we can see that the existing problems in the development of accounting and reporting of tolling operations have not been studied at the adequate level. Moreover, theoretical and methodological aspects of accounting of business transactions between the enterprise processing raw materials and the customer have not been developed as a

single object. Solution of these problems is of great practical importance within the framework of developing financial reports based on international standards.

### DATA and Methodology

Such research methods as observation, generalization, grouping, comparison, theoretical and practical study and accounting methods have been widely used in this research paper.

The Regulation “On the procedure for reflecting operations related to raw materials supplied for processing in accounting” is a statutory act that determines the procedure for implementation of tolling operations at the industrial enterprises of the republic [4].

In accordance with this Regulation, processing operations carried out within the territory of the Republic of Uzbekistan shall mean operations performed with foreign persons and related to the following aspects:

- processing and handling of goods;
- repair of goods, including their restoration and bringing to rights;
- production of goods, including assembly, installation and adjusting them in compliance with other goods;
- full or partial use of goods that help or facilitate processing.

The amount of import customs duties and taxes paid when the goods are brought to the industrial enterprise for processing will be refunded when the processing products are exported again from the customs territory.

There are external and internal types of tolling. In case of external tolling raw materials are usually imported from abroad under state control and without paying customs duties and taxes. Internal tolling involves the processing of raw materials received from enterprises in other regions of the country.

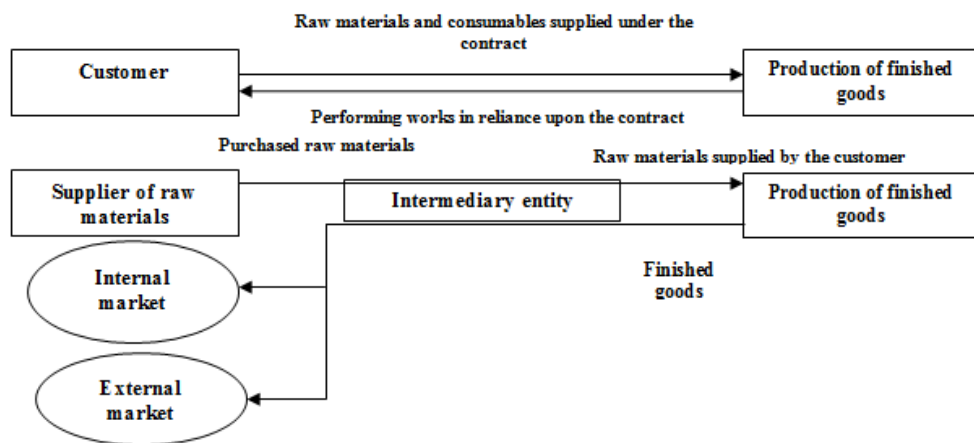


Figure 1. Flow chart of economic transactions by external tolling

Source: Developed by the author in reliance upon the research results.

Obligatory requisites of the initial documents compiled by the customer and the tolling party, the procedure for their preparation, acceptance, storage, as well as the procedure for the document flow are regulated in accordance with article 14 of the Law of the Republic of Uzbekistan “On Accounting” [1] and the Regulation on the document flow in accounting.

Industrial enterprises will have to conclude a contract with enterprises for the processing of foreign goods according to the established procedure. The contract must contain the following provisions:

- value and quantity of foreign goods imported for processing;
- procedure for accepting materials for processing by quality;
- quantity and value of local raw materials and consumables used in processing;
- value and quantity of finished products;
- terms for processing and value in freely convertible currency (hard currency);
- terms of delivery of the finished products;
- payment conditions, forms and terms;
- the responsibility of the tolling party for the inefficient and non-targeted use of the received materials;
- other conditions depending on the wishes of the parties.

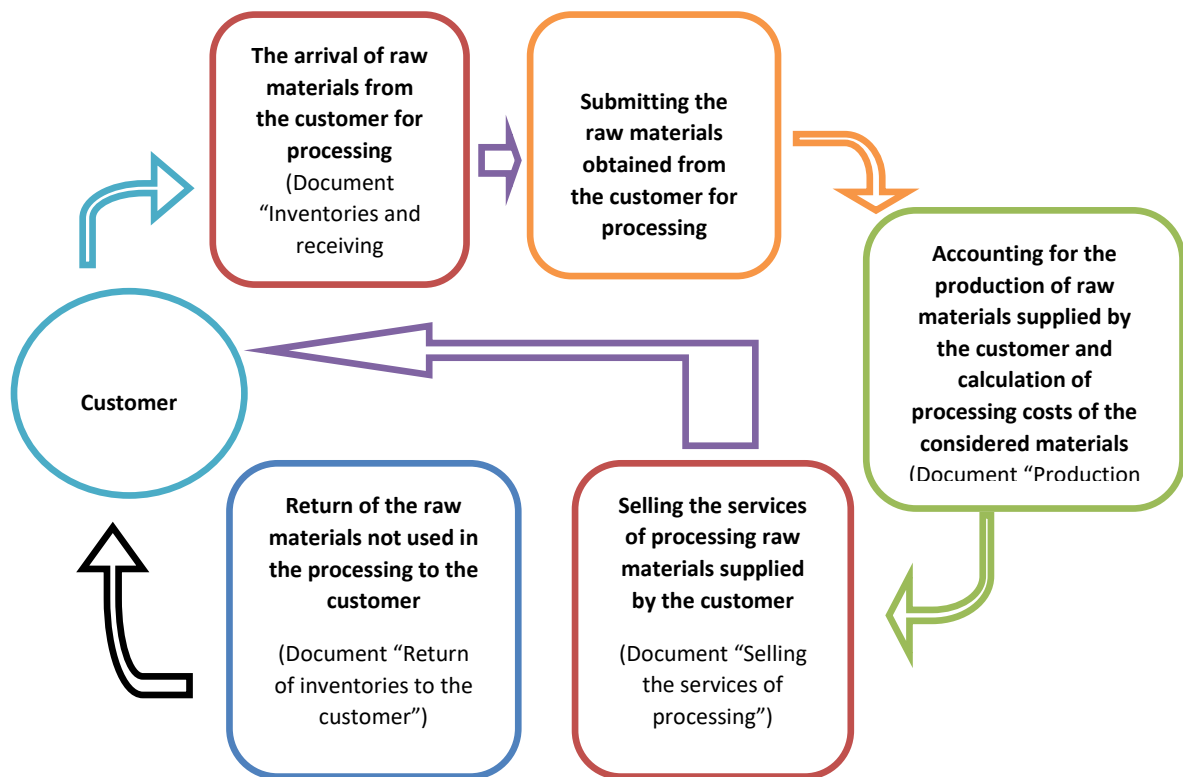


Figure 2. The process for processing raw materials supplied by the customer

Source: Developed by the author in reliance upon the research.

When raw materials supplied by the customer provided to the tolling party, their value is not written off from the balance sheet, but is taken into account in the account “Materials supplied for external processing” according to the value recorded in the accounts, which account for other relevant materials.

The work performed on the processing of raw materials supplied by the customer is debited to the accounts where the products obtained directly from the processing are taken into account, and if the products obtained from the processing are of a direct nature:

- a) if the core business represents production of finished products (performance of work, provision of services) - in the accounts accounting for the main production;
- b) if it refers to auxiliary production serving the main production or the core business of the entity - in the accounts accounting for auxiliary production;
- c) if it refers to the use for the purposes of general production - in the accounts accounting for general production expenses;
- d) if it refers to eliminating of unusable products in production - in the accounts accounting for unusable products in production;
- e) if it refers to use in the needs of service enterprises - in the accounting accounts of service enterprises;
- f) if it refers to the customer's warehouse for future use in economic activity - it is taken into account in the accounts accounting for the relevant materials.

### **Results And Discussion**

Interactions between the industrial enterprise and customers according to the type of the core business are defined as follows:

- with domestic customers - by the goods supply contract;
- with foreign manufacturers - by an export contract for the supply of products;
- with a tolling contract for the delivery of finished products instead of raw materials;
- with a contract for remanufacturing finished products from supplied raw materials;
- with the contract for implementation of various works and services by the enterprise.

In our opinion, it is possible to single out the following aspects of the advertisement during the operations of industrial enterprises:

- 1) the contract is balanced, currency-free, pre-valued and usually long-term, as it envisages a long-term and stable relationship between the parties;
- 2) the mutual obligations of the parties on the export of raw materials and import of finished products shall be formalized by a single notice;
- 3) raw material cost, processing cost and finished product cost will have to be evaluated;
- 4) at the time of signing the contract there are determined mutual obligations of the parties are determined and production costs, labor costs, transport costs, customs payments, etc.;
- 5) delivery of the supplied raw material not only covers the agreed costs of the tolling party, but also ensures his planned income. For this purpose, the globally admitted values of raw materials and processing products are indicated in the contract;
- 6) claims for overdue delivery or claims regarding the quality of raw materials and its processing products are made by changing the amount of raw materials delivered;
- 7) payment of fines and damages are mainly in kind rather than money.

Operations on the raw materials supplied are included in the foreign trade turnover at the value of the processing of the supplied raw materials:

- to the export of the country that processes it;
- to the import of the country that owns the raw material being supplied.

In tolling, the raw materials supplied for processing do not become the property of the tolling party, but remains the property of the supplying party. The supplier provides the raw materials for the production of the partner and assumes the risks of sale as the owner of the property. The tolling party does not produce a finished product, but performs work on the processing of raw materials into such an environment and receives payment for processing services in the form of cash or raw materials (finished products), and in this case undertakes responsibility for the material support of production and the sale of finished products. When foreign goods are imported to an industrial enterprise for processing, they are placed in the customs regime according to the following documents:

- customs cargo declaration;
- contract;
- transport and transport tracking documents for processing goods (bills of lading, invoices, transportation permits, etc.);
- copy of the processing license, etc.

The terms of processing goods are determined by the customs authority, taking into account the duration of the process of processing goods and the ownership of their products being processed.

The output amount of processing products is determined by the contract. In this case, the customs authorities will be able to determine the compulsory output amount of processing products resulting from the processing of goods for customs purposes.

During tolling operations, the value of processing confirmed by the settlement calculation and included in the processing contract is a source of income. Settlements with the tolling party processing the goods are made both in monetary terms and in kind (for example, with processing raw materials or finished products).

Income in foreign exchange received for the processing of goods serves as an object of compulsory sale in accordance with the established procedure. The amount of compulsory sale of foreign exchange earnings (50 percent for export) is determined regardless of the form of calculation of the value of processing provided based on the contract.

Export of the finished product after processing on the basis of contracts concluded on the basis of payment in cash with the presence of a bank certificate confirming the receipt of foreign exchange income for processing and indicating the amount of currency on the basis of contracts concluded with the condition of payment of fees with imported raw materials (goods) is allowed if there is a document confirming mutual settlements with the imported raw materials (goods).

According to the established procedure, the customs authorities submit the customs cargo declaration registers to the authorized banks. After the completion of mutual settlements between the parties of the processing note on processing and the forced sale of a part of the foreign exchange proceeds, the bank and the customs authority will remove the note from the account.

According to the statements specified above, the materials supplied for processing remain the property of the supplier. Therefore, accounted at the tolling party, their value is reflected in the off-balance sheet "Materials accepted for processing". All subsequent costs are reflected in the account in the general order, that is, they are calculated in the "Main production" account, and the finished product is transferred to the warehouse (for export) as material assets accepted for responsible storage (table 1).

Table 1: Representation of the operations on the processing of the supplied raw materials at the tolling party

| Indicators                                                   | Debit                               | Credit |
|--------------------------------------------------------------|-------------------------------------|--------|
| The origin of materials supplied for processing is reflected | "Materials accepted for processing" |        |

|                                                                                 |                                                  |                                                                                                                                                     |
|---------------------------------------------------------------------------------|--------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------|
| The costs of processing the supplied raw materials (goods) are reflected        | “Main production”                                | “Accounts for accounting for depreciation of fixed assets”; “Settlements with employees on wages”; “Payments to the public targeted funds” and etc. |
| The finished product was transferred to the warehouse at the cost of processing | “Goods/material assets accepted for safekeeping” |                                                                                                                                                     |
| The supplied raw materials (goods) are written off                              |                                                  | “Materials accepted for processing”                                                                                                                 |
| Income from processing services is reflected                                    | “Accounts received from customers and suppliers” | “Income from performing works and providing services”                                                                                               |
| The cost of processing services is written off                                  | “Cost of works performed and services rendered”  | “Main production”                                                                                                                                   |
| Receipts received for processing the raw materials supplied                     | “Accounts for cash in foreign exchange”          | “Accounts received from customers and suppliers”                                                                                                    |

If it is envisaged to pay for the service provided by the enterprise with raw materials or finished products, they should be reflected in the debits of the following accounts for further use, i.e. as raw materials, consumables, finished products, etc. in the account “Accounts received from the buyers and customers” in relation with the credit:

Debit of “Accounts for accounting materials” (by the prime-cost of raw materials according to the contract).

Debit of “Finished products in warehouse” (by the prime-cost which includes raw materials and processing cost).

Credit of “Accounts received from buyers and customers”.

Operations related to raw materials supplied by the customers are reflected in accounting as follows:

when raw materials supplied by the customer are transferred for processing:

debit of “Materials supplied for external processing” account – by the amount of the raw materials supplied, by the value accounted at the customer;

credit of accounts accounting for materials;

when advance payments are made in the amounts envisaged on the contract for raw materials supplied for processing:

debit accounts accounting for advance payments made to suppliers and contractors – to the advance payment amount;

credit of accounts accounting for cash;

when the cost of raw materials supplied refers to production costs:

debit accounts accounting for main production, accounts accounting for auxiliary production, accounts accounting for general production costs, accounts accounting for defective products in production, accounts accounting for entities, which render services;

credit of “Materials supplied for external processing” account;

when the value of the work performed on the processing of raw materials supplied by the customer is included in the production costs and if the product obtained from the processing of raw materials supplied by the customer, is given by the customer directly to the production of products (performance of work, provision of services):

debit accounts accounting for primary production, accounts accounting for auxiliary production, accounts accounting for general expenses, accounts accounting for defective products in production, accounts accounting for servicing entities;

credit of “Accounts payable to suppliers and contractors”, “Accounts payable to separate divisions”, “Accounts payable to subsidiaries and affiliates”, “Other liabilities” account and accounts which account for other liabilities;

when the product obtained from the processing of raw materials supplied by the customer arrives at the customer’s warehouse for further use in economic activities:

accounts which account for debit of materials;

credit of “Materials supplied for external processing” account;

when the value of the work performed on the processing of raw materials supplied by the customer is taken to the value of the product obtained from the processing of raw materials supplied by the customer and if the product obtained from the processing of raw materials supplied by the customer is directly received in the customer’s warehouse for further use in economic activities:

accounts, which account for debit of materials;

credit of “Accounts payable to suppliers and contractors”, “Accounts payable to separate divisions”, “Accounts payable to subsidiaries and affiliates”, “Other liabilities” account and accounts which account for other liabilities.

Taking into account the value of services for the processing of raw materials (materials) provided as a turnover for sale by the enterprise as the tolling party, the customs declaration (invoice) is issued by the tolling party only for the value of processing.

Raw materials and consumables received for processing from the supplier are not considered the property of the enterprise and therefore cannot be taken into account in its balance sheet. This property should be recorded in the off-balance sheet account “Materials accepted for processing”.

The following sub-accounts can be opened for consumables and raw materials sent to the warehouse for processing:

- “Materials and stocks at the warehouse”;
- “Materials and stocks at the processing”.

There is an analytical account of the materials and stocks provided to the industrial enterprise in terms of customers, names, quantities and prices, as well as their storage and processing locations. The processing costs themselves are accounted for in the basic production account in connection with the accounts of the tolling party’s own materials, wages, depreciation, taxes, and general production costs.

In the industrial enterprise, until the finished product is delivered to the customer, consumables and materials are accounted for in the “Materials accepted for processing” account.

During processing, in addition to the cost of consumables and materials, the owner must include the rest of his expenses in the cost of the finished product - transport, business trip, general production and other costs.

In some cases, processing may result in material that needs to be further processed, rather than a finished product. In this case, the received property is reflected in the “Materials and stocks” account by the supplier, and the cost of processing is focused on increasing the value of the received materials.

In the industrial enterprise, not all raw materials and consumables received by the processor during the production process are consumed - waste inevitably occurs. At the same time, they will somehow have a certain value that needs to be taken into account.

In this case, according to the contract, the output remains at the processor free of charge, and - the value of the raw materials and materials sent for processing is recorded to the credit of the “Materials received for processing” account, and it is accepted into the “Materials and stocks” account at the same time.

## **CONCLUSION**

Raw materials supplied by the customer are taken into account in the off-balance sheet “Materials accepted for processing” account at the price stipulated in the contract on processing raw materials supplied by the customer.

In the author’s opinion, in this case it is appropriate to use the off-balance account “Goods accepted for safekeeping” because, after processing is completed, materials and stocks transfer their value to the finished product.

In order to ensure the control of the flow of raw materials supplied by the customer it is necessary to maintain a “Record of accounting raw materials supplied by the customer” in accordance with the Regulation “On the procedure for reflecting operations related to raw materials for processing in accounting”. The record of accounting raw materials supplied by the customer” signed by the head of the tolling party and authorized persons in accordance with the procedure established by law. In this record, the data about the reduction of the quantity and total indicators of raw materials supplied by the customer is indicated by the sign “minus” in the appropriate line of its types.

The cost of work performed on the processing of raw materials supplied by the customer is recognized at their production prime-cost, including the costs directly related to the processing of raw materials supplied by the customer based on the technology and organization of production.

The composition of costs included in the production prime-cost of the works performed on the processing of raw materials supplied by the customer is implemented in compliance with “Regulation on the composition of costs of production and sale of products (works, services) and the procedure for the formation of financial results” approved by the decision of the Cabinet of Ministers of the Republic of Uzbekistan №54 dated February 5, 1999.

The costs of delivering the product obtained from the processing of raw materials to the customer, carried out by the tolling party, are not added to the production cost of the work performed on the processing of raw materials supplied by the customers, but are referred to the period expenses.

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