

BASIS FOR THE DECISION TO REMOVE FROM THE RECORDS OF TAXABLE PERSONS REGISTERED FOR VAT IN ROMANIA SINCE 2011

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Abstract:

Since 2011, the persons registered for VAT in Romania finally have the right to apply for special exemption regime. This right is inserted in OUG 117/2010 and is conditioned by obtaining taxable income in the previous year less than the threshold for exemption. In this paper I want to underline both the advantages and disadvantages of such decision, both in terms of taxation and accounting.

Key words: VAT adjustment, threshold for exemption, accounting, taxation, exemption regime

JEL classification: H32, M41, M48

1. INTRODUCTION

The value added tax influences the cash flows of an entity through both the gap between the maturity date and the actual term of cashing from customers, as well as through pro-rata (when it is less than 100%), even if the Ministry of Public Finance deems it to have a neutral nature. For this reason, any entity must always base its decision to register as VAT payer or even be removed from the records of taxable persons registered for VAT.

From 2011, the Fiscal Code of Romania has made a significant amendment in this area, meaning that the special exemption may apply whenever the turnover¹ recorded in the previous year is below the threshold for exemption of EUR 35,000 (RON 119,000). Prior to this amendment, the entities that exceeded the threshold for exemption or opted to become VAT payers had no legal possibility to be removed from the records of VAT registered persons regardless of the annual turnover achieved. Therefore, a VAT payer could never return to the non-taxable status.

Fortunately, since 2011 the entities may request² until January 20 of the next year to be removed from the records of VAT registered persons in order to apply/re-apply the special exemption regime, in compliance with the threshold for exemption. Cancellation of VAT registration is valid from the first day of the month following the request for removal from the records, namely from February 1.

Therefore, after changing the records' conditions (taxable person/exempted from VAT) there comes the requirement to make all the VAT adjustments, both for capital goods (Art. 149 of the Fiscal Code) and for other goods and services (Art. 148 of the Fiscal Code). Such adjustments should be included in the VAT (to be submitted by 25 February) for the operations carried out in January.

¹ Art. 152, para. (2) of the Fiscal Code, as amended by section 75 of the Emergency Ordinance no. 117/2010 with effect from 01/01/2011.

² Art. 152, para. (7) of the Fiscal Code, as amended by section 75 of the Emergency Ordinance no. 117/2010 with effect from 01/01/2011.

The purpose of this paper is to analyze these adjustments themselves and issue some tax recommendations on the basis for the decision to remove from the records of persons registered for VAT that may apply again the special exemption regime together with the accounting implications of such decision.

2. FISCAL ANALYSIS OF VALUE ADDED TAX ADJUSTMENT FOR AN ENTITY THAT APPLIES AGAIN THE SPECIAL EXEMPTION REGIME STARTING WITH 2011 (FEBRUARY 1)

The change of the tax regime (from taxable operations into exempt operations and vice versa) is for any entity a mandatory value added tax adjustment event. The adjustment is made for each event, leading either to reduction in the value added tax previously deducted when capital goods are no longer used for economic purposes (serving to the activity exempt from value added tax) or when the entity is removed from the records of persons registered for VAT (adjustment for the state) or to increase in the input tax in the opposite situation (adjustment for the entity).

If the VAT tax regime changes (as happens when implementing again the special exemption regime) the entity must adjust the VAT both for the capital goods and for the other goods and services for which VAT was previously deducted and which are in stock.

For the capital goods purchased or manufactured/ upgraded for which VAT was previously deducted in the adjustment period (last 5 or 20 years³), the tax will be adjusted for the state with one-fifth or, where appropriate, one-twentieth of the initially deducted VAT for each year, until the end of the adjustment period. The adjustment period is determined taking into account the period from the date of purchase/manufacture or the commissioning date (but not earlier than January 1, 2007 - the year of accession to the EU) and until the date of the event that generates the adjustment (for example the implementation of the special exemption regime). In this respect, it is considered, regardless of the calendar date on which the purchase /manufacture/ commissioning, a full year and the last year (where the adjustment is made) is not taken into account.

For example, for an entity which applies again from February 1, 2011 the special exemption regime and which purchased a car with a useful life of seven years in December 2008 and for which the VAT of RON 6,000 was deducted, VAT will be adjusted for the state at a rate of two-fifths representing RON 2,400 (December 2008 is considered one year, 2009 and 2010, one year each, and January 2011 is not taken into account, resulting thus 3 years of the enacted 5 year adjustment period, therefore from the 5 years remained 2 for adjustment), amount that will be included in the statement of January 2011 (on input tax adjustments = RON -2,400). The same calculation (for the same entity) also takes place for a building purchased in March 2007 for which VAT was deducted in the amount of RON 38,000 (regardless of the date when 2007 begins, 2007 will be considered a full year and the last, respectively January 2011 is not taken into account; therefore from the period of 20 years only 4 years have passed) for which there will be adjusted the VAT already deducted in 2007 at a rate of 16/20, respectively for the amount of RON 30,400. In the statement of January 2011 at position 29 "adjustment for capital goods" the amount of RON 32,800 will be entered with a dash (i.e. RON 2,400 + RON 30,400; this amount will increase the VAT payable from the same period).

As I mentioned earlier, if inside the adjustment period (5 or 20 years) there occur events generating adjustment, then successive adjustments will be made for the same

³Art. 149 para.(1) of the Fiscal Code.

capital good, regardless of the number of such events.

For example, if during 2011 the entity in the above example will exceed the threshold for exemption in November 2011 (until December 10, 2011 the entity will submit an application to be entered in the records of persons registered for VAT), returning to the taxable regime in January 2012, will make the following adjustments for capital goods:

- for the car: of the 5 years (the legal period of adjustment) 4 years have passed (2008, 2009, 2010 and 2011), then making the adjustment for the entity for a fifth of the initial amount of RON 6,000, filling out in the statement for January 2012/ 1st quarter of 2012 input VAT + RON 1,200. Therefore, of the RON 6,000 initially deducted in December 2008 (with the purchase) the entity adjusted in January 2011 RON 2,400 for the state (ie deducted only the difference in the amount only RON 3,600), and in January 2012 adjusted for itself RON 1,200 (reaching a total of RON 4,800 of the RON 6,000 initially deducted);
- for the building: of the 20 years representing the mandatory period of adjustment 5 years have passed (March 2007 - December 2011), and will therefore adjust for itself 15/20 of the amount initially deducted in March 2007 of RON 38,000 and RON 28,500 (which will be entered in the statement as a positive amount to be deducted);
- in the statement of January 2012/ 1st quarter, at position 29 “adjustment for capital goods” the amount of RON 29,700 will be entered (i.e. RON 1,200 + RON 28,500)

If the entity exceeded the minimum threshold during 2011 and were registered as a VAT registered person at the latest starting with December 2011 then, in the first statement filed for 2011 (for the period when it becomes a VAT payer) it will adjust the entire value added tax for capital goods (car and building) in its favor, namely the amount which was found at position 29 in the statement of January 2011 (RON - 32,800), but this time with a “+” (will reduce VAT payable from the period related to that statement)/

It is worth making the following statement on the adjustment of capital goods:

- the input VAT adjustment is made within the period of adjustment only in the following cases⁴: the capital good is used wholly or partly for purposes other than the economic activities, for making transactions which are not tax deductible, namely for making transactions which are tax deductible in an extent different from the initial deduction; the capital good ceases to exist and is not subject to supply; the capital good was originally wholly/partially exempt from VAT, and then subject to a transaction for which tax is deductible; for the cases where there are changes in the factors used to calculate the tax deducted;
- there will not be an input tax adjustment for capital goods, if the amount that would result from the adjustment of each capital good is less than RON 1,000;
- the entity is required to enable control of the input tax and adjustments made, namely it must keep a statement of the capital goods which are subject to the input tax adjustment for a period commencing when the tax for the capital good purchase becomes due and ending 5 years after the expiry of the period during which adjustment may be claimed. Any other records, documents and ledgers on capital goods must be retained for the same period;

⁴Art. 149 para. (4) of the Fiscal Code.

- the input value added tax⁵ related to the transformation or modernization of a property or part thereof, which lead to an increase in the property value is adjusted by the person provided with the property or part thereof, if the transformation or modernization work is made by this person, and the value of each transformation or modernization is at least 20% of the total value reassessed after the transformation or modernization of the property or part thereof;
- the adjustment of the input tax for goods subject to lease, concession or any other method of provision to a person shall be made by the lessor, person who leases or provides the goods to another person;

For other goods and services⁶ in stock, other than capital goods, adjustment shall be made only if there is no supply/service to itself, which is carried out by the taxable entity.

Such adjustments are seen mostly as a result of legislative changes (as were those implemented by the Government Emergency Ordinance no. 117/2010) or due to changes in the scope of business, changes that either determine the transactions that did not have a deduction right to become taxable (including by using those goods/services to carry out taxable transactions with deduction right) or that certain transactions for which VAT was deducted to lose the deduction right (implicitly by applying again the special exemption regime).

Thus the entity **may** adjust the VAT (has the right, without being bound) for unused services, goods such as inventories and tangible fixed assets (which have a lifespan of less than 5 years and therefore were not considered capital goods) in stock, as inventory, on the registration of persons registered for VAT purposes. This adjustment has the effect of exercise of the deduction right for goods and services in stock (do not forget that the entity has borne the entire VAT related to purchases for the entire period in which the special exemption regime was granted)

If the entity has been registered for VAT and deducted the VAT related to unused goods and services in stock, it will be **required** to adjust the VAT on the date of reapplication of the special exemption regime. In the first case, the adjustment involves increasing the tax to be deducted, and the second case its decrease, to the amount representing the tax related to unused goods and services in stock upon changing the tax regime, tax to be entered in position 28 of the statement "Adjustments of the tax to be deducted". In the same time, for the first case a file shall be made regarding the tax on all unused goods and services in stock, which is submitted to the Ministry of Public Finance for approval of the tax related to them as deductible. The adjusted tax to be deducted for the goods and services in stock at the time of application of the normal tax regime is determined based on the ledger of sales and purchases made by the entity that applied the special exemption (in such ledgers the entity recorded the supplies of goods and services that would have been taxable unless made by a small business, and it also recorded the taxable goods and services purchased).

According to the purpose stated in the introduction to this article, I will continue to focus on the analysis of adjustments arising from the reapplication of the special exemption regime (removal from the records of persons registered for VAT). Thus, with the application of the special exemption regime with effect from February 1, the entity loses the right to deduct tax for undelivered movable property and unused services. Therefore, the entity will need to adjust the input tax for services and goods unused

⁵ Methodological Norms for applying Law no. 571/2003 concerning the Fiscal Code, section 54, amended by section 39 in the Decision no. 1620/2009 effective from 01/01/2010.

⁶ Methodological Norms for applying Law no. 571/2003 concerning the Fiscal Code, section 53.

when the change occurred. The adjustment represents in this case the cancellation of the right to deduct the VAT initially deducted⁷. For example, if the entity that will apply again the special exemption regime from February 1, 2011 had in stock (based on inventory) on January 31, 2011 property such as inventory supplies and goods worth RON 10,000 for which it had previously deducted VAT in the amount of RON 2,400 (consider that they have been purchased after July 1, 2010, that the VAT rate was 24%) will adjust that amount (RON 2,400) by entering in the VAT column with a dash, on position 28 of the VAT for January 2011 ("Adjustments of the tax to be deducted") and in the "value" column (from the same position in the statement) the amount of RON 10,000 with a dash.

3. ACCOUNTING ISSUES REGARDING VTA ADJUSTMENT FOR AN ENTITY THAT APPLIES AGAIN THE SPECIAL EXEMPTION REGIME STARTING WITH 2011 (FEBRUARY 1)

From an accounting perspective, the reapplication of the special exemption regime requires the reflection of the value added tax adjusted for the state (as we noted in section 2) related to the capital goods and other goods and services in stock before the change of the tax regime:

$$635 \text{ "Other taxes,} \quad = \quad 4426 \text{ "Input VAT"} \\ \text{duties and similar liabilities"} \quad \quad \quad$$

According to the example in section 2, for the capital goods there will be registered the VAT adjustment for the amount of RON 32,800 in January 2011 (being also entered as a minus amount in the statement of the same month, at position 29):

$$635 \text{ "Other taxes,} \quad = \quad 4426 \text{ "Input VAT"} \quad 32,800 \\ \text{duties and similar liabilities"} \quad \quad \quad$$

The same registration takes place at the VAT adjustment related to the other goods and services in stock on January 31, 2011 (the amount being entered with a dash at position 28 in the statement of that month):

$$635 \text{ "Other taxes,} \quad = \quad 4426 \text{ "Input VAT"} \quad 2,400 \\ \text{duties and similar liabilities"} \quad \quad \quad$$

The expenses collected in the account 635, when adjusting the value added tax, are deductible when calculating the income tax⁸.

If the new entity exceeds again the annual exemption limit (which is determined in proportion to the period from which the special regime applies, i.e. from February) the adjustment for the entity, as specified in section 2, will be reflected by the red reversal of the previous accounting article (with related references in the statement of first month from returning to the taxable regime).

4. CONCLUSIONS

The basis for the decision to remove from records of taxable persons registered for VAT (reapplication of the special exemption regime) involves comparing the benefits from changing the tax regime with the financial disadvantages caused by the

⁷ Methodological Norms for applying Law no. 571/2003 concerning the Fiscal Code, section 53, para. (6).

⁸ Methodological Norms for applying Law no. 571/2003 concerning the Fiscal Code, section 23, point b.

requirement to achieve value added tax adjustment as specified in section 2.

We have on the one hand, benefits such as cash flow decongestion as, since is no longer a VAT payer, the entity no longer suffers from gaps between the maturity date and the actual term of cashing VAT from customers, nor from the application of a prorate less than 100%. However, small entities (because we are talking about them) may reduce their tariffs or sales prices and thus become more competitive. Finally, the entities carrying out within immaterial activities mainly in the non-material sphere (service provision) are favored by the appreciation of the special exemption regime (they recorded a low proportion of input VAT and therefore arrived in a position to collect VAT for the state, without receiving almost at all the right of deduction). Let's not forget the advantage of simplifying the accounting records and the documents produced for the VAT exempt entities.

The major disadvantage of reapplication of the special exemption regime with effect from February this year (as from 2011) is the financial effort that is required with the VAT adjustment because they have both the obligation of determining the adjustment to the state for the capital goods held on January 31 (within the period of 5 or 20 years) and the other goods and services in stock at the same time, but especially the obligation to pay these amounts until February 25. From the examples given in section 2, only for capital goods entity is required to make an additional payment (generated by the VAT adjustment) of RON 32,800.

In conclusion, each entity must base its decision to reapply the special exemption regime; the payment amounts resulting from the VAT adjustment are a key indicator.

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