

# THE ROMANIAN ACCOUNTING SYSTEM AND THE ACCOUNTING-TAXATION RATIO

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*In the context of a developed capital market, the dimensioning of the accounting profit is very important for investors, considering the financing of the economical entities to a higher degree than that offered by the banking system. The disconnection between accountancy and taxation stands as an essential premise. Considering this, we find three categories of major risks to be significant, together with the expanding tendencies regarding the distortions of the accounting result, which refer especially to the Romanian accounting and taxing system: creative accountancy (a form of disconnection between accountancy and taxation), taxation (a form of connection between accountancy and taxation) and the inflationary phenomenon. Even though the latter is rather low, the particularities of the Romanian economy creates certain conditions for a significant enhancement of the effect of general frugal having important taxing implications on the decapitalization of the economic entities.*

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## **1.Introduction - the materialization of Double Entry implementation in Romania**

The materialization of double entry in the Romanian Principalities was not exactly estimated, there are some opinions that sustain that “it is impossible that the venetians that came to our countries [...] should not have spread out the secrets of this art that is vital to any merchant willing to observe by systematical calculations, how his trade goes”<sup>547</sup>. On the other hand, real proofs of double entry accountancy can be found “in the accounting notes registers of the great merchants from Sibiu, Braşov and Bucharest from the XVIII century”<sup>548</sup>.

The organic regulation from 1831 played a significant role in the evolution of the Romanian accountancy. “For the first time in the Romanian Principalities a regulate accountancy was organized based on the Organic Regulation, that would make possible the controlling of the assets that were used by the state servants; [...] The public houses service, the public education service, the mining service were organised, all f them being under state control”<sup>549</sup>. At state level the double entry accountancy was introduced after 1929.

## **2.The methodology of accounting research regarding the accounting and taxation of income and the results of the economical entities**

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<sup>547</sup> Rusu D., Fra Luca di Borgo și doctrinele contabilității în cultura economică românească, Edition Junimea, Iași, 1991, pg.92.

<sup>548</sup> Ionaşcu I., Epistemologia contabilității, Edition Economică, Bucureşti, 1997, pg.176.

<sup>549</sup> Demetrescu C. G., Istoria contabilității, Edition Ştiinţifică, Bucureşti, 1972, pg.289.

From an utility point of view, the accounting result is at the boundary of two disciplines: accountancy and taxation and it serves the interests of a large diversity of users, among the most important are the investors and the state institutions. There is a great level of difficulty in setting up the right balance between the two categories mainly because the accounting and fiscal regulations are continuously changing.

In order that a capital market should evolve in a close connection with the economy, a dimension of the factors is to be determined, in this case we refer to the profit level that will reflect objectively the result of the activity of the enterprise from the point of view of the potential investors' interest, without neglecting its utility for the taxing necessities of the state.

These details imply the necessity of a disconnection tendency between accountancy and taxation, which will be a change for the Romanian accounting system that will be achieved in time, at least from a practical point of view.

From this point of view we intended to emphasise some risks that appear at this level, from the perspective of:

**-creative accountancy** (an expression of the disconnection between accountancy and taxation). The risks consist in some less ethical tendencies of artificially oversizing and undersizing the accounting and the tax profit according to certain objectives. It was considered that these risks can be controlled through a better activity of accounting regulation;

**-taxation** (an expression of connecting accountancy to taxation). The risks consist of some tendencies of artificial diminishing of the accounting and tax profit in order to achieve a tax economy towards the state institutions. This phenomenon is against potential investors' interest that do not have the possibility of seeing the efficiency of the activity of an enterprise to its real dimension. The risks can be diminished through extraccounting determining of the size of the profit tax on the basis of the taxable profit determined on the taxing principles and regulations, with minimal influences on accountancy. We consider that regardless of the size of the profit tax due at the end of the financial period (superior or inferior), the accounting profit has to reflect the economical reality so that the investors can get some correct information.

**-inflationary phenomenon** which shows, even in the case of a reduced rate of inflation, the risk of calculating and paying the tax on some artificial fiscal profit with serious consequences for the enterprise decapitalization when the tax and dividends are paid.

### **3. Results and discussions**

#### ***3.1. The historical fracture concept applied to the Romanian accountancy evolution***

After the Second World War Romania did not continued its existence starting from what it used to be, but it entered the sovietical influence area. In this context, "the new political ideology that marked Romania's development, requires the utilization of the historical rupture concept in the evolution of Romanian accountancy"<sup>550</sup>.

Under these circumstances the accounting norming in Romania becomes the state's exclusive mark starting with 1947, when it was created, within the Minister of Industry and Commerce, a Permanent Council of norming the accountancy. This Council had as a priority the elaboration of a general frame of accounts, applicable to all the industrial enterprises.

It may be observed that this event coincide with the elaboration of the French Accounting Plan in 1947.

The period 1950-1990 can be characterized by the evolution of accountancy towards monism, from an informational point of view (the only receiver of the accounting information being the state).

During this period a circuit of ideas expressed globally took place in the accountancy field. But the Romanian accountancy stayed off this circuit.

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<sup>550</sup> Neag R., *Reforma contabilității românești între modelele francez și anglo-saxon*, Edition Economică, București, 2000, pg.202.

After the fallen of the communist regime, the new governmental authorities imposed a number of legislative reforms, meant to contribute to the development of an economy oriented towards a market economy. The new Accountancy Law 82/1991 supports this. This reform implied the transformation of the financial statements, from statements meant to create some statistics used in order to observe the execution of plans at macro economical level, to a complex of financial statements meant to accurately inform some different categories of users.

### ***3.2. The primary orientation of the accounting-taxation ratio in Romania***

During this post revolutionary period Romania had to choose an accounting system, adapted to the new political, economical and social changes, one of the models presented above. The option for a continental model or an Anglo-Saxon one was revealed through the Accountancy Law 82/1991, which implied a very detailed copy of the French accounting system.

The objective or subjective motifs of this option can be varied:

- the most powerful argument can be noted as being the fact that “it has never been considered that the French accounting system have not been adequate to Romania”<sup>551</sup>;

- the similarity between Romania and France as regarding the existence of a code of laws (statute law);

- due to the fact that Romania was a developing country that was orienting towards the market economy, the predominant way of financing was through creditors, banks, and less through the financial markets. The Romanian exchange market came into being much later;

- because of the informational monism in the communist period, the accounting profession in Romania was only at the beginning, and the influence that this provide in order to protect certain accounting rights was insignificant;

- the Romanian intellectual and political elite was sent to school in France several times;

- the communist regime also had some connections with France, perhaps more than with any other country from Western Europe;

- the influence that was exerted by Belgium and French specialists, who advised the Romanian government when choosing its alternatives regarding the new accounting system (in a similar way as with the present-day influence for adopting the Accounting International Standards);

- the Anglo-Saxon accounting model was not very wide spread in Europe (being characteristic only to the United Kingdom, The Netherlands and Ireland).

Consequently, one of the elements that were adopted together with the entire French accounting system was also the strong connection between accountancy and taxation. As a conclusion, taking into account the characteristics of the Romanian accounting system, influenced by taxation, it is nowadays defined by:

- the predominance of the banking sector for financing as a disadvantage for the financial markets;

- the prevalence of the statute law as a disadvantage for unwritten law;

- the law provides detailed accounting rules, and they are not being elaborated by independent and legitimate organisms;

- the accounting profession in Romania is insufficiently developed (The Corp of Auditors and Authorized Accountants came into being only in 1994);

- the main users would be the following, taken in order: fiscal authorities, creditors, and last, the investors;

- users' role in the process of elaborating the accounting regulations is insignificant;

- the predominance of the caution principle;

- the tendency of some limited publications of accounting reports;

- a large number of evaluation and accounting options;

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<sup>551</sup> Roberts A., The recent romanian accounting reforms: another case of cultural intrusion?, Edition Economică, București, 2000, pg.36.

- the estimation of a benefit more cautious than useful;
- tendencies in creating some funds from the dispensable profit.

### **3.3.Perspectives regarding the accounting-taxation ratio**

Regarding the perspectives for the accounting-taxation ratio in Romania, it was mentioned that they are according to the international tendencies regarding the disconnection. Taking into account some of the recent evolutions (adopting the IV Directive of the European Economic Communities) we can say that the seeds that lead (at least theoretically in the beginning) to the possibility of gradually opening the road towards an efficient accounting system, where accountancy and taxation work independently from one another, exist. This tendency becomes more certain if we take into consideration Romanian's perspectives to join the European Union. This event implies also joining the official position of the Union, regarding the acknowledgement and utilization of the international accounting norms, and at the same time the disconnection between accountancy and taxation.

The perspectives of the disconnection related to joining the European Union are promoted by the importance of a favorable regular report that depends on the taxation level, such as<sup>552</sup>:



The conclusion is that a disconnection ratio between accountancy and taxation would be associated with a low level of taxation. The consequence is the decreasing of the country risk and at the same time a favourable Regular Report on Romania.

As regarding the actual typology of the accounting-taxation ratio in Romania (connection) we consider that accounting information influenced by taxation is not very credible as regarding the possibility to ensure the faithful image and also the essential objective of accountancy.

Contextually the questions that can arise are: Wouldn't an independency ratio between the two sciences be more appropriate? Is the idea of the accounting principles being influenced by the fiscal principle or the other way around justified, taking into account the fact that their essential objectives: the faithful image and the maximization of budgetary income can be affected? To what extent would accountancy and taxation carry out their objectives, independently from one another?

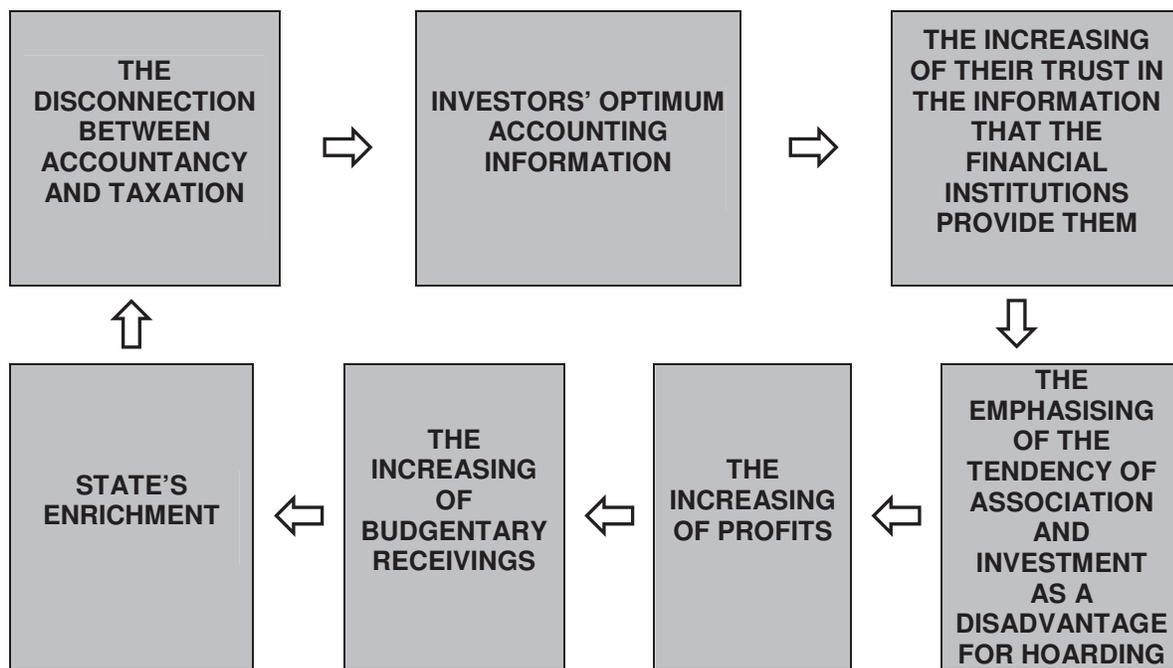
And, finally, what is our opinion? Do we choose connection or disconnection?

We believe that the objectives of both sciences can be achieved, their principles being respected, but we cannot forget the fact that the information source for both of them is accountancy. Therefore the idea of total disconnection between accountancy and taxation is not completely achievable. But we can refer to an interaction relation between accountancy and taxation.

The beneficiaries of the disconnection between accountancy and taxation would be first of all the investors and, second, the state itself. This hypothesis is provided by the following causality relation described in the next diagram:

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<sup>552</sup> Berinde, Sorin R., "Perspectives regarding the taxation system in Romania", StudiaUniversitatis Babes Bolyai – Negotia, no. 3, 2009.



Therefore the disconnection between accountancy and taxation creates the premises for a better apprising of the investors. The consequence of them disposing of real accounting information would be the increasing of their trust in the information provided by the financial statements and the investment, as a disadvantage for saving. The increasing of the profits is assimilated to the increasing of investments and at the same time to the increasing of the budgetary receivings that refer generally to taxes and especially to profit tax, this thing leading to the state's enrichment.

#### 4. Conclusions - The limits of disconnection between accountancy and taxation

The perspectives of disconnection between accountancy and taxation reveal some disadvantages. Contextually the risks that the creative accountancy represents for an accountancy disconnected from taxation, were mentioned, they being materialized in some technics that have as a result:

- the real financial administration of the accounting result (increasing it);
- the increasing of its own capitals;
- the reducing of the debt rate.

The premises of using the accounting creativity technics in the disconnected accounting systems are ensured by:

- the determination of managers' salaries taking into account the dimension of the accounting result. The consequences would be the adopting of the creative tricks that would lead to the increasing of the accounting result in order to increase their own benefits. On the other hand there is a tendency of increasing the losses for crisis periods in order to better emphasize the next possible profits;
- the high level of interpretability and inconsistency of laws;
- the pressure of certain users categories (especially investors);
- the evaluation of the imaterial investments is sometimes difficult.

The creative account technics with direct impact on the dimension of the accounting result are:

- the lease-back operations;
- selling-rebuying the investments titles;
- circular tranzactions with high price stocks;
- production assets without real utilization.

To conclude the matters discussed we can say that the accounting result can be influenced in the case of a taxation connected ratio (decreasing it). On the other hand, the accounting result is subject to an increasing risk due to the creative accountancy. Under these circumstances, a question arises: Which risk is better to be assumed taking into account the dimension of the accounting result? We believe that the accounting result should keep an equal distance towards the risk of taxation decreasing and the risk of accounting creativity increasing. True information would be provided this way both for the investors and the state's institutions.

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