

Tax Alert
No 2017 – 14
15 November 2017

AMENDMENTS TO THE FISCAL CODE

Please be informed that in the Official Journal of Romania no. 885/10.11.2017 it was published the Emergency Government Ordinance no. 79/2017 amending the Fiscal Code (“Ordinance”).

The Ordinance will enter into force on 1 January 2018.

SUMMARY

Corporate Income Tax. Implementation of the EU Directive 1164/2016 on externalisation of the profits.

- In case of associated companies, exceeding borrowing costs will be deducted in the limit of **200.000 Euro/fiscal year**. The amount that exceeds this deductible cap will be deducted in the limit of **10%** / fiscal year applied to a taxable base expressly regulated by the Ordinance.
- Introduction of the exit taxation: measure preventing the erosion of the taxable base in case of transfer of assets outside Romania.
- Introduction of the anti-abusive rule that will allow the Romanian authorities to refuse taxpayers the tax benefits obtained from abusive arrangements.
- Introduction of certain rules regarding controlled foreign company (CFC) that aim to prevent tax avoidance by diverting revenue to subsidiaries in tax havens.

Profit tax rate is maintained at 16%. Dividend tax rate is maintained at 5%.

Individual Income Tax

- Reduction of individual income tax to **10%** from 16%.
- Dividend tax rate is maintained at **5%**

Social contributions

- Reduction of number of social contributions from 9 to **3**
- Reduction of total social contributions with **2%**
- Transfer of contributions from employers to employees.
From gross salary employees will owe total contributions of 35%, out of which:
 - ✓ **25%** social security contribution
 - ✓ **10%** health insurance contribution
- Contributions will be computed, withheld, declared and paid by the employer
- Employers will due insurance work contribution of **2.25%**

Micro-companies' income tax

- Increase of the cap to be classified as micro-company, from 500.000 Euro to **1 million Euro**
- All taxpayers are included in the micro-companies' income, including those who receive income from management and consultancy

We draw your attention to the fact that the Ordinance must be approved by the Parliament.

It is possible that the approval law will bring amendments to the Ordinance.

We hope that the approval law will be adopted by the Parliament until 31 December 2017, namely until the date on the Ordinance will enter into force, so that we know the tax burden.

We present below, in detail, the most important amendments of the Ordinance brought to the Fiscal Code.

CORPORATE TAX

Description of the current situation

- Currently, the Fiscal Code regulates abusive provisions related to artificial transactions and rules for calculating the tax result based on a mechanism for limiting / non-deducting certain types of expenses or similar items that do not directly compete for obtaining taxable income e.g.: interest paid between affiliated persons, provision of services between affiliated persons), items of expense considered to carry risks related to the erosion of the taxable base.

Amendments

- To combat tax evasion practices corresponding to the corporate income tax, **the Council Directive 2016/1164/EU of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market (ATAD)** was transposed in advance of the mandatory transposition deadline of 31 December 2018, except for the provisions on non-uniform treatment of hybrids, for which the transposition deadline was postponed until 31 December 2019, according to the Art. 1 point 7 of Council Directive 2017/952/EU of 29 May 2017 amending Directive 2016/1164/EU as regards the non-uniform treatment of hybrid elements involving third countries and the need to transpose them uniformly.

Rules regarding limitation of interest deductibility

- Since the deduction method from ATAD (use of a cap of EBITDA¹) differs from current internal method (use of a limitation method via thin capitalisation rules), it has been repealed Art. 27 “Interest and foreign exchange expenses” of the Fiscal Code and were introduced new deduction rules for borrowing costs incurred by the taxpayers.
- *Exceeding borrowing costs* means the amount by which the deductible borrowing costs of a taxpayer exceed taxable interest revenues and other economically equivalent taxable revenues that the taxpayer receives.

1 EBITDA – tax gains of the taxpayer before interest, taxes and amortization

- Taxpayer has the right to deduct, in a fiscal period, exceeding borrowing costs up to the ceiling representing the RON equivalent of the amount of **200.000 Euro**, computed at the exchange rate communicated by the National Bank of Romania valid for the last day of the fiscal quarter/year („Deductible Ceiling”).

- *Exceeding borrowing costs*, which exceed the Deductible Ceiling, are limited deducted in the fiscal period in which these are borne, until the level of **10%** from the following taxable base:

Taxable base used to establish the exceeding borrowing costs, deductible in computing the taxable result, is determined as follows:

income recorded in accordance in accordance with applicable accounting regulations
– expenses recorded in accordance in accordance with applicable accounting regulations
– non-taxable income
+ profit tax expenses
+ exceeding borrowing costs
+ deductible expenses representing fiscal amortization

- If the taxable base has a negative value or equal with zero, exceeding borrowing costs are non-deductible in the reference fiscal period, but are reported, without time limitation, in the following fiscal years in the same deduction conditions.
- For taxpayers that must apply limited interest deductibility, fiscal value of the assets does not include interest costs and other interest-equivalent costs from economic perspective.
- **Exclusions from the scope of limitation rules of the borrowing costs**
 - If the taxpayer is an independent entity, meaning that is not part of a consolidated group for financial accounting purposes, and has no associated company and no permanent establishment, this taxpayer deducts entirely exceeding borrowing costs, in the fiscal period in which these are borne.
 - Exceeding borrowing costs are not limited if these derive from loans used to finance a public infrastructure project for long-term, whose purpose is to supply, improve, to operate and/or to keep an asset of large proportions, considered to be for public interest, if the project economic operators are registered in the EU, and the borrowing costs, the assets used for the project and the income recorded by the project operators derive from/are from EU.
- The rules concerned are also applicable to interest and net foreign exchanges losses carried forward under the provisions of the art. 27 “Interest and foreign exchange expenses” from the current Fiscal Code, provisions in force until 31 December 2017 including.

- In case of independent entities, interest and net foreign exchange losses, carried forward under the provisions of art. 27 “Interest and foreign exchange expenses” of the current Fiscal Code in force until 31 December 2017 including, are entirely deductible.

Fiscal regime of transfer of assets, of tax residence and/or of economic activity performed through permanent establishment for which Romania loses the taxation right („Exit taxation”)

- For transfer of assets, of tax residence and/or of economic activity performed through permanent establishment, taxpayer is subject to profit tax, in accordance with the following rules:
 - It is determined the difference between the market value of the assets transferred in a fiscal period and their fiscal value;
 - If the difference computed is a gain, over this shall be applied profit tax of 16%;
 - If the difference is a loss, this may be recovered from the gains resulted from the operations having the same nature.
- Thus, it will be taxed the economic value of any capital gain created on the Romanian territory, even if this gain was not realised by the exit moment.
- The profit tax so computed shall be reported and paid, for the reference fiscal period.
- The taxpayer, that applies the above rules, benefits from right to rescheduling payment for this tax, by payment in instalments over five years, if it meets the conditions provided in the Fiscal Procedure Code and if the taxpayer is in any of the situations provided in the ordinance.
- *Market value* is the amount for which an asset can be exchanged or mutual obligations can be settled between willing unrelated buyers and sellers in a direct transaction.

Market value is established in accordance with transfer pricing rules.

Anti-abuse rule

- For the purposes of calculating the corporate tax liability, the tax authority shall ignore an arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of the applicable tax law, are not genuine having regard to all relevant facts and circumstances. An arrangement may comprise more than one step or part.
- An arrangement or a series thereof shall be regarded as non-genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality.
- Where arrangements or a series thereof are ignored in accordance with paragraph 1, the tax liability shall be calculated in accordance with profit tax rules from the Fiscal Code.

Rules regarding controlled foreign companies (CFC)

- It is provided reattribution of the income to a CFC, subject to reduced tax in the residency country, to the Romanian taxpayer, parent-company, which becomes, thus, taxable for the attributed income in accordance with CFC rules, in Romania.
- Identification criteria of a CFC entity are:
 - the entity is owned, directly or indirectly, by a Romanian profit taxpayer, in a percent exceeding 50% of the share capital or in case the taxpayer is entitled to receive more than 50% of the profits of that entity;
 - the actual corporate tax paid on its profits by the controlled entity is lower than the difference between the corporate tax that would have been charged on the entity under the applicable profit tax rules from the Fiscal Code of the taxpayer and the actual corporate tax paid on its profits by the entity.
- Income which will be attributed to the Romanian taxpayer, under CFC rules, for taxation are:
 - interest or any other income generated by financial assets;
 - royalties or any other income generated from intellectual property;
 - dividends and income from the disposal of shares;
 - income from financial leasing;
 - income from insurance, banking and other financial activities;
 - income from invoicing companies that earn sales and services income from goods and services purchased from and sold to associated enterprises, and add no or little economic value

MICRO-COMPANIES' INCOME TAX

- **All taxpayers are included in the micro-companies' income.**

Therefore, this system will be applied also by companies that obtain management and consultancy income.

- **Increase of the cap for classifying in this system from 500.000 Euro to 1 million Euro.**

INDIVIDUAL INCOME TAXE

Tax rate

- **Decrease of the income tax from 16% to 10% for the following categories of persons / income:**
 - employees
 - retired persons
 - authorised individuals, copyrights and individual office (e.g.: lawyers, doctors, notaries)
 - rent
 - awards
 - agricultural activities
 - investment income (e.g.: interest, gains from transfer of securities)
 - income from other sources

- 10% rate also applies to annual income norm, the tax being final.

Dividend tax rate is kept at 5%.

Income from independent activities

- For income from intellectual property rights, the tax rate for advance income payments on the account of income tax, which shall be withheld by the income payer, is of 7% applied to the gross income. (Currently the rate is of 10% for a final income tax rate of 16%).

- Health insurance contribution may be no longer deducted from the annual net income.

Salary income

- Increase of personal deductions for individuals. New deductions are:
 - For individuals with salary up to 1,950 lei and for those who do not have persons in their care: 510 lei (increased from 300 lei)
 - For taxpayers with a dependent person: 670 lei (increased from 400 lei)
 - For taxpayers with two dependents: 830 lei (increased from 500 lei)
 - For taxpayers with three dependents: 990 lei (increased from 600 lei)
 - For taxpayers with four or more dependents: 1,310 lei (increased from 800 lei)
 - For taxpayers who earn monthly gross wages ranging from 1,951 lei to 3,600 lei, the personal deductions are degressive in relation to the above and are set according to a table provided by the Ordinance

- Personal deduction is granted for individuals that have a monthly gross income up **1.950 lei** including (ceiling increased from 1.500 lei).

- For taxpayers who obtain monthly gross salary income of over **3.600 lei** no personal deduction is granted (ceiling increased from 3.000 lei).

Income from pensions

- It is clarified that the rights received by individuals according to Law no. 411/2004 on private pension funds and Law no. 204/2006 on voluntary pensions, represent income from pensions.
- In determining the monthly taxable income for the amounts received as single payment in accordance with the Law no. 411/2004 and Law no. 204/2006, each pension fund grants a single non-taxable income ceiling, which is currently 2,000 lei and remains unchanged.

Transitional provisions

- For revenues realised in the fiscal year 2017, tax liabilities are those in force at the date when the income was obtained.
- Provisions on income tax apply to income earned and expenses incurred by individuals as of 1 January 2018.
- In the case of interest income for fixed term deposits / sight / current accounts, acquired savings instruments, civil contracts concluded before the date of 1 January 2018, the 10% tax rate is applied starting with the current / deposited / redeemed / paid revenue, as of that date.
- In the case of income from salaries and pension income, the provisions on income tax apply for the starting with the income obtained for January 2018.

SOCIAL CONTRIBUTIONS

1. SALARY INCOME

Contribution rates

Description of the current situation

Currently, rates of mandatory social contributions are the following:

Contribution	Total rate	Employee	Employer
Social security contribution	26.3% for normal working conditions applied on gross gains	10.5%	15.8%
	31.3% for special working conditions applied on gross gains	10.5%	20.8%
	36.3% for particular working conditions and for other working conditions applied on gross gains	10.5%	25.8%
Health insurance contribution	10.7% applied on gross gains	5.5%	5.2%
Unemployment insurance contribution	1% applied on gross gains	0.5%	0.5%
Contribution for holidays and indemnities of health insurance	0.85% applied on total gross gains realised by the employees, but capped at the product between the number of insured persons and the value of 12 minimum gross salaries per economy	–	0.85%
Contribution for holidays and indemnities of health insurance	0.15 – 0.85% differentiated according to the risk class	–	0.15% - 0.85%
Contribution to the Fund to Guaranty Salary Receivables	0.25% applied on gross gains	–	0.25%
Total for normal working conditions	39.25% - 39.95%	16,5%	22.75% - 23.45%

Amendments

- **Reduction of social contributions and their transfer from employers to employees.**
 - Level of contributions decreases with **2%**: from **39.25%** contributions paid to a gross salary to **37.25%**.
 - From a total of 22.75% contributions due by the employer, 20% is transferred to the employee.
 - In total, for gross salary:
 - ✓ **35%** will be contributions withheld by the employer in the name of the employee,
 - ✓ and the contributions remained at the employer of 2.75% (after the transfer of 20% to the employee), decrease at **2.25%** and cover risks for unemployment, work accidents, medical leaves and salary receivables.

These are included in a single contribution: work insurance contribution.

- **From the 9 contributions paid currently by the employee and employer remained only 3:**
 - pension contribution – paid by the employee
 - health contribution – paid by the employee
 - work insurance contribution – paid by the employer
- There are decreased pension contributions for special conditions:
 - pension contribution for special work conditions decreases from 31.3% to **29%** (-2.3%)
 - pension contribution for special work conditions decreases from 36.3% to **33%** (-3.3%)

Social security contribution

- **Rates of the social security contributions are the following:**
 - **25%** due by the employees or for those for which the social security contribution shall be paid
 - **4%** due by the employers in case of special working conditions
 - **8%** due by the employers in case of particular working conditions and other working conditions
- Pensioners of the social security systems owe social security for salary income (currently, they are except).

Health insurance contribution

- **Health insurance contribution rate is of 10% due by the employees or for those for which the health contribution shall be paid**

Work insurance contribution

- **Rate of work insurance contribution is of 2.25%.**
- Taxpayers obliged to pay the work insurance contribution are, as the case may be:
 - natural and legal persons who have the status of employers or are assimilated to them, for Romanian citizens, for citizens of other states or for stateless persons, while they are domiciled or residing in Romania, in compliance with the provisions of the European legislation applicable in the field of social security, as well as of the agreements on social security systems to which Romania is a party;
 - Romanian citizens, citizens of other states or stateless persons during their domicile or residence in Romania, and who earns salary income in Romania from employers from states not subject to the applicable European legislation in the field of security social, as well as agreements on the social security systems to which Romania is a party.
- Work insurance contribution is for salary income and salary assimilated.
- Work insurance contribution is due also in the case when salary income and salary assimilated obtained by the individuals whose income is tax exempt, thus:
 - individuals with severe disabilities;
 - Individuals, for salary income and salary assimilated, as a result of the computer program creation activity;
 - individuals, for salary income and salary assimilated, as a result of performing research and development activity and innovation;
 - individuals, for salary income and salary assimilated, as a result of carrying out the activity on the basis of an individual labour contract concluded for a period of 12 months, with Romanian legal persons carrying out seasonal activities.

Other provisions

- The social security contribution and the health insurance contribution due by individuals who receive salary income or salary assimilated on the basis of a full-time or part-time individual labour contract may not be less than the level of social contributions related the country-wide minimum salary in force for the month for which the social contributions are due, corresponding to the number of working days in the month in which the contract was active (part-time measure).

- The above measure does not apply in case of individuals that are in any of the following situations:
- are students aged up to 26 years in a form of schooling;
 - are apprentices, according to the law, under the age of 18;
 - are people with disabilities or other categories of persons, who by law can work less than 8 hours a day;
 - have the status of old-age pensioners in the public pension scheme, except for old-age pensioners who benefit from service pensions under special laws / statutes, as well as those who cumulate the old-age pension in the system pension public with the pension established in one of the pension systems not integrated with the public pension system;
 - earns salary income on the basis of two or more individual labour contracts during the same month, and the cumulative monthly base for them is at least equal to the gross minimum basic salary in the country.

The employer must require justifying documents from the persons which are in the situations mentioned at the letters a), c) and d), and in the situation at the letter e), the application procedure is established by order of the Ministry of Finance.

Summary of the new rates

Contribution	Employee	Employer	Total
Social security contribution	25%	--	
	--	4% for normal working conditions	
	--	8% for particular working conditions and for other working conditions	
Health insurance contribution	10%		
Work insurance contribution	--	2.25%	
Total	35%	2.25% - 10.25%	37.25% - 45.25%

2. INCOME FROM INDEPENDENT ACTIVITIES

Social security contribution

- Individuals who obtain income from independent activities (e.g. traders, doctors, lawyers, notaries, journalists, writers, artists etc.) will compute and due social security contribution to a chosen income, which however may not be less than a minimum salary per economy („Minimum Ceiling”).
- Therefore, these persons will pay no longer social security contribution reported on the amounts obtained from independent activities.
- Individuals, who in the previous fiscal year obtained cumulated income from independent activities below the Minimum Ceiling, are not obliged to submit income return and do not owe social security contribution for the current year.

However, these persons may opt to submit the income return and to pay social security contribution for the current year, in the same conditions provided for the persons who obtain monthly income higher than the minimum gross salary. As a rule, the option is mandatory for the whole fiscal year.

Specific exemptions on income from independent activities

- Remain unchanged the provisions according to which do not owe the social security contribution for the income from independent activities:
 - individuals insured in their own social insurance systems, which are not obliged to insure in the public pension system, for which there is an obligation to ensure in these systems according to the law (lawyers, notaries, monastic staff, military personnel);
 - people who are retired.

3. PROVISIONS REGARDING HEALTH INSURANCE CONTRIBUTION

Income subject to health insurance contribution

- Individuals (who are not except from payment of health insurance contribution (e.g.: children up to 18 years, students)), owe health insurance contribution if they obtain cumulated annual income at least equal with 12 gross minimum salaries („Annual Ceiling”) from one or several income source from the following categories of income:
 - income from independent activities;
 - income from joint venture with a legal person;
 - income from rent of goods;
 - investment income;
 - income from agricultural, forestry and fish farming activities;
 - income from other sources.

- These provisions do not apply in case of income obtained from:
 - individuals with severe disabilities, for income realised by them;
 - individuals, for salary income and salary assimilate further to performing to computer program creation.

Computation base of the health insurance contribution

- **Monthly computation base for which individuals due health insurance contribution is minimum gross salary per economy.**
- Income considered for verifying the Annual Ceiling is that realised from one or several income source, from the following categories:
 - net income from independent activities;
 - gross income from joint venture with a legal person;
 - net income or income norm from rent of goods;
 - investment income / capital gain;
 - net income or income norm from agricultural, forestry and fish farming activities;
 - gross income / taxable income from other sources.
- Classifying in the Annual Ceiling is realised by summing the annual income mentioned above, realised in the previous fiscal.
- Individuals obliged to pay health insurance contribution shall submit annually to the tax authority, until 31 January including of the year for which health insurance contribution is established, a tax return on the classifying of the income in the Annual Ceiling.
- In case of taxpayers who start an activity or cease to obtain income during the fiscal year, and the estimated monthly income to be obtained, from one or several of income source from those mentioned above, is at least equal with level of the minimum gross salary per economy in force in the month in which the income is estimated, shall submit that return within 30 days from the date when the event occurred.
- Individuals, who obtain annual income below the level of 12 minim monthly salaries, may opt to submit the tax return mentioned above and to pay health insurance contribution for the current year, in the same conditions provided for the persons who obtain annual income higher than the level of 12 minimum gross salaries. As a rule, the option is mandatory for the whole fiscal year.

Computation and payment of the health insurance contribution

- Health insurance contribution due by individuals is established by the competent tax authority, through a taxation decision, based on the return regarding classifying in the Annual Ceiling.
- If the taxation decision computation base of the health insurance contribution is mentioned monthly, while the payment shall be performed quarterly, in 4 equal instalments, by 25th including of the last month from each quarter.
- Individuals who during the fiscal year cease the activity or enter into temporary suspension of the activity, shall submit to the competent tax authority, within 30 days from the date when the event occurred data, a declaration to stop the payment of the health insurance contribution.

Health insurance contribution for individuals with no income

- Individuals who do not obtain income and who are excepted from payment of health insurance contribution, owe this contribution as follows:
 - monthly, by applying the rate over the minim gross salary per economy, and shall pay the health insurance contribution for a period of at least 12 consecutive months, starting with the month in which is submitted the return for establishing the contribution; or
 - at the date on they access the services granted by the public health insurance, by submitting the return for establishing the contribution, applying the rate over a computation base represented by the value of 7-time gross minim salary per economy.
- For individuals without income computation base over which is paid health insurance contribution is the minimum gross salary in the month for the contribution is due, to corelate with the increase of the monthly minimum gross salary and with the fiscal regime applicable to other categories of taxpayers to the national health insurance system.

4. TRANZITIONAL PROVISIONS

- For the income related to the fiscal year 2017, mandatory social contributions are those in force in the period to which the income is related.
- Provisions regarding mandatory social contributions will be applied to the income realised starting with 1 January 2018.

VAT

- Clarify that the sanctioning of an economic agent with the refusal to deduct VAT is possible only if there is evidence that he has clear information about the activity of the tax evasion firms with which he entered into commercial relations.

It is provided that the competent tax authorities have the right to refuse deduction of VAT if, after administering the evidence provided for by law, they can show beyond doubt that the taxable person knew or ought to have known that the operation put forward to justify the right to deduct was involved in a VAT fraud occurring upstream or downstream of the supply chain.

EXCISE DUTIES

- Extension of confiscation also over means of transportation for persons who make evasion by trading unmarked excisable products: alcohol and tobacco products.

For additional information, please contact the following persons:

PhD Stela Colun – Tax advisor

Mobile: +40 748 733 865

E-mail: stela.colun@colman.ro

Alina Mănescu – Tax advisor

Mobile: +40 728 182 395

E-mail: alina.manescu@colman.ro

Colman Tax SRL

Tax Advisory Firm authorised by the Chamber of Tax Consultants from Romania

3 Jean Texier Street, 4th Floor, 5th Apt.

011901 Bucharest, Sector 1

This material is informative. Colman Tax SRL assumes no responsibility for the use of the information contained in this bulletin without the prior consultation of our consultants.