

ACCOUNTING AND FISCAL ASPECTS RELATED TO CONSTRUCTIONS AND LAND

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***Abstract.** This paper approaches aspects related to the value added tax in the case of operations with real property. The presentation of the theoretical notions and the applications are grouped on types of operations: exempt from VAT; voluntarily liable to pay VAT, and liable to pay VAT under the law. The analysed taxpayers were mainly legal entities that carry out business subject to VAT. A small percentage is represented by information related to non-taxable natural persons trading in real property.*

Keywords: VAT, constructions, land, delivery, rental, property unit.

JEL Classification Codes: M41, K34.

1. CONTEXT OF THE APPROACHED TOPICS

The economic progress and the approach of modern life generate complex problems the resolution of which needs solid tax and accounting law knowledge.

Before the year 2008, there was no express accounting regulation on the demolition of a partially amortized construction located on a site where a new building was to be erected. At that time, a notion occurred according to which the non-amortized value of the demolished building should be turned into the book value of the new building. The reason was that the company should not decrease its profit. Meanwhile, the accounting legislation in Romania took into account the case of demolished buildings, the resolution of which will be approached in this paper.

In relation to the application of the legal provisions on VAT, difficulties were faced in the case of constructions and land delivered exempt of VAT. The application of the VAT exemption regime can only be made simultaneously with the compliance with the provisions concerning the adjustment of the tax on capital goods. If following the adjustment, a negative value of the deducted tax is obtained, the taxpayer owes VAT.

In the first transactions with land and buildings, carried out after Romania's adhesion to the EU, in the according of Romanian companies, tax legislation interpretation errors were found. In certain cases, constructions exempt from VAT were delivered and the provisions concerning the adjustment of the tax for capital goods were not applied. Tax inspectors established the VAT to be paid to the state budget and the ancillary delay payments.

Another case that generated delicate situations was represented by transactions on land and buildings carried out by non-taxable natural persons. The frequently asked question has the purpose to clarify whether a natural persons may become a taxable person and implicitly become liable to pay VAT for the transactions of land and buildings.



2. FISCAL AND ACCOUNTING REGIME

If a building is demolished so that another one may be built, the demolition expenses are recognised according to their nature, with taking into account the site fit out costs. The same accounting treatment is applied to costs representing the non-amortized value of the demolished building or the cost of the respective asset, where such asset is highlighted as stock. Source: Order of the Minister of Public Finance no. 1802/2014, ITEM 226 (4)

Example: Building with a book value of 100,000 lei, 80% amortized, the building is demolished. A new building will be erected on the same site. In this case, the non-amortized value is $100,000 \times 20\% = 20,000$ lei.

Table no. 1 Highlighting the building

Income statement			
%	=	212	100,000
2812			80,000
6583			20,000
Verified by	Prepared by		

Key: 212 Buildings; 2812 Amortization of buildings; 6583 Net value of assets disposed and other capital transactions.

Observation: In the version supported before the year 2008, entities interested in not diminishing the profit of the accounting year, the value still not amortized would be reflected by replacing account 6583 “Net value of assets disposed and other capital transactions” by account 231 “Tangible assets in progress”. This situation would lead to the overestimation of the new asset and the non-compliance with the prudence principle.

The second category of problems is related to VAT in the case of deliveries of land and buildings. For clarification purposes, we will present the classification of land and buildings.

Table no. 2 Classification of deliveries of land and buildings

Deliveries of land and buildings	1) Exempt from VAT	By applying the provisions concerning VAT adjustment for capital goods
	2) Taxable	2a) Voluntarily taxable
		2 b) Taxable under the law

According to art. 292 para (2) letter f) of the Fiscal Code, the delivery of buildings/parts of buildings and of the land they are built on, as well as any other land is included in transactions exempt from VAT. As an exception, the exemption is not applicable to the delivery of new buildings, parts of new buildings or building land.

Observation: deliveries of new buildings and building land are not exempt from VAT.

According to the legal definition: “*the delivery of a new building or of part thereof*” means the delivery performed no later than on 31st December of the year following the one of the first

occupation or use of the building or part thereof, as the case may be, following the transformation” Source Art. 292 para 2) letter f) of the Fiscal Code.

Example: A building was purchased in 2012, the date of its first occupation is 10/04/2012. The building was sold on 10/01/2014. Due to the fact that the delivery date is after the day of 31/12/2013, it is considered that the sale object is no longer a new building. If the delivery had been made by the day of 31/12/2013, the sale object would have been a new building.

The Fiscal Code further includes revamping or renovation works into the category of new constructions if the value of these transformations without VAT amounts to at least 50% of the value of the building or of the part of the building after the transformation.

From the aforementioned provisions it results that the delivery of building land is not included into the category of transactions exempt from VAT. On the other hand, the delivery of old buildings and the related land is exempt from VAT.

When a single property unit is delivered which is composed of a building and the land on which it is erected, identified by a single cadastral number, the fiscal regime concerning VAT is applied depending on the rules provided by the methodological norms for the application of the Fiscal Code. The synthesis of these rules is shown in the table below:

Table no. 3 The fiscal regime concerning the delivery of a property unit

It. no.	Explanations	VAT fiscal regime
1	The value of the land on which the building is erected (V_t) is lower than the value of the building (V_e)	$V_t < V_e \Rightarrow$ the land on which the building is erected observes the building regime
2	The value of the building (V_e) is lower than the value of the land (V_t)	$V_e < V_t \Rightarrow$ the building will observe the regime of the land on which it is erected
3	When the land and the building have equal values	$V_e = V_t$ depending on the real property with the biggest surface. The building footprint of the construction will be taken into account.

Key: V_e -Value of the building; V_t -Value of the land

Observation: According to the Methodological Norms for the application of the Fiscal Code, the value of the land and the value of the building result from the expert's/valuation report.

In relation to the VAT adjustment, in the case of capital goods, it is necessary to mention the in the specialized literature, land and buildings are also named real property. Real property is also included in the category of capital goods.

For deliveries of real property exempt from VAT, found in the adjustment period, the initially deducted VAT is decreased. According to the provisions of Art. 305 of the Fiscal Code, the adjustment period is of 20 years for real property.

Example: A taxable person bought a building for its business on 20 August 2012 and deducted VAT in the amount of VAT 200,000 RON at the time of the purchase. In May 2019, this person decided to deliver the building exempt from VAT. The adjustment period is of 20 years starting from 1st January 2012 and until and including 2031. The adjustment must be made for the entire tax corresponding to the period remaining from the adjustment period, more specifically 13 years, and the person in question must repay 13/20 of the initially deducted VAT: 2,000,000 RON/ 20 x 13 = a negative adjustment of 130,000 RON).

Table no. 4 – VAT adjustment

Income statement -lei-			
635	=	4426	130.000
Verified by		Prepared by	

Key: 635 „Other taxes, duties and similar expenses”; 4426 “Input VAT”.

The accounting record in Table no. 4 leads to the increase in the VAT to be paid in the fiscal period corresponding to the date when the building was delivered,

According to the provisions of Art. 292 para. (2) letter e) of the Fiscal Code, the real property rental and real estate leasing are also transactions exempt from VAT.

In cases where a building was purchased with the purpose to be used for business purposes with 100% deductible VAT, and was subsequently rented under the regime of exemption from VAT, the landlord must adjust the initially deducted VAT.

Example: A taxable persons registered for VAT purposes purchased a building in 2015 in order to carry out transactions for which he has the right to deduct the entire value added tax on the day of the purchase, in the amount of 150,000 lei. In 2020 he rents 25% of the building surface under the regime of exemption from value added tax. The adjustment period is 20 years, beginning from 1st January 2015 and until and including 2034. The adjustment must be made for the entire period corresponding to the period remaining from the adjustment period, more specifically 15 years. Consequently, the person in question must repay: $150,000 \times 15 / 20 \times 25\% = 28,125$ RON.

The delivery and lease of real property can be voluntarily taxable transactions, if the landlord submits a notice to the competent fiscal body. Within taxable deliveries, by applying the legal VAT rate, we discover a new classification: a) voluntarily liable and v) liable under the law.

The deliveries liable under the law include the delivery of building land and new buildings.

The Fiscal Code provides in Art. 331 that, for 100,000 RON, the legal VAT rate being 19%.

Table. no. 5 will show the accounting records in two versions: a) the customer is a legal entity registered for VAT purposes and simplification measures are applied; b) the customer is a legal entity not registered for VAT purposes, the supplier delivers under the normal taxation regime.

Table no.5- Accounting records concerning the delivery with reverse taxation and under normal taxation regime

In the seller's accounting		-RON-		RON-	
Version 1: with reverse taxation:					
461	=	7583	100,000	212	= 404 100,000

				4426	=	4427	19,000
Version 2: Under normal taxation regime							
461	=	%	119,000	212	=	404	119,000
		7583	100,000				
		4427	19,000				

Key: 461 “Sundry debtors”; 7583 “Proceeds from the disposal of assets and other capital transactions”; 212 “Buildings”; 404 “Suppliers of non- assets; 4426 “Input VAT”; 4427 “Output VAT”.

Observations: In the customer's accounting, when simplification measures are applied, the record <<4426=4427>> is the equivalent of the exercise of the right to deduct VAT. Goods purchased by applying reversed taxation observe the fiscal regime of goods for which VAT was deducted. If the customer is not registered for VAT purposes, the tax mentioned on the purchasing invoice is not recoverable and it is included in the purchase price.

A natural persons who earns income from real property transactions, in certain cases, may become a taxable person registered for VAT purposes. Natural persons are not considered taxable persons if they earn income from the sale of their own buildings and land, in which they lived or which they used for personal purposes.

If a natural person purchases real property for sale, the delivery of such goods is a taxable delivery if more than one transaction is carried out during one calendar year. The first delivery is not taxable, but it is taken into account in the calculation of the ceiling provided in art. 310 of the Fiscal Code. The current VAT exemption threshold is 300,000 RON.

3. CONCLUSIONS

Real property transactions have significant values with considerable impact in the financial and fiscal management of the taxpayer. We draw the attention to the correct classification of the delivery of property unit comprising a building and the related land, into transactions exempt from VAT.

We want to remind that, if the goods in question are in the 20-year adjustment period, the initially deducted VAT will be adjusted. Following the adjustment, the liability to the state budget will increase.

We also need to highlight that the delivery of land without building implies the appropriate inclusion into one of the following two categories: building land and land not used for building purposes.

In compliance with the legal provisions, in the transactions with real property, two taxable transactions were delimited: voluntarily liable transactions, and transactions liable under the law.

The recommendation would be for the landlord of real property to choose the taxation of the delivery, real estate leasing and real property rental. Thus, complex calculations would be avoided and an increased attention would be paid to the VAT adjustment.

As a result of the significant values related to the deductible VAT, the Fiscal Code established simplification measures, which implies reverse taxation, avoiding the actual deduction of the VAT for purchases. These measures are meant to decrease the huge amounts representing recoverable VAT that would be recorded by the buyers of real property.

We should not ignore the cases where natural persons who sell real property may become taxable persons, if they carry out more than one transaction per calendar year. If they exceed the Vat exemption threshold, taxable natural persons have the obligation to register themselves for VAT purposes.

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