

THE ADJUSTMENT OF THE DEDUCTIBLE V.A.T. IN THE CASE OF CAPITAL ASSETS

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Abstract: Tax payers have to adjust the tax deducted for detained capital assets, or for assets purchased, constructed, transformed or modernized beginning with the 1st of January, 2007. Since the conditions existent at the date of exertion of the right to deduction is being modified from various reasons (change of the destination of the assets' use, changes of the elements used at calculating the initially deducted tax, cessation of the asset's existence and so on), the adjustment of the initially deducted tax has emerged as a necessity. Adjustment measures are applied to the deducted tax and to the operations exempted regarding the lease, the rental and the leasing of fixed assets, as well as to the delivery of a construction, of a part of the construction or to the land on which it is built, as well as to any other land.

1. General aspects

Capital assets represent all tangible fixed assets, as well as operations such as the construction, transformation or modernization of tangible fixed assets. Tangible fixed assets represent any asset owned in order to be used in the production or delivery of assets or in the carrying out of services, in order to be rented to third parties or for administrative aims, if this asset has a normal use period longer than a year and a value greater than the limit foreseen by Government's decision or by legal provisions concerning the value added tax from the Fiscal Code.

There are not included in the category of capital assets the following elements: reparations or works of maintenance of the assets, even in the circumstances in which these operations are realized by the beneficiary of an agreement of lease, rental or any other agreement by which the tangible fixed assets are put at the disposal of another person. Packaging which can be used several times are also not considered as capital assets.

The assets that are the object of leasing, rental or of any other method of putting them at the disposal of a person are considered capital assets pertaining to the person who rents, lease them or puts them at the disposal of another person. In this case, the adjustment of the deductible tax is done by the owner of the assets.

The moment when the good is considered purchased by the user, from the point of view of the value added tax, is the moment when the right of property is transferred by the financier to the user. For the tax due on capital assets acquired by a leasing contract, the period of adjustment begins on January the first of the year in which the right of property on assets takes place, but the adjustment is applied to entire deductible tax corresponding to capital assets, including the tax paid or due before the transfer of the rights of property took place.

The deductible tax afferent to capital assets represent the acquitted or due tax, afferent to any operation linked to the acquisition, fabrication, construction,

transformation or modernization of these assets. It does not enter into the category of deductible tax afferent to capital assets the paid or due tax afferent to the reparation or maintenance of these assets or the tax afferent to the acquisition of spare parts destined to the reparation or maintenance of capital assets. The deductible tax represents the deducted tax on the basis of Vat invoices delivered by suppliers, respectively the tax the beneficiary emphasizes in the VAT deduction both as deductible tax as well as collected tax for the assets for which the simplification measures and reverse taxation are applied.

The deductible tax afferent to capital assets is adjusted *in the circumstances in which the rules regarding self-delivery or self-services are not applied*.

Self-delivery is an operation assimilated to the delivery of assets made with payment, defined such as follows:

-the taking over by a tax payer of purchased mobile assets or of produced by these in order to be used in purposes which are not linked to the unfolded economic activity, if the tax afferent to the assets in question or of their component parts has been entirely or partially deducted, or

-the taking over by a tax payer of purchased mobile assets or of produced by these in order to be put at the disposal of other persons for free, if the tax afferent to the assets in question or of their component parts has been entirely or partially deducted.

Self-services is an operation assimilated to carrying out paid services, defined such as follows:

-the temporary use of assets which are part of the assets of a tax payer, in purposes that are not linked to his economic activity or in order to be put at the disposal of other persons, with a view to their use for free, if the tax for the assets in question has been entirely or partially deducted;

-the services that are included in the economic activity of the tax payer, carried out for free for the personal use of its employees or for the use of other persons.

2. The adjustment period

Depending on the nature of the capital asset, its adjustment is done:

-on a *20-year period* for the construction or for the acquisition of a *fixed asset*, as well as for the transformation or modernization of a fixed asset, if the value of each transformation or modernization is of at least 20% of the total value of the fixed asset which has been thus transformed or modernized;

-on a *5-year period* for *other capital assets* purchased or produced;

The adjustment period begins with:

-for *the fixed capital assets that are constructed for a tax payer*-starting with the 1st of January of the year when the assets are used for the first time, if the year of the first use is the year of Romania's integration into the EU or another year previous to integration; the adjustment is applied to the whole amount of the deductible tax afferent to the capital asset, inclusively for the paid or due tax before the date of the adhesion;

-for *fixed capital assets purchased in 2007 or during a year after the adhesion*-from the 1st of January of the year when the assets were acquired; the adjustment is applied for the whole amount of the deductible tax afferent to the capital asset, inclusively for the paid or due tax before the adhesion date;

-for *fixed assets transformed or modernized*-starting with the 1st of January of the year when the assets are used for the first time after transformation or modernization; if each transformation or modernization has a value of at least 20% of the total value of the fixed asset which has been thus transformed or modernized, and the year of the first

use after transformation or modernization is the year of the adhesion or a year following the adhesion, the adjustment is done for the sum of the deductible tax afferent to transformation or modernization, inclusively for the sum of the deductible tax paid or due before the adhesion date;

-for *other capital assets acquired or produced at the date of the adhesion*-starting with the 1st of January of the year when the assets were acquired or produced.

In the situation in which *works of transformation or modernization are done by the person at the disposal of whom is put the fixed asset or a part of it*, and the value of each transformation or modernization is of at least 20% of the total value after transformation or modernization of the fixed asset or of a part of the fixed asset, the deductible VAT is adjusted by this person. There are taken into consideration the operations of transformation or modernisation that rise the value of the fixed asset. The updated values of the goods will be used, as they are registered in the accounting.

In the situation in which during the adjustment period it expires the agreement by which the fixed asset or a part of it was put at the disposal of another person, the deductible VAT afferent to the operations of transformation or modernization is adjusted only once for the entire period of adjustment that is left, including the year when the change of destination of use occurs, respectively the asset is returned to the owner.

3. Situations in which there must be applied the adjustment of the deductible tax for capital assets

a) The adjustment of the deductible tax for capital assets is applied if the asset is used by the tax payer, entirely or partially, for other purposes than for economic activities, for the realization of operations which do not suppose the right to deduction of the tax or for the realization of operations which allow the right of tax deduction in a different way than the initial deduction.

In these situations, the adjustment is applied during the adjustment period, to a fifth or, according to the case, to a twentieth of the initially deducted tax, for each year when there is a change in the destination of use. By exception, if the capital asset is used entirely to other purposes than economic activities or for the realization of operations which do not allow the right to tax deduction, the adjustment of deduction is done only once for the entire period of adjustment that is left, including the year when the change of destination of use occurs. These provisions were in force in 2007.

Examples:

a.1.) example for the situation in which the capital asset is used for other purposes than for economic activity:

A tax payer bought a building for his economic activity on the 19th of April, 2007 for which there is deducted a sum of 500,000 lei. On the 10th of September, 2008, this person decides to use the building entirely for dwelling. The adjustment period is of 20 years and it begins with the 1st of January, 2007 and ends on 2026, inclusively.

The adjustment must be done for the period which is left (2008-2026) and the person must return 19 twentieths of the VAT initially deducted, respectively $500,000 \times 19/20 = 475,000$ lei.

a.2) Example for the situation in which the capital asset is used for operations which do not allow deduction:

A tax payer acquires a fixed asset in 2007 in order to unfold operations with deduction right and deducts entirely the VAT on the date of acquisition in the amount of 500,000 lei. In 2010 he entirely rents the asset submitted to a regime of VAT exemption.

The adjustment period is of 20 years starting with the 1st of January 2007 till 2026, inclusively.

The adjustment must be done for the period which is left (2010-2026) and the person must return 17 twentieths of the VAT initially deducted, respectively $500,000 \times 17/20 = 425,000$ lei.

a.3) Example for the situation in which the capital asset is used for operations which allow deduction in a different way than the initial deduction:

A tax payer owns a hotel that was bought in 2007 and there was applied a VAT deduction of 6 million lei for the purchase of this fixed asset. In 2010, at the ground floor of this hotel there is built a casino which occupies 30% of the building's surface. The gambling activity being exempted of VAT without deduction right, the person in question must adjust the tax initially deducted, proportionally with the surface occupied by the casino.

The adjustment period is of 20 years beginning with the 1st of January till the end of 2026. For 2007, 2008 and 2009 the tax payer does not adjust the initially deducted tax, afferent to these years, which represents $300,000 \text{ lei} \times 3 \text{ years} = 900,000$ lei.

For the period which is left, 2010-2026 the adjustment is applied annually and it raises to the amount of $300,000 \times 30\% = 90,000$ lei-undeductible tax, which is included in the tax deduction on added value for the last fiscal period of each year.

Starting with the 1st of January, 2008, the adjustment of the deduction for all capital assets, irrespective of their use, is done only once for the entire adjustment period which is left, including the year when the change of the destination of use occurs.

Since in 2007, for capital assets used entirely for other purposes than economic activities or for the realization of operations which do not allow deduction, the adjustment of deduction was done only once for the entire period of adjustment which is left, we can conclude that the new provisions can be applied for assets that have been partially used for other purposes than economic activities or for the realization of operations which gave the right to deduction in a different way than the initial deduction.

If for these goods, during 2007, the adjustment was applied to a fifth or, according to the case, to a twentieth of the deducted tax, in 2008, the tax afferent to the part of the capital asset used for operations which do not allow deduction, respectively the difference left of 4/5 or 19/20 will be adjusted only once.

Example:

A tax payer acquired in February 2007 a building for which there was applied a Vat deduction of 6,000,000 lei. In September 2007, the person in question rents 30% of the surface of the fixed asset submitted to an exemption regime. In September 2007, the tax payer applied the following adjustment:

$6,000,000 \text{ lei} / 20 \text{ years} = 300,000 \text{ lei/year}$; the tax to be adjusted afferent to 2007 due to the change of destination of use of the asset: $300,000 \text{ lei} \times 30\% = 90,000$ lei which must be registered with the sign minus in the Vat deduction afferent to the last period of report for the year 2007. In 2008, the tax payer must apply the adjustment for 19/20 of the tax afferent to the building used for operations which do not entitle to deduction, respectively $90,000 \text{ lei} \times 19 \text{ years} = 1,710,000$ lei.

If starting from the 1st of January, 2008 and till the end of 2026 the surface of the rented fixed asset submitted to exemption regime, each time there will be applied the adjustment of the tax only once in the deduction of the month when the change appears.

b) In the cases in which **there occur changes of elements used for calculating the deducted tax**, the adjustment is applied within the framework of the adjustment period, for a fifth or for a twentieth of the initially deducted tax for each year during which changes to the elements of the deducted tax occur.

Example:

A tax payer subject to mixed regime bought an equipment during August 2007 in the amount of 40,000 lei, plus 19% VAT, that is 7,600 lei. The provisional pro-rate applied in 2007 was of 30%, and the deducted tax was of 2,280 lei ($7,600 \times 30\%$). The final pro-rate calculated at the end of 2007 is of 25%.

At the end of 2007 the tax adjustment is done on the basis of the final pro-rate, respectively $7,600 \times 25\% = 1,900$ lei tax to be deducted, which is compared to the deducted tax on the basis of the provisional pro-rate (2,280), and the difference of 380 is registered in the deduction for the month of December as undeductible tax. This adjustment of the deduction refers to the entire sum initially deducted in a provisional manner and, consequently, also covers the adjustment afferent to the first fifth for the capital assets.

The adjustment for 2008, 2009, 2010 and 2011 is done such as follows:

The deductible VAT of 7,600 lei is divided by 5 years (the adjustment period), resulting 1,520 lei.

The actual VAT deducted on the basis of the final pro-rate for the first period is divided in its turn by 5, resulting 380 lei.

The annual deductible tax of 1,520 lei is multiplied by the final pro-rate for each of the following periods and it is compared to 380. The resulted difference will constitute the adjustment of deduction either in favor of the state, or of the tax payer.

Any change of the pro-rate in the next years, respectively after the end of the last adjustment year (2011) will not influence anymore the deductions applied for this equipment, except for self-deliveries for which there is no time limit.

c) In the case of **delivery of assets or of any other operation for which the tax must be collected**, the initial tax deducted entirely or partially must be adjusted. The supplementary tax to be deducted is limited to the value is limited to the value of the tax collected for the delivery of the asset or for any other operation. The adjustment of the deductible tax is applied only once for the entire period of adjustment left, including the year within the framework of the adjustment period left, including the year during which appears the obligation of adjustment, and it is of at most one fifth or, according to the case, one twentieth per year, of the value of the undeducted tax till the moment of adjustment.

Example:

A tax payer bought an equipment on the 1st of April, 2007 of 30,000 lei +VAT (19%=5,700), which he used for his economic activity (40%) and for personal purpose (60%). Consequently, he deduces only 2,280 lei. On the 25th of August 2008 he sells the equipment for the sum of 25,000 lei +VAT (19%=4,750 lei).

In this case, it is theoretically an adjustment of the deduction in favor of the tax payer, of four fifths of 3,420 lei (VAT initially undeducted), that is 2,736 lei.

d) In the situation in which the **capital asset ceases its existence** as a consequence of cassation before the expiration of the normal duration of functioning or after the expiration of the normal duration of functioning, but during the adjustment period, the adjustment of the deductible tax is done only once for the entire period of adjustment left, including the year during which the obligation of adjustment appears, and it is of at

most one fifth or, according to the case, of one twentieth per year, of the value of the initially deducted tax.

Examples:

On the 30th of November, 2007, a tax payer buys a fixed means worth 10,000 lei +VAT (19%=1,900) and deduces 1,900 lei. The normal duration of functioning is of 5 years. On the 8th of December 2009, the fixed means is subject to cassation. In this case, there is an adjustment in favor of the state, worth two fifths of 1,900 lei, respectively 760 lei.

If the capital asset is submitted to cassation after the expiration of the duration of functioning of 5 years, the adjustment is not applied anymore.

In the case of destruction of the capital assets as a consequence of natural calamities or other force majeure cases, the adjustment of the tax is not performed anymore.

e) If the supplier has already adjusted the taxation basis for capital assets for which there was issued an invoice and afterwards the operation is cancelled entirely or partially before the delivery of assets, in the case of total or partial refuse regarding the quantity, the quality or the prices of delivered assets, or in the case in which rebates, commissions, risturns and other price reductions were granted after the delivery of assets, the beneficiary adjusts the taxation basis on the basis of the invoice issued by the supplier.

4. Obligations on behalf of tax payers

The tax payer must keep a *report* of capital assets which are subject to deductible tax, which allow the control of the deductible tax and of performed adjustments. This situation must be maintained for a period which starts the moment when the tax afferent to the acquisition of the capital asset becomes eligible and ends five years after the expiration of the period in which the adjustment of deduction can be required. Any other registrations, documents and journals regarding the capital assets must be kept for the same period.

The adjustment of the deductible tax afferent to capital assets, in the situation in which it would result as a consequence of adjustment is less than 1,000 lei.

With a view to the adjustment of the deductible tax afferent to capital assets, the tax payers are obliged to keep a Registry of capital assets, in which they must emphasize and focus on, for each capital asset, the following pieces of information:

- a) the date of acquisition, fabrication, construction or transformation/modernization;
- b) the value (taxation basis) of the capital asset;
- c) the deductible tax afferent to the capital asset;
- d) the deducted tax;
- e) the applied adjustments.

5. Conclusion

Of all presented above, we can conclude that for fixed assets constructed, acquired, transformed or modernized after the integration date, the adjustment must be done by all the tax payers who have the right to entire or partial deduction of the afferent tax only if the asset is used by the tax payer in question, entirely or partially, for other purposes than economic activities, for the realization of operations which do not allow a tax deduction or for the realization of operations which allow the tax deduction in a different manner than the initial deduction.

The difference between adjustments which is applied for these fixed assets and the adjustments applied for fixed assets constructed, acquired, transformed or modernized before the integration date is that for the latter, the adjustment is applied only if the assets are used for/or after the integration date in operations which are tax exempted (the lease, rental or leasing of fixed assets, the delivery of a construction, of a part of it or of the land on which it is built, as well as of any other piece of land).

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