RELATIVE TAX MATTERS TO INSOLVENCY PROCEDURE

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In terms of tax rules, we find rules in the Tax Code which link to specific stages of insolvency procedure the production of some tax effects.
In this paper, we present these legal provisions, among which we mention: the integral deductibility of the losses recorded when clearing from the list of the uncollected debts if the insolvency procedure of debtors was closed on a law court's decision, the adjustment of collected VAT if the debt can not be collected because of the bankruptcy of the beneficiary; application of the simplification measures for the deliveries / procurements / by a person against whom the insolvency procedure was opened, and so on.

Keywords: insolvency procedure, bankruptcy procedure, legal reorganization

JEL Classification: H3, H32

I. Introductory Considerations

Lately, in the global economic crisis, more and more economic agents face with financial difficulties, which, in some cases, led them to the termination of payments. This state of affairs has reacted also on their business partners, who, thus, were unable to achieve the debts.
The Romanian law givers had constant concerns in reforming, adjusting and improving the legal regimen of insolvency, the last major legislative reform being the Law No. 85/2006 on insolvency procedure.
In terms of tax rules, we find rules in the Tax Code which link to specific stages of insolvency procedure the production of some tax effects.
Thus, by way of example, we show that the Tax Code regulates the integral deductibility of the losses recorded when clearing from the list of the uncollected debts if the insolvency procedure of debtors was closed on a law court's decision, the adjustment of collected VAT if the debt can not be collected because of the bankruptcy of the beneficiary; application of the simplification measures for the deliveries / procurements / by a person against whom the insolvency procedure was opened, and so on.
In what follows we suggest, for the correct interpretation and application of tax regulations, to clarify the concepts of operation of tax law giver and which we find in the Law no. 85/2006 on insolvency procedure.

II. Short presentation of the insolvency procedure

The Law No. 85/2006 regulates two forms of the insolvency procedure – the general procedure and the simplified procedure, each applying in certain circumstances expressly regulated, but which do not form the subject of our study.
The general procedure represents the procedure whereby the debtor enters, after the observation period, successively, the legal reorganization procedure and the bankruptcy procedure or, separately, only the legal reorganization procedure or only the bankruptcy procedure[81].

81 Art. 3 item 24 of the Law no. 85/2006.

The simplified procedure is the procedure whereby the debtor enters directly the bankruptcy procedure, either once with the opening of the insolvency procedure or after a period of observation of maximum 60 days[82].
The legal reorganization is defined, by the item 20 of the article 3, as the procedure to be applied to the debtor, legal person, in order to pay its debts, according to the payment program of debts. The reorganization procedure involves the drafting, approval, implementation and compliance with a plan, called reorganization plan, which may provide, together or separately:
- Operational restructuring and / or financial restructuring of the debtor;
- Corporate restructuring by altering the structure of stock share;
- Restriction of activity by the liquidation of some assets from the debtor's property.
The bankruptcy procedure is defined, in the text of the item 23 of the article 3, as the collective and egalitarian corporate insolvency procedure which applies to the debtor in order to liquidate its property to cover its liabilities, being followed by the deletion of the debtor from the registry where it is registered.
In a synthetic speech, given the definitions above:
- the general procedure, in the most extended form, involves going through the following chronological phases: the opening of the insolvency procedure; the entry into reorganization;
- assuming the success of the plan of reorganization, the insolvency procedure closes;
- assuming the failure of reorganization, the bankruptcy procedure is opened; the liquidation of the debtor's property, the closure of the procedure and the cancellation of the debtor;
- the simplified procedure involves: opening the insolvency procedure and concomitantly / subsequently the opening of the bankruptcy procedure, the liquidation of the debtor's property, the closure and cancellation procedure of the debtor.

III. Presentation of tax rules that are incident in the insolvency procedure

We present hereinafter the tax regulations incident in the insolvency procedure, contained both in Title II relating to tax on profit, and Title VI, on the value added tax.
A. Article 21 paragraph (2) letter n) of the Tax Code, provides that the law giver regulates the integral deductibility of the losses recorded by removing from the list of the uncollected debts **if the bankruptcy procedure of the debtors was closed on a law court's decision,** considering that these losses are expenses incurred for the purpose of achieving revenues.
B. In addition, the integral deductibility is regulated, or, where appropriate, limited, as we show below, of the provisions established for the uncollected customers:

- for the debts registered after 01.01.2007[83]

The provision is fully deductible up to a percentage of 100% of the debts on customers.
In order to be deductible, the provision established under the Article 22 paragraph 1, letter j, it is necessary that these debts to meet cumulatively the following conditions:
- there are registered after the 1st of January 2007;
- the debt is owned by a legal person on whom the procedure of opening the bankruptcy is declared, on the grounds of a law court's decision which attests this situation;
- there are not guaranteed by another person;
- there are due by a person who is not affiliated with the taxpayer;
- there were included in the taxable incomes of the taxpayer.

- for the debts registered before 01.01.2004[84]

The provisions established for the debts on customers, registered by taxpayers before the 1st of January 2004, are deductible within the limits laid down in the art. Article 22 paragraph (1) letter

82 art. 3 item 25 of the Law no. 85/2006.
83 art.22 paragraph 1 letter j of the Law no. 571/2003 with its subsequent amendments and additions
84 Art.22 paragraph 8 of the Law no. 571/2003 with its subsequent amendments and additions

c)[85]. . In order to be deductible, the provisions established under the Article 22 paragraph (8), it is necessary that these debts to meet cumulatively the following conditions:
- there are not guaranteed by another person;
- there are due by a person who is not affiliated with the taxpayer;
- there were included in the taxable incomes of the taxpayer;
- the debt is held on a legal person on whom the bankruptcy procedure was opened, on the grounds of a law court's decision which attests this situation; - there haven't been established tax deductible provisions for that debt
It can be noted that in the legal assumptions presented above, it is made reference to the decision of opening the bankruptcy procedure, respectively the decision on closing the bankruptcy procedure, without the law giver to clarify whether those decisions should be irrevocable.
Given that, according to the art. 12 paragraph 1 of the Law no. 85/2006, these decisions are final and enforceable, we consider that, in the absence of a relative express regulation regarding the irrevocable character of the decisions, the deductibility of loss, as well as of provisions, to which we referred above, appears at the time of ruling the decisions.
C. According to the art. 160 paragraph (2) letter d) of the Tax Code, the application of simplification measures is mandatory if the insolvency procedure was opened, at least against one of the contracting parties, either the provider / supplier or the beneficiary. As an exception, there are not applied the simplification measures in the case of goods supplied in the retail trade.
It is known that the simplification measures consisted in the following:
- on the invoices issued for the respective operations, suppliers are obliged to register the word "reverse charge", without registering the afferent charge;
- on the invoices received from suppliers, beneficiaries will sign up the afferent charge, that they highlight both as the collected tax, as well as the deductible tax in the tax settlement. Accountant, the beneficiary shall register during the tax period 4426 = 4427 with the amount of the afferent charge;
- for the operations subject to simplification measures it is not made the payment of the tax between supplier and beneficiary. The accounting registration 4426 = 4427 to the buyer is called the self liquidation of the value added tax, the collection of value added tax to the level of deductible tax is assimilated to the payment to the supplier / provider.
The Tax Code regulates two conditions, whose cumulative meeting is necessary for the application of the simplification measures: both supplier and beneficiary must be registered for a VAT purpose, respectively the operation should be taxable.
Regarding the second condition, namely, that the operation to be taxable for the application of the simplification measures, we consider that it should be made some clarifications. Given the specific of the simplification measures, meaning that the provider / supplier does not collect the VAT for the respective operation, and makes no actual payment of the VAT between supplier and beneficiary, in practice, there have appeared some situations in which it has been mistaken the application of the simplification measures with an exempted operation.
As stated above, the operations for which the simplification measures are applied are taxable transactions, the simplification measures representing a form of payment of VAT. Thus, for the exempted operations without the right to deduct for which one may choose to charge, covered by the art. 141 paragraph 2 letter e[86] and letter f)[87], there shall not be applied "automatically" the simplification measures, but only assuming that it chooses to charge transactions, by filing the appropriate notifications.
Example:

85 for the year 2008, the provision is deductible up to 30% of the uncollected debts.
86 hire, rent, leasing of real estate
87 Total/partial delivery of an old building and lands of any kind, except those available for building

A trading company which has entered into insolvency procedure sells an agricultural land and does not choose to charge - because there aren't economic and tax reasons to express this option[88]: the delivery shall be made within an exempted regimen, without the right to deduct. If choosing for charging, it is compulsory to apply the simplification measures.
According to the art. 138 paragraph 1 letter d of the Tax Code, the tax base is reduced if the equivalent value of the delivered goods or provided services can not be collected because of the bankruptcy of the beneficiary. The adjustment is allowed from the date of the ruling of the law court's decision to close the procedure laid down by the Law no. 85/2006 on insolvency procedure, decision remaining final and irrevocable.
An additional condition for the adjustment of VAT is included in the item 20 paragraph 3 of the Government Decision 44/2004, which states that the adjustment of the tax base of value added tax, referred to in the art. 138 letter d) of the Tax Code is permitted only if the date of declaration of bankruptcy of the beneficiaries has occurred after the 1st of January 2004, including for the invoices issued before that date, if the equivalent value of the delivered goods / provided services or the value added tax recorded in these invoices can not be collected because of the bankruptcy of the beneficiary.
The judgement for this regulation consists in abiding the principles of neutrality and transparency of VAT. Basically, it reaches a situation in which the supplier / provider pays VAT to the budget, which was not collected from the client, provided that the failure of the debts is not attributable to him.
Given the specifics of this situation, respectively the fact that after the date of closing the bankruptcy procedure, the debtor is cancelled, the adjustment made in the case covered by the art. 138 paragraph 1, letter d has the following features:
- the adjustment is made by issuing an invoice with the values entered with a minus, but which it shall also not be notified to the beneficiary;
- the beneficiary shall not adjust, correlatively, the right to deduct that he practised for the respective operation.
Example:
SC X LLC provides services to SC Y LLC, collecting the afferent VAT on this transaction. Subsequently, SC Y LLC, is cancelled as a result of closing the bankruptcy procedure, but without the SC X LLC to collect its debt. In this situation, in the settlement afferent to the tax period (month/quarter) when the decision to close the bankruptcy procedure remained final and irrevocable, SC X LLC shall be able to reduce the initially collected VAT.
It is necessary to point out that in drafting the text of the art. 138 paragraph 1 letter d, the tax law giver uses an inaccurate terminology when operating with the notions contained in the Law no. 85/2006, which creates difficulties of interpretation. Thus, it is noted that the non-collection of the debt is due to the bankruptcy of the debtor, but the tax adjustment is made on the law court's decision, final and irrevocable, of closing the insolvency procedure.
Or, as we showed above, the insolvency procedure regulated by the Law no. 85/2006 can be closed also as a consequence of achieving the reorganization plan, case in which, obviously, the debtor does not go also through the bankruptcy procedure. This inaccuracy should be corrected, just to ensure the accuracy of the legal text.
D. The reimbursement of VAT for the impossibility of recovering the tax paid by the supplier, if the tax was erroneously entered in the invoice and for which the beneficiary, of course, has no right to deduct.
According to the art. 150 paragraph 3 of the Tax Code, any person who entered a tax on an invoice or any other document serving as invoice is required to pay it.

88 For instance: it did not deduct the VAT on land acquisition as it purchased it from a natural person, and, consequently, has no obligation to adjust the deducted VAT, if it resells it under the exemption regimen without the right to deduct.

The person who wrongly enters the tax into an invoice or another document treated as an invoice, shall pay this tax to the state budget, and the beneficiary will not be entitled to deduct such tax. In this case, the beneficiary may request the supplier or provider the correction of the invoice prepared wrongly, by issuing an invoice with the minus sign and a new correct invoice.
Assuming that the supplier or provider is unable to correct the invoice issued in error due to the release of the liquidation, bankruptcy, cancellation procedure or other similar situations, the tax law giver regulated by the item 58 paragraph 2 of the Government Decision 44/2004, a refund procedure of this tax not due to the budget, the beneficiary-applicant must proving the fact that he paid this tax to the supplier, as well as the fact that the supplier has paid the respective tax to the state budget.
Frequently, such an erroneous invoicing of the value added tax appears for the exempted operations without the right to deduct, but for which there is an option to charge, covered by the art. 141 paragraph 2 letter e and letter f of the Tax Code.
For example, assuming that it is rented a building and the owner invoices as normal charge, without filing to the tax authorities the notification by which he expresses this option, the renter has no right to deduct this tax and will require the owner to correct the invoice.
There is a possibility that since the invoicing date, the owner trading company to be declared bankrupt and thus to be unable to correct the invoices. In this situation, the renter will request the reimbursement from the budget of the value added tax, but needing to prove that he paid that tax to the owner as well as the fact that the owner has paid such tax to the state budget.

IV. Conclusions

From the above exposed, it appears that the tax law giver was concerned to cut the financial financial losses of economic agents whose business partners have been declared bankrupt as a result of not collecting the debts held on them. In practice, however, given the fairly long period before declaring bankruptcy (several years), inflation tends to cancel the positive effects of these regulations.

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