

A COMPARATIVE STUDY ON THE INCOME TAX FOR PHYSICAL PERSONS AND LEGAL ENTITIES

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Abstract: As per the Fiscal Code, the incomes obtained from independent activities are included in the category of incomes that are subject to the income tax. They include: trading income, income obtained from freelance activities, and income resulting from intellectual property rights, obtained individually and/or in some sort of association, including from related activities.

Key words: the income tax, the corporate tax, the income tax for physical persons, the income tax for micro-companies.

1. The taxation on the incomes obtained from independent activities

The income obtained from freelance activities is the kind of income resulting from professions such as: medical practitioner, lawyer, notary, financial auditor, fiscal advisor, expert accountant, chartered accountant, advisor for security placements, architect, or practitioner of any other profession established by law, carried out in an independent manner.

The practice of these professions is established through distinct laws, specific to each of them, and from a legal point of view these activities can be organized either in individual offices or in trading or civil companies, as is the case.

Thus, for instance, in the case of such professions as expert accountant and chartered accountant, the laws under effect in this field provide that these professions can be practiced either individually, within own offices, or the professionals can form trading companies, as per the applicable law.

When these professions are practiced individually, the income resulting is subject to taxation as per the legal regulations specific to the income obtained by physical persons; when these professions are practiced within civil or trading companies, the income obtained is subject to taxation as per the rules applicable to legal entities (either income tax, or income tax for micro-companies, as is the case).

In Romania, the taxation of these incomes obtained by physical persons in an individual manner was conducted, until the year 2004 inclusively, by applying on the net income, established in a real system, a set of tax quotas established by instalments of taxable income, according to the annual standards set forward in legal regulations; the tax quotas then varied between 18% and 40% for the income that exceeded the maximum limit.

Following the introduction of the flat income tax, beginning with January 1st 2005, this kind of income is taxed by applying a quota of 16% to the net income established in a real system.

The tax payers who obtain incomes by performing an independent activity (except for the incomes for which the tax is withdrawn at the source), must pay a tax, during the year, in the form of advance payments, on the account of the income tax, such tax being established based on the income estimated for the current year or based on the net income obtained from that activity in the previous year, by applying to it the legal tax quota. The advance payments are to be made in 4 equal instalments, until the 15th of each month of each trimester.

In the year subsequent to the year when these incomes were obtained, a final taxation is carried out, based on the data actually achieved, and the tax on the net annual income is calculated by the competent fiscal body, in basis of the income statement, by applying the legal tax quota to the net annual taxable income of that fiscal year.

The net income obtained from independent activities is calculated, in a real system, as a difference between the gross income and the expenses entailed by the process of obtaining the income, deductible, based on the data provided by the single-entry bookkeeping. The tax payers who establish the net income in a real system must keep a record of the operations through the single-entry bookkeeping system, to fill in the Check register, the Inventory-register, and other accounting documents, as provided by the law.

Since, as it was indicated before, these tax payers may choose to pay the income tax either as per the laws specific to physical persons, or as provided by the laws applicable to legal entities (corporate tax or income tax for micro-companies, depending on their option), my paper will conduct a **comparative study** between the three forms of taxation – **the income tax for physical persons – the corporate tax – the income tax for micro-companies**, as they were in 2004, respectively 2005, to emphasise the differences between them and the advantages of each of them. To this purpose, the paper analyzes a private consulting room where income is obtained by performing medical professions; the tax due for this income, in the three versions described above, was calculated based on the data provided by the accounting registers.

2. General presentation of the private consulting room

The general medicine consulting room of “Doctor Andru Dana” is a sanitary unit established as per the Government Order no. 124/1998, on the establishment and registering of private consulting rooms. This consulting room is working according to the provisions of the Government Order no. 153/2003 on the organization and functioning of private consulting rooms. This private consulting room has no legal personality, and it exists only in the form of “Consulting Room”.

The scope of this consulting room includes:

- providing primary medical assistance (as treatment or prevention);
- providing emergency medical assistance;
- providing activities related to the medical profession.

A. The income of the consulting room is obtained from the following:

- medical services provided in basis of the contract signed with the District department of health insurance, or other physical persons or legal entities;
- medical services paid directly by the clients;
- donations, sponsorships;
- counselling and advising activities in the field of medicine;
- activities contracted with the units that coordinate the learning and research activities in the network of the Ministry of Health;
- other sources obtained in compliance with the legal provisions, including the ones obtained from selling the owned equipment that is worn out (either physically, or no longer up to date), as well as the exceeding equipment owned.

The income obtained from the activity of the consulting room is to be submitted to taxation according to the legal provisions on the taxation of the incomes resulting from activities carried out in basis of free initiative.

The bookkeeping of the private consulting room uses single entries, as per the Accountancy law, and is performed by qualified personnel, in basis of a service providing contract for performing bookkeeping activities.

B. Categories of deductible expenses for the private consulting room

The character of the activity carried out in the private consulting room entails deductible expenses which are common to other companies too, as well as specific expenses:

- expenses related to the personnel:
 - salary expenses;
 - compulsory contributions;
 - travels, assignments, transfers, related to the medical activity carried out;
- expenses related to materials and services – drugs and sanitary materials;
- expenses related to maintenance and administration;
- materials specific to the sanitary field;
- materials and services that have a functional character;
- taxes for professional organizations;

- taxes for continuous medical training;
- insurances;
- inventory items;
- current and capital repairs;
- books and published materials;
- protocol.

3. Calculation of the net income and due tax

The present study is based on the accounting documents of the private consulting room.

According to the accounting registers, in 2004 the Consulting Room of Doctor Andru recorded incomes amounting to 277.141.299 lei, as follows:

- income obtained from medical services provided in basis of the contract signed with the District department of health insurance
270.525.799 lei
- income obtained from medical services paid directly by the clients
1.320.000 lei
- income obtained from various taxes
5.295.500 lei

TOTAL	INCOME
277.141.299 lei	

According to the laws under effect concerning the deductible expenses for a private consulting room, as well as to the explanatory accounting documents, in 2004 the total expenses amounted to 261.251.220 lei, as follows:

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|---|----------------|
| - expenses related to salaries | 69.805.200 lei |
| - expenses related to sanitary materials | 35.138.939 lei |
| - expenses related to inventory items | 23.261.164 lei |
| - expenses related to pharmaceutical products – drugs | 18.187.800 lei |
| - expenses related to fuel | 15.394.075 lei |
| - expenses related to the insurances | 18.915.900 lei |
| - expenses related to the monthly car instalments | 46.381.440 lei |
| - expenses related to taxes and contributions | 9.389.000 lei |
| - expenses related to heating | 7.480.918 lei |
| - expenses related to the phone bill | 3.800.000 lei |
| - expenses related to services provided through third parties | 3.372.081 lei |
| - expenses related to the power supply | 2.425.396 lei |
| - expenses related to water supply, the sewage system, and cleaning | 4.004.455 lei |
| - expenses related to the rent for the location | 1.474.352 lei |
| - travelling expenses | 2.220.000 lei |

TOTAL EXPENSES	261.251.220 lei
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A) The tax on the income obtained from independent activities

The net income obtained from independent activities is established in this case as the difference between the gross income achieved and the expenses entailed by the process of achieving this income – deductible, registered in the single-entry bookkeeping, as follows:

Gross income	= 277.141.299 lei
Expenses	= 261.251.220 lei
Net income	= 15.890.079 lei

For the year 2004 the tax quota applied to this part of the income was of 18%, and for the year 2005 the quota applied was that of 16% (the flat income tax).

The due income tax is shown in **Table 1.:**

Table 1

The income tax due for the period 2004-2005

Year	Net income (lei)	Tax quota	Due Tax (lei)
2004	15.890.079	18 %	2.860.214
2005	15.890.079	16 %	2.542.413

B) The corporate tax

The taxable profit is calculated as the difference between the incomes obtained from any source and the expenses made in order to obtain income, during one fiscal year, out of which non-taxable incomes are subtracted, and to which non-deductible expenses are added.

Incomes = 277.141.299

Expenses = 261.251.220

Profit = 15.890.079

The corporate tax quota applicable to the taxable profit was of 25% until the 1st of January 2005; afterwards, the system changed to apply the flat income tax of 16%.

The due corporate tax is shown in **table 2.:**

Table 2.

The corporate tax due for the period 2004-2005

Year	Taxable profit (lei)	Tax quota	Due Tax (lei)
2004	15.890.079	25 %	3.972.250
2005	15.890.079	16 %	2.542.413

C) The income tax for micro-companies

The Romanian legal entities that meet the legal requirements for being established as micro-companies may choose between paying the tax either as corporate tax or income tax.

Total incomes = 277.141.299 lei

The tax quota for the year 2004 was of 1,5%, and beginning with the 1st of January 2005, it changed to 3%.

The income tax for the micro-company is shown in **table 3.:**

Table 3.

The income tax for the micro-company due for the period 2004-2005

Year	Total income (lei)	Tax quota	Due Tax (lei)
2004	277.141.299	1,5 %	4.157.119
2005	277.141.299	3 %	8.314.239

The comparative status of the three tax categories, for the years 2004 and 2005, applied to the study conducted on the private consulting room, is shown in **table 4.:**

Table 4.

Comparative status of the three tax categories, for the years 2004 and 2005

Year	Independent activities		Corporate tax		Income tax for a micro-company	
	Tax quota	Due tax (lei)	Tax quota	Due tax (lei)	Tax quota	Due tax (lei)
2004	18 %	2.860.214	25 %	3.972.250	1,5 %	4.157.119

2005	16 %	2.542.413	16 %	2.542.413	3 %	8.314.239
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4. Conclusions

This comparative study of the situation of the three tax categories for the years 2004 and 2005, applied to the same income, to the Private Consulting Room of "Doctor Andru", leads to the following conclusions:

a) In **2004** the most disadvantageous situation from the point of view of tax obligations was that of the micro-company that paid an income tax, although the tax quota was the smallest of them all. This is due to the fact that the 1,5 % quota was applied to all the incomes. The most advantageous form of organization, taking into account the calculation of the tax for 2004, is that of freelance professional, which was also the form chosen by the Private Consulting Room of "Doctor Andru".

In conclusion, in 2004 the Private Consulting Room had the most advantageous form of organization.

b) For **2005** the comparative study leads to the same conclusion as for 2004, which is, that the micro-company paying an income tax has the most disadvantages. In return, there is an equality of status between the freelance professionals (physical persons) and those who pay the corporate tax, because the same quota of 16 % is applied in both cases.

c) **The comparative situation for the years 2004 and 2005**, in that which concerns the three tax categories, clearly shows that the tax quotas for physical persons and the corporate tax payers were down in 2005 to the flat income tax quota of 16 %, which puts the year 2005 in a more advantageous situation as 2004.

By contrast, for the micro-companies paying the income tax, the tax quota doubled from 1,5 % to 3 %, which is a disadvantage. Still, the new laws provide the micro-companies with the option of choosing to pay the corporate tax instead, which is an option that didn't exist in 2004.

In conclusion, in the case of the income tax for independent activities, and of the corporate tax, the introduction of the flat income tax quota of 16 % led to an obvious decrease of the due tax and, implicitly, is the most advantageous option from this point of view. In that which concerns the micro-companies that pay an income tax, although the tax quota doubled, many economic agents have chosen this form of organization most probably for other reasons related to fiscal control.

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