

Comparative Fiscal Analysis of Taxation of Income Obtained by Micro-Enterprises in Romania

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Year 2013 brought major changes in taxation of income obtained by micro-enterprises in Romania, therefore the fiscal analysis aims to clarify fundamental matters as regards the object and subject of taxation, tax base and calculation method, declaration and payment of micro-enterprises income tax. We chose a comparative analysis for three basic reasons, namely: (i) taxation principle change occurred: the option to apply the income taxation system has become a liability for the payment of microenterprises income tax, in compliance with certain conditions; (ii) taxation system has an impact on legal persons in Romania, considering that many of them get annual taxable income below 65,000 EUR; (iii) any corporate income tax / income tax payer must annually review the conditions imposed for micro-enterprises and decide which is the system of taxation for the next fiscal year. In the absence of periodic review, fiscal risks of distorting tax liabilities are significant.

Keywords: *micro-enterprise, taxable income, micro-enterprises income tax, taxation system., corporate income tax, fiscal loss*

A) What is the tax treatment valid until 01.02.2013?

Between 01.01.2004 - 31.12.2009 tax on income obtained by micro-enterprises was regulated by Title IV of the Tax Code.

Between 01.01.2010 -31.12.2010, all taxpayers who have been paying tax on income obtained by micro-enterprises under Title IV of the Tax Code, mandatory became annual income tax payers with quarterly payments.

As of 01.01.2011, income tax was reintroduced by Title IV, index 1 of

the Tax code. All taxpayers that, during the fiscal year 2010 were payers of corporate income tax were able to opt for taxation of income obtained by micro-enterprises even if they were payers of corporate income tax of micro-enterprises regulated by Title IV of the Tax code valid until 31.12.2009.

By 01.02.2013, the main characteristics regulated by Title IV index 1 are the following:

- tax “*was optional*”;

- micro-enterprise was the Romanian legal entity that *cumulatively met the following four conditions*, on December, the 31st of the last fiscal year: (i) *it achieved income* (other than income obtained from activities specified expressly by law in art. 112 index 2 (sixth paragraph) of the Tax Code, such as income from consultancy and management);

- (ii) *it had between 1 and 9 employees*, employed based on an individual employment contract, under the provisions of the Labour Code, regardless of the duration of working time (suspended employment contracts were also taken into account), recorded in the payrolls and general record of employees on a monthly basis;

- (iii) *it achieved taxable income* (total income less non-taxable income referred to in Art. 112 index 7 of the Tax Code, such as provisional income or income derived from stored/tied-up output production) *not exceeding the equivalent in RON of 100.000 EUR* at the NBR exchange rate from the completion of the previous fiscal year;

- (iv) *its share capital* is held by other persons than the state and local authorities (Warning: the Romanian legal entity who has a share capital held by a shareholder or a partner of a legal entity with more than 250 employees cannot be a micro-enterprise);

- Micro-enterprises that were payers of income tax *ceased this taxation system once with the fiscal year* following the one during which they could not meet at least one of the four conditions mentioned above. However, there were *two major exceptions*: (i) if the threshold of 100.000 € would have been exceeded during the year, the micro-enterprise *was obliged* to calculate and pay *corporate income tax starting with the quarter* during which it exceeded the limit of 100.000 €, taking into account income / expenses recorded as from the beginning of the year; (ii) micro-enterprises that, during a quarter, began to carry out business of those referred to in Art. 112 index 2 paragraph (6) of the Tax code tax, owed income tax taking into account income / expenses recorded since that quarter;

• Income tax payers are entitled to recover tax loss recorded over a period of 5 years or 7 years, depending on the year they recorded that loss. Fiscal principle regulated by the Romanian tax law does not allow recovery of tax losses in the period in which the entity was a payer of income tax for the micro-enterprises during the years in which it becomes a corporate income tax payer, leading to the creation of tax disadvantages for entities that are set up and get, for the first years of business, much lower income in relation to expenses incurred.

• Micro-enterprises paying income tax *were entitled to withdraw* from this taxation system and *opt to pay corporate income tax* starting from next fiscal year, by submission of deed of undertaking (form 010) by 31st of January of the following year;

• Provided the micro-enterprise *would have become corporate income tax payer*, either due to the non-compliance with the cumulative conditions imposed by law, or as a result of its own waiver options, *it was not be able to return to taxation* of microenterprises income (as it was considered that the option right was unique and was lost at the same time with the tax capacity of micro- enterprise).

For example, the company BBB SRL, business scope “Other telecommunication activities” (NACE code 6190), since 01.01.2010 it has opted for taxation of its income as a micro-enterprise (share capital is owned by the sole shareholder- a natural person, number of employees: 5, remained constant during the analyzed period).

During the year 2012 it achieved total income amounting to 500.000 lei, of which 350.000 lei turnover, income for cost of services in progress 95.000 lei (credit balance) income resulted from adjustment to depreciation of accounts receivable 40.000 lei (recognized following a partial collection of a doubtful debt recorded as expenses in the fiscal year 2011); income from compensation, from insurance companies for damage caused on one of its own means of transport- 12.000 lei, interest income 3.000 lei. Evolution of NBR rate valid at the end of the fiscal year: 4.3197 lei / euro (2011), as well as 4.4287 lei (2012).

For the year 2012, micro-enterprise had a maximum limit of taxable income of 431.970 lei (100.000 € * 4.3197 lei / euro - NBR exchange rate valid at the end of fiscal year 2011).

It was noted that taxable income were 353.000 lei (350.000 lei – 3.000 lei), while non-taxable income was in the amount of 147.000 lei (95.000 lei

+ 40.000 lei + 12.000 lei). In this case, the company recorded, in the I-IVth quarters (by Form 100) a total income tax of the micro-enterprises in the amount of 10.590 lei ($3\% * 353.000$ lei).

In terms of exceeding the legal limit, it is found that the value in euro of taxable income is 81,718.64 EUR (353.000 lei / 4.3197 lei per euro). Therefore, the management decided to keep the taxation system also for the year 2013.

For the year 2013, micro-enterprise established a maximum limit of taxable income of 442.870 lei ($100.000 \text{ €} * 4.4287$ lei / euro - NBR exchange rate valid at the end of fiscal year 2012). Further, we will present the legal provisions valid from 01.02.2013 and will comment on the actual fiscal situation of the micro-enterprise analyzed by us.

B) What is the tax treatment valid since 01.02.2013?

From 01.02.2013, substantive changes occur in income taxation of micro-enterprises, this taxation system becoming mandatory for most entities, within the limits of and under the law. Below, we intend to present the main issues in force since 01.02.2013, in terms of entities that have previously applied this taxation system, of those who were corporate income tax payers, but also of those who are established in the current year.

b1) What is a micro-enterprise?

The main change aims to the rescission of condition on the number of employees and change of condition related to the size of taxable income from 100.000 EUR to 65.000 EUR. Thus, the micro-enterprise is a Romanian legal entity which cumulatively meets the following conditions, on December, the 31st of the last fiscal year (Article 112 index 1 of the Tax Code 1):

1)	obtains income, other than those derived from activities: in the banking field; in insurance and reinsurance fields, capital market, except legal persons performing intermediation activities; in these fields of gambling, consultancy and management;
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Obs.: Classification of income derived from consulting and management services is done as before, by analyzing contracts signed, as well as other documents justifying the income nature. However, we deem as being very useful the express indication through the Methodological Norms and NACE codes related to the field of consulting and management.

2)	<p>achieved income that <i>did not exceed the equivalent in RON of 65.000 EURO</i>;</p> <p>Observation: In our opinion, this value limit is valid beginning with fiscal year 2013, as the Romanian legal entities that have opted for taxation system on the income of micro-enterprises, according to the legal regulations in force until February the 1st, 2013 (when the limit was 100.000 EUR) preserves this tax regime also for 2013, according to art. 112 index 2 paragraph (7) of the Tax Code. Returning to our example, micro-enterprise BBB SRL remains an income tax payer (even if its taxable income in 2012 exceeds those 65.000 euro), except that <i>for the year 2013, the maximum taxable income</i> is not 442.870 lei (100.000 € * 4, 4287 lei / euro, at the NBR exchange rate of 31.12.2012) but is 287,865.50 lei (65.000 EURO * 4.4287 lei / EURO).</p>
3)	its share capital is held by persons, others than the state and local authorities.

b2) in which cases must be declared and paid the income tax for the micro-enterprises?

If the above conditions are cumulatively met (referred to in Art. 112 index 1), income tax for the micro-enterprises is mandatory, as follows:

(1)	<p>An already established Romanian legal entity that is an income tax payer is liable to pay tax on income obtained by the micro-enterprise starting from the next fiscal year, if it meets the conditions stipulated in art. 112 index 1, by submitting Form 010 "Tax Registration Statement/ Statement of amendments for legal entities, partnerships and other entities without legal personality" until January, the 31st of the following year to the one during which the conditions were met (i.e. January, the 31st of the year for which income tax is paid for micro-enterprises).</p> <p style="text-align: center;">ATTENTION:</p> <p>For the year 2013, the Romanian legal persons paying corporate income tax, which, on December the 31st, 2012 meet the conditions stipulated in Art. 112 index 1 of the Tax Code, are required to pay income tax on micro-enterprises since February the 1st, 2013 and are to notify the competent tax authorities on the amendment of taxatibo system by submitting <i>Form 010, until March, the 25th 2013, inclusively.</i></p> <p>Also up to March the 25th, 2013 inclusively, the taxpayer shall also submit the declaration of income tax due for the taxable profit earned in the period January the 1st, 2013 to January the 31st, 2013, by derogation from the provisions of art. 34 and 35.</p>
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EXAMPLES:	
	<p>(E.1.) Suppose that a company paying income tax in year 2012 is in the same situation described by us for micro-enterprise BBB SRL (fully privately owned capital, scope of business- „other telecommunications activities”, taxable income in terms of income tax in the amount of 353.000 lei). In such case, this company is required that, in 2013, it shall also calculate, declare and pay corporate income tax, as it exceeded the maximum limit of 65.000 EURO for the year 2012 (79,707.36 EUR at the NBR exchange rate valid for the year 2012), regardless of the number of employees.</p> <p>(E.2.) The same corporate income tax payer as in the previous example, earned in 2012 taxable income totaling 221.435 lei (50.000 € * 4.4287 lei / EUR), with a total of 15 employees. This means it will due income tax on microenterprises as from 01.02.2013;</p> <p>(E.3.) If a corporate income tax payer (fully privately ownership) earned, in 2012, income from trade activities worth 75.000 EUR, with a total of 10 employees, it shall still owe corporate income tax in 2013, as it exceeded the value limit of 65.000 EUR ;</p> <p>(E.4) If a corporate income tax payer (fully privately ownership) earned, in 2012, income from consulting services worth 50.000 EUR, it shall still owe corporate tax income in 2013, due to the fact that it does not cumulatively meet the conditions of Article 112 index 1, i.e. it does not meet the condition stipulated at letter a), that means it earned income within the limit of 65.000 EUR, but they are derived from consulting services.</p>
(2)	<p>A Romanian legal entity who is newly established, is required to pay income tax on micro-enterprises as from the first fiscal year, if the condition stipulated in art. 112 index 1 letter d) (its capital is held by persons other than the state and local authorities) is fulfilled at the registration with the Trade Register. In this case, legal entities that are established during the fiscal year enroll the mention in the application for registration with the Trade Register.</p> <p>In our opinion, the legislature should clarify by the Rules, if and under what conditions, the newly established taxpayers who have, in their scope of business, the services provided in art. 112 index 6 (i.e. consultancy and management) are required to pay tax on income for the micro-enterprises.</p>

According to art. 26 paragraph (4) of the Tax Code, Romanian legal entities who have been paying corporate income tax and, in this period, they recorded tax loss and subsequently they are required to become payers of tax on income of the micro-enterprises, will recover the tax loss recorded in Form 101 for the period it was a corporate income tax payer according to Art.

26 paragraph (1) and Art. 26 paragraph (5) from the date they shall return to the system of corporate income tax payers. This loss is recovered for the period between the date of registration for the tax loss and the limit of those 5 years and 7 years, as the case may be.

b3) What are the legal persons who are NOT required to declare and pay tax on income of the micro-enterprises?

According to art. 112 index 2 paragraph (6) of the Tax Code, there is no obligation to apply the income tax system on the micro-enterprises for the Romanian legal entities which:

- a) carry out activities in the banking field;
- b) carry out activities in the field of insurance and reinsurance, capital market, except legal persons performing intermediation activities in these fields;
- c) carry out activities in the field of gambling, consultancy and management.

In our opinion, the new regulations should be clarified by methodological norms in the meaning of specifying expressly whether paragraph (6) also refers to the possibility to choose this taxation system, for the Romanian legal persons who obtain income from activities referred to in paragraph (6) (e.g. consultancy) and satisfy the other two conditions on the limit of 65,000 EUR and ownership structure.

b4) under what circumstances, is the tax on income for the micro-enterprises not necessary to be declared and paid?

It is maintained the rule according to which the micro-enterprises do not apply this taxation system since fiscal year following the year during which they no longer meet one of the conditions stipulated in art. 112 index 1 of the Tax code, as they are required to notify the exit from the income tax system by January, the 31st of the following year.

However, micro-enterprises notify to the competent tax authorities their exit from the micro-enterprise income taxation system, during that year, within 30 days from the occurrence of the event - by submitting Form 010 - in the following two situations:

(1)	<p>Micro-enterprises that, during a quarter, start carrying out activities of the kind referred to in Art. 112 index 2 paragraph (6) of the Tax Code (in the fields such as banking, insurance and reinsurance, capital market, gambling, consultancy and management), <i>owe corporate income tax taking into account those income and expenses recorded as from such quarter</i> (See section 7 of the Methodological rules for the application of Art. 112 index 2 of the Tax Code).</p>
(2)	<p>If during a fiscal year, a micro-enterprise obtains income exceeding the limit of 65.000 EUR, it will pay corporate income tax taking into account the income and expenses incurred from the beginning of the fiscal year. Calculation and payment of the corporate income tax is made as from the quarter during which the limit of 65.000 EUR was exceeded. Corporate income tax payable represents the difference between the corporate income tax calculated from the beginning of the fiscal year by the end of the reporting period and the tax of income for the micro-enterprises due for such current year.</p> <p style="text-align: center;">ATTENTION:</p> <p>For the corporate income tax of 2013, income and expenses incurred from the beginning of the fiscal year (01.01.2013), as well as from 01.02.2013 are taken into account.</p> <p>For example:</p> <p>(E.1) If a taxpayer (with fully privately shareholding) was a corporate income tax payer for the micro-enterprises in 2012 and in the same year, it achieved taxable income amounting to 90.000 EUR, it will remain corporate income tax payer in 2013. If, in the third quarter of 2013 (July-September 2013) it exceeds 65.000 EUR (at the exchange rate of 4.4287 lei / eur), then it becomes a corporate income tax payer, taking into account all income and expenses incurred since 01.01.2013. Attention: In this case, the corporate income tax due is the difference between corporate income tax calculated from the beginning of the fiscal year by the end of the third quarter and the corporate income tax for the micro-enterprises payable during that year (first and second quarters).</p> <p>(E.2) If a corporate income tax payer (with fully privately shareholding) achieved in 2012 income from agriculture amounting to 50.000 €, with a total of 15 employees, it will owe income tax as from 01.02.2013. If during February to December 2013, it exceeds the limit of 65.000 EUR, then it will become again a corporate income tax payer, taking into account all income and expenses incurred since 01.02.2013. The reason? For the period 01.01.2013 - 31.01.2013, it was required to submit the Form 101 in accordance with art. 112 index 2 paragraph (3) of the Tax code.</p>

News: By repealing provisions relating to failure to return to income taxation, within the limits of and under the law, an income tax payer *may become* a corporate income tax payer and subsequently *be able to become again* an income tax payer and once again to become a corporate income tax

payer, depending, of course, on the fulfillment or non-fulfillment of cumulative conditions laid down in the new art. 112 index 1 of the Tax Code.

b5) Which is the basis for calculating income tax for the micro-enterprises?

According to art. 112 index 7 of the Tax Code (unamended), income tax of the micro-enterprises is levied on income derived from any sources, minus: a). income related to the costs of product stocks; b). income related to the cost of services in progress; c). Own work capitalized; d). grants related to income; e). provisional income and adjustments for depreciation or loss of value; f). income obtained from the repayment or cancellation of interest and / or late fees, which were non-deductible expenses at the calculation of the taxable profit; g). income from compensation from insurance / reinsurance companies, for damage caused to property such as stocks or own tangible assets.

Micro-enterprises are required to keep track of tax depreciation under art. 24 of Title II "Income Taxes" of the Tax code. Moreover, if a micro-enterprise purchases an electronic cash register, their purchase value is deducted from the tax base, in accordance with the supporting document, in the quarter when they were put into operation, under the law.

b6) which is the tax rate on the income of micro-enterprises? Tax rate is still 3%.

b7) which is the term of payment of income tax for microenterprises? Tax payment is made quarterly, until the 25th of the month following the quarter for which the tax is calculated.

b8) What is the deadline for submission of micro-enterprise income tax statement? Micro-enterprises **quarterly submit** Form 100, until the 25th of the month following the quarter for which the tax is calculated.

For example, returning to the analyzed company - BBB SRL – with the scope of business „Other telecommunication activities” (NACE code 6190), let us remind that, in the year 2012, it paid tax on income for micro-enterprises. NBR exchange rate valid for the end of the previous year was 4.4287 lei, meaning that, for the year 2013, micro-enterprise had a maximum limit of taxable income worthing 287,865.50 lei (65.000 EUR * 4.4287 lei / EUR). Suppose that, in year 2013, it has achieved:

Version 1: Total income in the amount of 300.000 lei, of which: turnover- 245.000 lei, income resulted from adjustment to depreciation of accounts receivable- 50.000 lei, interest income- 5.000 lei. In this case, taxable income was 250.000 lei and were included in the legal maximum limit, i.e. the company recorded, in the 1st-1vth quarters (by Form 100) a total income tax of micro-enterprises in the amount of 7.500 lei micro ($3\% * 250.000$ lei). For the year 2014, it is bound to continue applying income tax, as it meets all legal requirements and it should take into account the maximum amount of 65.000 EUR at the NBR exchange rate valid for 31.12.2013;

Version 2: Total income in the amount of 400.000 lei, of which: turnover- 420.000 lei, income related to cost for services in progress- 25.000 lei (balance due), interest income- 5.000 lei. In this case, taxable income was 425.000 lei and exceeded the legal maximum limit.

Entity recorded, for the quarters I-III (Form 100) a total income tax of micro-enterprises in the amount of 6.000 lei ($3\% * 200.000$ lei-taxable income for the first three quarters);

Since exceeding the maximum limit occurred at 10.10.2013, entity shall submit the statement of amendments by 10.11.2013 010 by which it modifies its tax vector, becoming tax income payer as from the fourth quarter of 2013. However, it shall pay income tax taking into account the income and expenses incurred from the beginning of the fiscal year (01.01-31.12.2013). Considering all income as being taxable and considering that the size of tax deductible expenses is 300.000 lei, it follows that the annual income tax is 16.000 lei ($16\% * 100.000$ lei tax profit).

By 25.03.2014, the analyzed entity must submit Form 101 "Statement on corporate income tax" and pay the difference of 10.000 lei (16.000 representing corporate income tax minus 6.000 lei representing tax on income for micro-enterprises).

Conclusions

Comparative analysis allowed us to find out that there were substantial changes regarding taxation method, by passing from the option-based principle to principle based on obligation of microenterprises to pay income tax, in compliance with certain conditions.

We also noticed that the maximum limit of taxable income was reduced from 100.000 EUR to 65.000 EUR, at the NBR exchange rate valid for the end of the previous financial year. In addition, the number of cumulative

conditions was reduced from four to three, by the exclusion of condition related to the number of employees.

If for the micro-enterprises existing on 31.12.2012, the new maximum amount limit applies with income obtained since 01.01.2013, for the corporate income tax payers existing on 31.12.2012, the new amount limit of 65.000 EUR is levied on income earned in the year 2012, in the sense that they may become income tax payers since 01.02.2013 if they meet the new conditions regulated by the tax law for micro-enterprises.

I emphasized that any income tax / corporate income tax payer must annually review the conditions imposed for micro-enterprises and decide which is the taxation system for the next fiscal year. The reason is generated by the change of taxation principle:

(i) for example, by 31.01.2013, inclusively, micro-enterprises were entitled to waive income tax (as it was optional) and become corporate income tax payer, but they could not return from the corporate income tax payer to micro-enterprise income tax payer;

(ii) after 01.02.2013, to the extent they meet the three cumulative conditions, micro-enterprises are required to continue applying the income tax system (as taxation is compulsory). Similarly, corporate income tax payers are required to change the taxation system.

To the extent they do not meet one of the cumulative conditions, micro-enterprises are obliged to apply the profit tax system starting from the next year or even during the current fiscal year (for the exceeding of the maximum limit of 65.000 EUR or in case of obtaining income from activities such as consulting and management services).

Moreover, it is mandatory to return to the taxation of income whenever the Romanian legal person meets the three cumulative conditions.

References

www.infisc.ro (materials have been selected from Infisc portal on the calculation, declaration, payment of income tax. Also, several examples have been used both in section „Tax cases”, as well as in the section entitled „Accounting monographs”.

Law no. 571/2003 on the Tax Code, as amended and supplemented; Government Decision no. 44 of January the 22nd, 2004 approving the Methodological Norms for applying Law no. 571/2003 regarding the Tax Code, as amended and supplemented.