STUDY ON THE APPLICATION OF CASH ACCOUNTING SYSTEM FOR VAT IN ROMANIA

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Abstract
The cash accounting system for VAT has been implemented in Romania as of 1 January 2013 and now turns one year of application in Romania. Since its implementation the system has sparked controversy, being harshly criticised by professional accountants in Romania and elsewhere. Criticisms mainly concerned the following issues: no possibility to choose to apply the system, breach of the VAT neutrality principles, maximum period of 90 days to postpone the chargeability of VAT for unpaid deliveries, while VAT deduction was subject to payment of the value of goods and services invoiced without specifying any term. In this article we would like to examine the extent to which the legislative changes that came into effect as of 1 January 2014 improve the cash accounting system for VAT in Romania. We will also analyse to what extent the system applied in 2013 has brought advantages/disadvantages to the economic entities in Romania based on a survey carried out on a heterogeneous sample of companies in the county of Gorj, regarded as nationally representative. Finally, we intend to compare the cash accounting system for VAT in Romania with its UK counterpart.

***Keywords*:** chargeability, VAT, cash accounting system for VAT, VAT deduction, VAT collection, VAT under settlement

JEL Classification: *M40, M41, H32, E62*

1. Introduction

Implemented in 2013 [12], the cash accounting system for VAT has brought the following new aspects [5, 6] for the economic entities registered for VAT purposes with businesses established in Romania [3, 4, 12] compared to the standard VAT system [1, 2]:

- continuous tracking of turnover since its level generated the mandatory application of the cash accounting system for VAT and was based on the criterion of RON 2,250,000 ceiling (about EUR 664,800 at the rate on the date of accession to the EU, i.e. EUR 508,050 at the rate set by the National Bank of Romania for the end of 2012, i.e. EUR 501,706 at the end of 2013) and getting out of the system for overrunning the ceiling, beginning with the second tax period;
- "cash accounting for VAT" indication on invoices (for those applying the cash accounting system for VAT);
- while the standard VAT system assumed that VAT chargeability should coincide with the taxable event (i.e. issue of invoice), the cash accounting system for VAT deferred by up to 90 calendar days the collection of VAT for unpaid invoices, on the one hand, and deferred the VAT deduction until payment of the invoices to suppliers;
- the automatic registration of taxpayers for whom the application of the cash accounting system for VAT was binding by not exceeding the ceiling mentioned above in the "Register of people applying the cash accounting system for VAT". This register, that can be accessed online, also had to be used by taxpayers for whom the application of the cash accounting system for VAT was not binding (also called standard VAT system, the ceiling being exceeded) [1, 2, 5] as a tool for tracking the deductibility of VAT on invoices issued by taxpayers applying the cash accounting system for VAT (they could only deduct VAT when paying the suppliers) [3, 4];
- taxpayers not applying the cash accounting system for VAT are required to check if their suppliers apply the said system because in this case the VAT deduction is made only when paying the suppliers (again, they do not apply the cash accounting system for VAT). The immediate deduction of VAT on purchases is possible only where both business partners (supplier and customer) do not apply the cash accounting system for VAT;

- amendment of the Form 300 (type 301 “Monthly VAT return” and 302 “Quarterly VAT return”) for all taxpayers (VAT deferred on collection/deduction was recorded in a separate return as undue VAT for both deliveries and acquisitions);
- in terms of administration and accounting, the application of the cash accounting system for VAT generated an extra effort for the professional accountants responsible for bookkeeping [5, 6, 7]. The drawbacks were major as they were generated by higher administrative costs (VAT deduction was subject to payment of debts to suppliers and the chargeability of output VAT depended on customers' collection including on the transactions treated as collection [5]. However, they had to manage new forms of VAT journals and VAT returns). Finally, the professional accountants had to check for each invoice recorded if the supplier/customer was registered in the “Register of people applying the cash accounting system for VAT” in order to correctly interpret the right to deduct.
- Similarly, the inspection bodies felt a strain of the control and NAFA [National Agency for Fiscal Administration] had to manage the Form 097 and the “Register of people applying the cash accounting system for VAT” (entries and deletions).

As expected, the State was the main winner as that implementation of the cash accounting system for VAT in Romania in 2013 has mainly served its interest and the European legislation provisions were also violated [5, 9]. In addition, most taxpayers for whom the application of the cash accounting system for VAT was binding in 2013 have experienced cash flow problems and bottlenecks, the most disadvantaged are the SMEs (taxpayers not applying the cash accounting system for VAT shifted to suppliers that also did not apply the cash accounting system for VAT, in order to ensure immediate deductibility of VAT on acquisitions; the effect was devastating and small taxpayers were driven off the market) [10]. Although the cash accounting system for VAT, in semantic terms, would have meant a release of liquidity in the market, basically the only good thing it has brought was a delay of up to 90 calendar days, given that crediting was difficult through the banking system. This advantage was little felt in practice because many taxpayers who were facing financial blockage had ongoing agreements with public institutions for which the collections had delays exceeding six months, or even 12 months quite often.

In conclusion, as expected for any European country (even if sometimes we seem to behave differently from other European countries) the cash accounting system for VAT in Romania has been improved as of 1 January 2014. These issues will be examined next.

2. The cash accounting system for VAT as of 1 January 2014 in Romania

Fortunately, the cash accounting system for VAT has been improved from 1 January 2014, and the Minister for SMEs and Tourism himself has publicly argued that the mandatory application of the cash accounting system for VAT “created distortions in the market and disadvantaged small and medium enterprises” [9, 10].

The new cash accounting system for VAT applicable in Romania after 1 January 2014 is optional and not mandatory, allowing taxpayers with annual turnover below the same ceiling (about EUR 500,000) to choose whether to apply the system or not [11].

In terms of declarative obligations, by failing to file any notice, the taxpayers will continue to be kept by NAFA in 2014 as well in the “Register of people applying the cash accounting system for VAT” (they will continue to apply the system) and the return to the standard VAT system necessarily requires the submission of a notice, i.e. the Form 097 (they will be removed from the Register as of 1st January of the next tax period).

The new cash accounting system for VAT brings another major improvement, namely the elimination of the 90 day-period. Consequently, starting with the invoices issued from 1 January 2014, the collection of VAT is deferred until receipt of the claim, at which point we can say that this system no longer distorts the principle of VAT neutrality, that is both collection and deduction of VAT shall be deferred until invoice receipt/payment (such a criticised issue for the system applied in 2013).

Next we shall make a few remarks on the implications of the changes occurring after 1 January 2014:

- getting out of the cash accounting system for VAT is optional for taxpayers who applied the said system in 2013 and who in 2013 had a turnover below the ceiling (about EUR 500,000), and it is performed by notification of NAFA at any time during 2014 (the effective removal of the Register is done as of the 1st of the next tax period);
- for those leaving the cash accounting system for VAT, the chargeability of VAT occurs on the date of full or partial receipt of the value of goods delivered/services provided on the basis of invoices issued before 31 December 2013 (the taxable event occurs before 31/12/2013). In other words, for the operations where cash accounting was applied, the same treatment will apply after leaving the cash accounting system for VAT;
- The taxpayers newly established in 2014 may choose to apply the cash accounting system for VAT (the same notice 097) and are required to apply this system until the end of 2014 (considered to be

the first year). Of course, if the ceiling set (EUR 500,000, i.e. RON 2,250,000) is exceeded during 2014, the normal taxation system will be used starting with the 1st of the second tax period).

3. Study on the application of the cash accounting system for VAT based on a survey conducted in 2013

In order to highlight how the cash accounting system for VAT brought advantages/disadvantages in 2013, we conducted a survey among 30 heterogeneous companies (small, medium and large) based in the county of Gorj, randomly selected and regarded as nationally representative.

Following the activity of the 30 companies and the discussions with their representatives have revealed the following:

- the companies with activity in immaterial field (service provisions) that applied the cash accounting system for VAT and did not usually have unpaid debts (their main suppliers are included in the scope of utilities: energy, water, gas etc.) were not advantaged or disadvantaged, as the deduction of VAT has not changed substantially from the standard VAT system (applied in 2012). However, as long as the service provisions were intended for natural persons (small businesses), VAT collection was not different from the standard system as the services were paid upon invoicing or within 7 days. Where these companies, usually design, architecture and software companies, included public institutions in the customers' portfolio, they felt an advantage in applying the cash accounting system for VAT as they were able to postpone VAT chargeability by 90 calendar days. For example, given that February 2013 had 28 days, the limit of 90 calendar days for invoices issued on 01/01/2013 was 01/05/2013, and VAT to the State was to be made by 25/07/2013 for those with quarterly returns (instead of 25/04/2013), i.e. by 25/06/2013 for those with monthly returns (instead of 25/02/2013);
- the trade companies were seriously disadvantaged, particularly those selling to natural persons, as they were forced to postpone the deduction of VAT on invoices unpaid until their payment and VAT was collected at the time of sale (the value of deliveries was immediately collected from natural persons). All these companies have experienced serious cash flow problems and bottlenecks, ending in more than 70% of cases to reschedule the tax liabilities arising from increased, sometimes doubled VAT (based on debt repayment schedule file filed with NAFA);
- the production companies were also affected as they usually work on trade credit (supplier credit), a phenomenon similar to those in the trade;
- the most disadvantaged were the small companies that starting with 1 February 2013 had to replace income tax with tax on micro-enterprise income due to a turnover for 2012 between RON 220,000 (i.e. EUR 65,000 at the rate on the date of accession to the EU) and RON 287,865 (representing EUR 65,000 at the rate set by the National Bank of Romania on 31/12/2012) and that also continued to pay VAT (due to the annual turnover of over RON 220,000), while applying the cash accounting system for VAT;

4. The UK cash accounting system for VAT

Since 2014 the cash accounting system for VAT applicable in Romania is much improved over the original version applied in 2013. For comparison, we shall outline next some aspects of the same system that applies in the UK [8]:

- VAT chargeability is given by the date of invoice receipt/payment (as in Romania);
- the cash accounting system for VAT is optional in the UK (as in Romania)
- the ceiling used in order to be able to use the cash accounting system for VAT is 1,350,000 pounds in UK, representing approximately RON 7,250,000 at the rate set by the National Bank of Romania on 31/12/2013 for GBP (compared to RON 2,250,000 in Romania). Note that this ceiling is anticipated for the next fiscal year (in Romania the ceiling refers to the turnover of the previous calendar year);
- the cash accounting system for VAT can be used (only in the first year of application) until a turnover of GBP 1,600,000 is achieved (approximately RON 8,600,000 at the rate set by the National Bank of Romania on 31/12/2013) by UK taxpayers (there is nothing similar for Romania);
- the UK taxpayers may opt for the cash accounting system for VAT if: they have outstanding debts of VAT, have been convicted for offences within the scope of VAT or have been penalised for tax evasion over the last year and when the turnover of the previous year exceeds GBP 1,350,000 (in Romania, the taxpayers convicted for tax evasion offences are punished automatically by withdrawing the VAT payer code and the ceiling for the previous year is RON 2,250,000 = about GBP 418,000 or EUR 500,000 at the rate set by the National Bank of Romania on 31/12/2013);

- in the UK, even when the cash accounting system for VAT is applied, the standard VAT system is used for the following operations: deliveries/acquisitions of goods in leasing, rental, respectively from other EU countries; the removal of goods from a customs warehouse or free zone; for invoices issued with due dates higher than 6 months; invoice issue before the supply of goods or services (in Romania the exceptions relate to: acquisitions of goods/services for which the reverse charge applies; intra-Community acquisitions of goods; imports);
- in the UK taxpayers may opt for the cash accounting system for VAT without notifying the tax authority. The cash accounting system for VAT is applied from the beginning of any tax period if the taxpayers are already registered for VAT (observing the ceiling mentioned above), respectively for those who are registered for VAT from the date of registration as VAT payers;
- in UK, the cash accounting system for VAT may be left by choice (voluntarily) without notifying the tax authority at the end of any tax period. The cash accounting system for VAT may be reapplied at any time, by choice, without notice, from the beginning of a tax period;
- the records of unpaid suppliers and uncollected customers must be performed faithfully by the UK taxpayers (like in Romania).

5. Conclusions

The remediation of the most criticised issues concerning the regulation of the cash accounting system for VAT in Romania as of 01/01/2014 is a sign of normality for Romania. The possibility of opting for the cash accounting system for VAT and elimination of the due date to collect VAT are major improvements. From this point, this system applied in Romania is similar to that used in other EU countries (UK, Poland, etc.).

The standard VAT system requires:

- VAT collection for any invoice issued, even if it is not paid by the client;
- VAT deduction for any invoice received, even if the supplier remains unpaid.

The cash accounting system for VAT requires:

- postponement of VAT collection for any invoice until the date of payment by the customer. If the invoice is never paid by the customer (the following are similar to collection: compensation, payment in kind, assignment of receivables, the use of payment instruments [3]) then VAT is no longer collected (it is not due to the state);
- VAT deduction for any invoice received, only on the date of payment to the supplier.

Without resuming the disadvantages created by the application in 2013 of the cash accounting system for VAT in Romania as originally regulated [8] (improperly named at that time, as the collection disregarded receipt if it exceeded the period of 90 calendar days), we shall dwell on a few pros and cons for the improved system (with effect from 01/01/2014).

Thus, the arguments in favour of the option of applying this system by the Romanian taxpayers (with a previous turnover lower than the ceiling of about EUR 500,00) include the possibility of achieving a better estimate of the cash-flow, especially in situations where there are claims with cumbersome and lengthy collection. Thus there are no more bottlenecks arising from contractual relationships with public institutions that are among the customers with extremely cumbersome and delayed settlement.

The major disadvantage of applying the cash accounting system for VAT in Romania as of 2014 is that VAT may be deduced only when paying the suppliers. This should be taken into account by taxpayers who mainly use the supplier credit when they choose to apply the cash accounting system for VAT. However, for the newly created taxpayers, the application of the cash accounting system for VAT may also mean giving up the deduction of VAT on the purchase of inventories, machinery and other procurement required for the start of business, until the actual payment thereof.

6. References

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