ACCOUNTING TREATMENT FOR MICRO-ENTITIES LEVEL SINCE 2014

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Abstract

In this paper is presented, based on amendments to the Tax Code of the Government Emergency Ordinance no. 102/2013, the accounting treatment that is applied by micro-entities from Romania, especially to the revenues from foreign exchange. That is because it is influenced by the new changes applied from January 1st 2014. More specifically, these changes have excluded from taxable income base of micro foreign exchange income and financial income as a result of the settlement of claims and liabilities in lei, according to a currency different from that to which was originally recorded, on the one hand, opposing the inclusion in the taxable only in the fourth quarter of the difference between income from favorable foreign exchange and foreign exchange expenditure, ie the difference between financial income recorded due to the settlement of claims and liabilities in lei, according to a currency different from that to which they were originally recorded, and financial expenses related, cumulative registered early.

Keywords: micro-entities, accounting treatment, revenue from exchange differences, expenses and profit

JEL Classification: M40, M41

1. Introduction

The fiscality of micro-entities was initially regulated by Government Ordinance no. 24/2001, with the subsequent amendments and supplements.

According to the original text [1], the companies ranked in the category of micro-entities were required to pay an income tax rate of 1.5% in the total income from any source, calculated and paid quarterly, beginning with September 1, 2001.

Subsequently, the Minister of Finance no. 1880/2001 recognized the non taxable income based on “fictitious” as well as the realization provisions or from unfinished production, or from production of property for their own use.

The initial regulation for the Romanian micro-entities [1] provided cumulative criteria for classifying companies in the category of micro, namely:

• to produce goods, to sell their products or services (except banking, insurance, reinsurance, capital markets and foreign trade);
• to have private capital;
• to have maximum nine employees, including;
• to achieve by the end of the year a total income up to € 100,000, inclusive;
• the partners or shareholders that own more than 25% of the share capital must not have more than 250 employees [2] (that condition was stipulated in the Law no. 133/1999 on SME’s).

From the beginning there was a question of whether companies with no employee had to be classified in the category of micro-entities. During times, new regulations tried to answer to that question. From April 9th 2003 the criterion about the number of employees changed from “up to nine” to “one to nine, including” [3]. This condition was considered accomplished if the entity engaged minimum one employee until the end of the year 2003 [4].

All the criteria were established at the end of the every year. If any of the criteria was broken during one year then the entity was not able to be ranked as micro-entity any more.

From an accounting perspective, in 2001 and 2002, micro-entities have implemented a specific chart of accounts, very simplified [5]. Since 2003, the micro-entities applied the chart of accounts to simplified accounting regulations harmonized with EU directives [6], similar to all the other companies that are not required application of international accounting standards.

2. Current fiscal treatment

The initial law [1] also provided tax incentives for micro-entities, namely:

• deduction from the taxable base of the consideration fiscal electronic cash registers, acquired according to law;
• deduction of the tax value of depreciable assets for investments made in authorized activities;
• 20% tax reduction when increasing the number of employees to ensure at least 10%.
The last two incentives were applied only during September-December 2001 and January-June 2002 [7]. Currently, under “Title IV enterprises’ income tax” [8] and the latest amendments [10] for micro-entities, the legislation defines micro-entity as Romanian entity which satisfies the following conditions at 31 December of the previous fiscal year:

- income (including brokers and insurance agents), except banking, insurance, reinsurance, capital markets and gambling;
- revenues from consulting and management are to a maximum of 20% of total revenue; classification is performed by analyzing contracts and other documents justifying the revenues;
- earned income that does not exceed the equivalent in lei of 65,000 euros using the exchange rate at year-end NBR;
- share capital is held by persons other than the state and local authorities;
- dissolution is not in liquidation, registered in the trade register or to the courts, according to the law.

A Romanian legal person which is newly created is obliged to pay tax on micro-entities revenues from the first year, if the condition for social capital is accomplished at the date of registration in the commercial register and not active in the areas exempted.

Micro-entities are no longer applying this system of taxation since the next fiscal year that no longer meet one of the conditions listed above.

If during a quarter a micro-entity start to carry out exempt (e.g. gambling), then that entity begin to owe the profit tax considering the incomes and expenses incurred from that quarter.

3. Revenue from exchange differences at micro-entities level

Enterprises’ income tax applies to income from any source quarterly, at the rate of 3%, except for:

a) income for the cost of inventories of products;
b) income for the cost of services in progress;
c) income from the production of tangible and intangible assets;
d) income from grants;
e) income from provisions and adjustments for depreciation or impairment;
f) revenue from the repayment or cancellation of interest and / or penalties for late payment, which were deductible in computing taxable profit;
g) income from compensation from insurance / reinsurance for property damage such as stocks or own tangible assets;

h) income from foreign exchange differences;
i) financial income recorded as a result of the settlement of claims and liabilities in lei according to an exchange rate different from that to which they were originally recorded;

j) the value of trade discounts granted after invoicing;

plus the following categories of income:

a) the trade discounts received after invoicing;
b) in the fourth quarter, the favorable difference between income from the foreign exchange / financial income recorded as a result of the settlement of receivables and payables denominated in domestic currency a function different from that to which they were originally recorded and expenses of foreign exchange differences / financial costs related cumulative registered early [9, 10].

So, beginning with January 1st 2014, an micro entity can have favorable (revenues) and unfavorable (losses) differences from foreign exchange, but the income tax will be influenced only at the final quarter of the year with the cumulative favorable difference between income from the foreign exchange.

For example, we consider this particular situation:

- 1st quarter of the year: 10000 lei revenue from differences from the foreign exchange;
- 2nd quarter of the year: 5000 lei losses from differences from the foreign exchange;
- 3rd quarter of the year: 3000 lei losses from differences from the foreign exchange;
- 4th quarter of the year: 2000 lei revenue from differences from the foreign exchange.

For the 1st till 3rd quarter of the year the income tax for micro entities will be uninfluenced from the differences from the foreign exchange. The tax calculation for the 4th quarter will be influenced with the favorable difference between income from the foreign exchange, respectively the tax base will be increased by 4000 lei (10000-5000-3000+2000). Thus the tax income will be higher by 4000 lei * 3% (120 lei).

Until 2014, the differences from the foreign exchange will have influenced only the tax income for the 1st quarter (10000 lei * 3%) and the 4th quarter (2000 lei * 3%). Thus, the total tax income for micro entities, for our example, would have been three times higher for the differences from the foreign exchange (12000 lei rather than 4000 lei).

Moreover, if we will consider (for the same example) for the 4th quarter 2000 lei (or more) losses from differences from the foreign exchange instead of 2000 lei revenue from differences from the foreign exchange, then the income tax for micro-entities influenced by the differences from the foreign exchange is zero (instead of 4000 lei * 3%, the micro-entity have no income tax from the differences from the foreign exchange).
Even though the net amount of the tax income beginning with 2014 will not be influenced by far, but in proportion, the tax income from the differences from the foreign exchange is very much influenced. The influence is higher if the foreign exchange is more fluctuating.

4. Accounting treatment for revenue from exchange differences at micro-entities level

The fiscal year of a micro-entity is the calendar year. If a micro which is established or ceases to exist, the fiscal year is the calendar year during which there was a legal entity.

If during a fiscal year a micro-entity income exceeding EUR 65,000 or share revenues from consulting and management in total income is over 20%, this entity will pay profit tax. Calculation and payment of profit tax is performed starting with the quarter that exceeded any of the limits laid down in this Article, taking into account the revenues and expenditures at the beginning of the fiscal year. The tax due is the difference between income tax calculated at the beginning of the fiscal year to the end of the reporting period and enterprises' revenues tax (as micro-entity) due in the year. The exchange rate for determining the equivalent in euros is the previous financial year-end.

Micro-entities which cease to exist after a reorganization or liquidation operations and during the operation have been paying profit tax, on entities' revenues tax calculation does not include the tax base on: the reserves of net profit reserves and from favorable exchange rate differences related to the available capital in the currency or currencies, and the corresponding amounts of reductions in the tax rate on profits distributed as own sources of funding, which were established during the entities which were taxable on profit.

In Romania, the accounting treatment for revenue from exchange differences at micro-entities level is based by this accounting article:

\[
\begin{array}{c}
698 \\
\text{"Expenses with income tax and other taxes that do not appear in the above items"} \\
\end{array}
\begin{array}{c}
* \\
4418 \\
\text{"Income tax"} \\
\end{array}
\]

5. Conclusions

The micro-entities are suffering many amendments since when they were defined in 2001. Also, the tax on revenues had changes during this period (2001-2014). For example, the tax is double than at the beginning (from 1.5% to 3%), the incentives are fewer, the calculation basis is different, the cumulative criteria for classifying companies in the category of micro are different (for example, from 100,000 euros the limit is now 65,000 euros).

Given the fact that many micro-entities recorded losses and still record losses in present, the state took a position against tax evasion in these companies by eliminating the criterion of number of employees and through setting the ceiling of 65,000 euros. In this way, even if these entities classified as micro-entities under the law, not accounting profit or tax records, however, they are obliged to pay to the state a share of 3% to total turnover.

Beginning with 2014, the income tax for micro-entities is influenced only the yearly favorable difference between income from the foreign exchange / financial income recorded as a result of the settlement of receivables and payables denominated in domestic currency a function different from that to which they were originally recorded and expenses of foreign exchange differences / financial costs related cumulative registered early.

Even though the net amount of the tax income will not be influenced by far (the micro-entities has total yearly revenues below 65000 euros), but in proportion, the tax income from the differences from the foreign exchange is very much influenced. So, this way of tax calculating is more accurate and more realistic for micro-entities. The influence is higher if the foreign exchange is more fluctuating.

6. References

[4] Law no. 232 of 31.05.2003, published in Official Gazette no. 373 of 31.05.2003, entry into force 31/05/2003 to approve Government Ordinance no. 36/2003 regarding the correlation of financial and tax provisions
regulations compliant with European directives, repealed and replaced in turn by OMPF 3055/2009 approving the Accounting Regulations compliant with European directives


