

LEGAL, FISCAL AND ACCOUNTING PECULIARITIES REGARDING THE AUTHORIZED CAPITAL INCREASE

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Abstract:

The matter regarding the increase of the authorized capital is of complex nature. In order to shed light on this, quite a substantial baggage of legal, fiscal and accounting knowledge is required. In this paper we engage in building a synthesis of the aspects which characterize the operations regarding the increase of the authorized capital. In the first part we depicted a few aspects regarding the size and the segments of the authorized capital; the elements and the form of the articles of association; the competence of the capital increase authorization; the form of the addendum to the articles of incorporation in the case of the authorized capital increase. The practical part of the paper resides in the presentation of two case studies. The former regards the capital increase by incorporating other elements of the owned capital.

Key words: authorized capital, increase, receivables, profit, tax

JEL classification: M41

Theoretical aspects regarding the authorized capital

Joint stock companies and limited liability companies are incorporated through articles of incorporation and articles of association, exceptions being made for limited liability companies with a sole shareholder, where the incorporation is made solely through articles of association.

The articles of incorporation and articles of association must be prepared and filled in as a sole document called “constitutive act”. When only one of them is filled in, that document will be called constitutive act.

The constitutive act is concluded under private signature, signed by all the associates or, in case of public subscription, by all the founders.

The authentic form of the constitutive act is mandatory when: 1) there is a real estate property among the goods which were subscribed as contribution to the authorized capital; 2) a general partnership or a limited partnership is established; 3) the joint stock company is established by public subscription.

Where joint stock companies and partnerships limited by shares are concerned, the authorized capital is divided in equal value shares and must not be under 90.000 lei. The number of shareholders in a joint stock company must not be under 2. The minimum face value of a share is 0,1 lei.

In the case of limited liability companies, the authorized capital cannot be under 200 lei and it's divided in equal value shares which cannot be under 10 lei. The shares must not be represented by negotiable instruments. In a limited liability company the number of the shareholders must be under 50.

Increasing the authorized capital

Until the Governmental Emergency Ordinance no. 82/2007 entered into force, the limited liability companies had no legal grounds for the increase of authorized capital. Their constitutive act provided that they could increase the authorized capital in

compliance with the legal provisions on this matter. Against all odds, the Companies Act no. 31/1990 did not bring this matter under regulation.

The article 221 of the Law no. 31/1990 has been modified by the GEO no. 82/2007. According to this modification, limited liability companies may increase their authorized capital through the same means and from the sources provided for the joint stock companies in article 210.

A summary of the legal means to increase the authorized capital in joint stock companies and limited liability companies shall be presented in the following table:

Means of increasing the capital	Financing the increase	
Supplementing the number of equity investments (stocks or shares)	In return of new cash contribution or/and contributions in kind;	The equity investments are paid by the contributors to the authorized capital
Increasing the face value of the securities		
Supplementing the number of equity investments (stocks or shares)	By incorporating reserves, except legal reserves and benefits or share premiums;	Free distribution
Increasing face value of the securities		
Supplementing the number of equity investments (stocks or shares)	By compensating liquid and exigible receivables with stocks/shares of the company.	

Increasing the authorized capital by incorporating other privately owned equity

According to the legal definition, as stated in article 7 (12) of the Fiscal Code, the dividend „is a distribution made in cash or in kind, by a legal person, to a contributor to that legal person, as a result of his/hers equity ownership in that particular legal person, except the following types: a) distribution of supplementary equity instruments which does not modify the percentage of equity ownership of all the participants; e) distribution of share premiums proportional to every participant’s share in the company.”

In practice, dividends are frequently distributed to the participants in a company from the net profit, depending of the provisions of the constitutive act.

An unusual situation arises when the increase of authorized capital is made by using privately owned equity. The sums used for this purpose (profit, share premiums, reserves – not legal reserves though) are not considered dividends if supplementing the equity does not lead to the modification of the percentage owned by each stockholder/shareholder.

Nonetheless, the fiscal law vaguely refers to supplementing the number of equity instruments. For this reason we believe that, in case of an increase in the face value of stocks/shares, used, privately owned equity would be given the same treatment as dividends, irrespective of the modification of the percentage owned by the participants.

To back up this information we must recall that the incorporation of personal equity instruments can be achieved by:

- Increasing the number of the equity instruments: art. 210 (2) of the Companies’ Law;
- Increasing the face value of the equity instruments: art. 210 (4) of the Companies’ Law;

In order to apply the tax regulations regarding sums destined for the increase of authorized capital we further present the case of a company which had an authorized capital of 90.000 lei, made of 36.000 shares with a face value of 2,5 lei. The shares belonged to two shareholders. One shareholder owned 99, 97% of the authorized

capital, i.e. 35.990 shares, the second one owned 0, 03% of the authorized capital, i.e. 10 shares. The positive result was 20.000 lei, the share premiums were 5.000 lei

If the increase of authorized capital is to be carried out by the issuance of 8.000 shares, with a face value of 2, 5 lei, of which 90% will be distributed to the main shareholder and the 10% difference to the minority shareholder, it's obvious that the increase modifies the percentage initially owned by the participants.

Summary of the shareholders' structure modification:

Running no.	Shareholder	Initial situation		Increase of authorized capital		Final situation	
		Share no.	P%	Share no.	P%	TA	P%
1.	A 1	35.990	99,97	7.200	90	43.190	98,16
2.	A 2	10	0,03	800	100	810	1,84
Total		36.000	100,00	8.000	100	44.000	100,00

In order to increase the authorized capital by issuing 8.000 shares, financing sources of a total net value of: $8.000 \times 2,5 \text{ lei} = 20.000 \text{ lei}$ are necessary. The increase caused the modification of the percentage owned by each shareholder and the sums used for this purpose are, therefore, treated as dividends and, consequently, submitted to appropriate tax procedures.

Regarding the dividend tax, the Law approving the Fiscal Code provides for tax regulations depending on the beneficiary of the dividends.

According to article 36 of the Fiscal Code, a Romanian legal person which distributes/pays dividends to a foreign legal person must withhold, declare and pay the dividend tax to the State budget. The dividend tax is established by applying a tax quota of 16% to the gross dividend usually distributed/paid to a Romanian legal person.

The dividend tax shall be declared and paid to the State budget until the 25th day of the month following the distribution/payment of the dividends. If the distributed dividends have not been paid until the end of the year in which the annual financial situations were approved, the dividend tax shall be paid till the 25th of January of the following year.

The dividends paid by a Romanian legal person to another Romanian legal person are **exempt from tax** if the beneficiary of the dividends owns, at the time of payment, a minimum of 10% of the equity instruments of the other legal person, for a period of 2 years, fulfilled until the payment date.

Also, the dividends paid by a Romanian legal person to the following persons/institutions are exempt from tax: **a)** optional retirement funds or privately managed retirement funds; **b)** public administrative bodies which exercise, by law, the rights and obligations that derive from their status as State shareholder of those Romanian legal persons.

Regarding the dividends distributed to Romanian natural persons, article 67 of the Fiscal Code provides that income representing dividends is submitted to a tax quota of 16% of its total sum. The obligation to calculate and withhold this type of tax rests upon the legal persons which shall, at the same time, pay the dividends to stockholders or shareholders. The tax payment deadline is until the 25th of the month following the one in which the dividends have been paid.

In case the dividends have been distributed but not paid to the stockholders or shareholders by the end of the year in which the financial situations were approved, the dividend tax shall be paid until the 25th of January of the following year.

In this paper, we consider the beneficiaries of issued shares to be Romanian natural persons. The analytical situation of net and gross amounts is presented in the following table:

Running no.	Shareholder	Number of shares	Gross sum	16% Tax	Net sum
1.	A 1	7.200	21.429	3.429	18.000
2.	A 2	800	2.381	381	2.000
Total		8.000	23.810	3.810	20.000

The next table shows how to mark out these operations regarding the increase of authorized capital in bookkeeping:

Running no.	Explanations	D	=	C	Sum in -lei-
1.	Transfer of privately owned sources to dividends:	%	=	457	23.810
					20.000
					3.810
2.	Dividend tax 16% x 23.810 = 3.810 lei:	457	=	446	3.810
3.	Increase of authorized capital:	457	=	1012	20.000

1012 Subscribed and paid capital; 11711 The carried forward result which represents the undistributed profit; 1041 Share premiums; 457 Payment dividends; 1012 Subscribed and paid capital; 446 Other similar taxes and payments.

The following table presents the situation of privately owned equity:

Running no.	Name	Privately owned equity		Dividend tax
		Initially	After the increase	
1	Subscribed and paid capital	90.000	110.000	
2.	Carried forward result	20.000	-	
3.	Share premiums	5.000	1.190	3.810
Total		115.000	111.190	3.810

Increasing the authorized capital by compensating liquid and exigible receivables of the company with its stocks or shares

Those who own liquid and exigible receivables over the company are its creditors. Towards its creditors the company is in debt.

Among the creditors we include the stockholders/shareholders. Their receivables were created by lending to the companies in which they participate.

According to O.M.F.P. no. 3055/2009, point 205 "The sums which have been deposited or temporarily left at the company's disposal by the stockholders/shareholders, as well as their respective interests, calculated in compliance with the law, are registered into the bookkeeping by distinct accounts".

Also, according to the Instructions of Use of the bookkeeping accounts, the debts regarding the reimbursement of deposited sums by the equity owners are marked out with the help of the 4551 account: stockholders/shareholders – running accounts,

and the interests of these loans are registered into the 4558 account: stockholders/shareholders – interests to running accounts.

In practice, we frequently encounter cases in which the sums received as loans from the stockholders/shareholders are cashed in through the company cashier, using a Cash In Disposition.

According to O.M.F.P. 3512/2008, code 14-4-4, a Cash In Disposition is a document used for the purpose of “cashing in sums that don’t represent income derived from the company’s activity, in compliance with the law”. We can safely conclude that for this type of sums there’s no need to issue a receipt.

The stockholders/shareholders may decide on the increase of authorized capital by compensating liquid and exigible receivables of the company with its stocks/shares if these receivables are due and can be evaluated in monetary units.

It’s obvious from the content of the Methodological Norm no. P/608 of 15th of April 1998, issued by the Romanian Chamber of Commerce and Industry, that, among the mandatory documents necessary for an increase of authorized capital, they require the extrajudicial bookkeeping expertise report also.

The main objective of the bookkeeping expertise report is to “check if stockholders’/shareholders’ receivables over the company really exist”.

Article 67 of the Fiscal Code provides that in the case civil agreement awarded loans, the calculation of the tax owed by income tax payers is performed when paying the interest.

The conversion of the receivables regarding interest in participation titles can be performed only subsequent to the retention of the tax concerning income from interest.

The transfer of the tax related to income from interest is performed on a monthly basis, no later than the 25th of the month subsequent to the payment of the interest.

In order to apply this set of rules, we shall consider that the shareholders lent the company the amount of 80.000 lei.

The money were deposited in the pay box. The loan agreement is concluded for a period of 2 years with annual interest of 10%. After 2 years the increase of the company’s authorized capital is decided to be performed through the conversion of the shareholders’ receivables in shares. The liquid and exigible receivables are of 96.000 lei, of which 16.000 represent interest.

In order to compensate the shareholders’ receivables a number of 9.344 shares are issued with a face value of 10 lei. The accounting records are as follows:

No.	Explanation	D	=	C	Amount -lei-
1.	Based on the collection order the loan received from the shareholders is recorded:	5311	=	4551	80.000
2.	Loan interest:	666	=	4558	16.000
3.	Retention of the interest income $16\% \times 16.000 = 2.560$	4558	=	446	2.560
4.	Capital increase subscription:	456	=	1012	93.440
5.	Receivables compensation with shares	%	=	456	93.440
		4551			80.000
		4558			13.440

1012 Paid capital; 4551. Shareholders – current accounts; 4558. Shareholders – current accounts interes; 456 Reimbursements of shareholders regarding the capital; 5311. Cash in lei.

Conclusions

Dividend tax is owed for the capital elements incorporated in the authorized capital only if the capital increase alters the percentage owned by the shareholders.

When compensating liquid and exigible receivables with shares, no tax is owed for the compensation operation.

The legal provisions concerning the interest income tax is applicable only when the loans awarded to the company based on civil agreements imply interest income.

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