



THE TAX IMPLICATIONS ON THE ECONOMIC ACTIVITY CONDUCTED IN PUBLIC INSTITUTIONS IN ROMANIA

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Abstract

Public institutions are entities through which the State conducts its activity, as regulated by Law 500/2002 on public finances. Like any other operating entity, the public institution acts through a budget, comprised of public revenues and expenditures. A particular case that I will address in this paper is that of the economic activity conducted in public institutions and the taxation-related aspects of this area of activity. I will also include here a structure of the revenues and expenditures of this area of activity and the way taxes and duties are determined.

Keyword: economic activity, accounting, public institutions, value added tax, corporate tax.

JEL Classification: M11, M40, M41

I. Introduction

The areas of activity covered by the budgetary system include: education, health, culture, justice, defense, public authority, social work, activities of strategic interest, transport and telecommunications, environmental protection, etc. All these areas of activity operate through public institutions (the credit release authorities who have competences and responsibilities in the preparation and appropriation of the budget and the way in which the assets of the institution are managed). These are managed by credit release authorities [1] that have specific financial and accounting responsibilities (Hlaciuc et al., 2017).

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Public institutions can receive both internal funding, from the authorising officer in charge of credit releases, as well as external funding, from foreign institutions (Ortega et al., 2008). External funding may also be of two types: reimbursable funding; non-reimbursable funding. At the same time, public institutions may be assigned budget appropriations according to the approved income and expenditure budget, appropriations assigned by the authorising officer, or they may use their own revenues, i.e. they do not receive funding from the institution to which they are subordinated (Hlaciuc et al., 2017). Public institutions may also receive donations or sponsorships from individuals, legal entities, associations, foundations or other categories of people (Manea, 2013). Table 1 summarises these categories of funding.

Table 1- Categories of funding

Internal funding	External fundig	Own funding	Other funding
State budget	External credits	Own revenues	Donations
Local budget	Non-reimbursable funds		Sponsorships
Special fund			Volunteering

Source: own interpretation

Taxes, duties and other state revenues, as well as the quotas and standards for expenditures for public institutions must be approved by law (Law 500/2002).

The category of own revenues includes:

- rents obtained from leasing property and premises,
- cultural and sporting events,
- artistic competitions,
- publications,
- editorial services,
- research studies and research activities,
- projects,
- sales of products originating from own or related activities
- provision of services.



Out of these categories of own revenues, a part thereof is used as public authority, and others are aimed at transferring ownership. The latter are included in the area of economic activity. Under the laws in force in Romania, more precisely under the tax regulations (Law 227/2015), such activities are subject to taxation.

II. The public institution as a taxable person

II.1. Registration for VAT purposes

In order for the public entity to acquire the status of taxable person, it must be registered for VAT purposes and as taxpayer. In order to determine whether the activity of a public institution is economic in nature or not, we must first analyse its definition. What does 'economic activity' consist of?

The tax code gives the following definition:

The economic activity is defined as 'the economic process that reflects people's actions, acts, behaviours, and decisions that result in attracting and using resources to manufacture goods and provide services to meet economic interests' (Law 227/2015). Another definition of the concept of economic activity is given by the financial and taxation regulations, according to which 'the economic activity is represented by the facts and actions related to attracting and using economic resources for the production, distribution, circulation, and consumption of goods or services, depending on needs and interest, in order to obtain profit' (www.infoinstitutii.ro). Economic activities can also be defined as 'the entirety of human actions aimed at obtaining material goods and services of any kind, needed to meet normal life needs, provided that resources are limited' (Stancu & Şerban, 2009). Thus, it is possible to determine what are the economic activities conducted by public entities.

First of all, we should consider what activities are not included in the area of public activity. Then, we should analyse whether such activity is aimed at making a profit. Last but not least, if the good or service in question is subject to disposal.

Below are listed a few examples:

- Research activity conducted within an educational institution, whose results (i.e. of the research) are 'sold' (disposed of).
- The activity conducted by a café located on the premises of a city hall
- The rental of own premises or goods

As such, in this 'special case' - i.e. given the economic activity conducted - the public institution acts as an economic entity and is, consequently, subject to taxation.



We should mention here the corporate tax and the value added tax.

In what concerns registration for VAT purposes, under Romanian law only the entities that exceed a turnover threshold of *RON 300,000* (the equivalent of EUR 88,500, calculated using the exchange rate in force on the date of Romania's accession to the European Union, i.e. EUR 1,00 = RON 3,3817) (Law 72/2018).

Public institutions (meaning, most of the times, city halls and ministries) may be non-taxable persons from a VAT perspective - when they do not conduct any economic activity - or partially taxable persons - when they conduct economic activities subject to VAT in addition to their regular utility-related activities (Law no. 207/2015).

The situations in which a public institution conducts economic activities are extremely varied, some of which are mentioned in the Tax Code, art. 127, paragraph 6 (Law 227/2015).

The basic principle states that public institutions must be subject to the same VAT treatment as other ordinary economic operators, in order to avoid competition distortions. In other words, avoiding creating disadvantages for private economic agents is desirable, given the fact that they are forced to practice higher prices as a result of VAT, while public operators charge VAT-free prices for the same type of goods or services.

The procedure used for the registration of public institutions for VAT purposes is similar to that used for the registration of companies established in Romania. However, in the case of public institutions, the VAT code issued is different from the tax number. The public institution requesting to be registered for VAT purposes will be issued a registration code for VAT purposes only for the part of the structure or of the activity that is a taxable person, while a different tax number is assigned for the activities for which the institution is not a taxable person. The VAT obtained may also be used, where appropriate, for intra-Community transactions, as a result of its activation in the Register of Intra-Community Operators.

Another issue is the accuracy of the identification information contained in the procurement contracts entered into by the public institution (Order no. 1917/2015). Concerns might arise in relation to a potential deduction being denied, on the grounds that the contract does not include, for example, the VAT code of the public institution, but the tax number used by the public institution as a non-taxable person. However, this should not invalidate the right to deduct the VAT, and in this respect a correct invoice, containing all the required elements, is of the utmost importance.



II.2. Corporate tax

The corporate tax remains one of the most disputed taxes because it appears to be disadvantageous, as it is a tax that influences the behavior of investors, this is the case for the private environment. In the public institutions, things are somewhat simple.

According to the Romanian tax regulations (Law 207/2015), tax payers obliged to pay corporate income tax are:

- Romanian legal persons, for the taxable profit obtained from any source, both in Romania and abroad. It is part of this group of autonomous administrations, national companies, national societies, commercial companies (irrespective of the legal form of ownership and form of ownership) including those with foreign capital or foreign capital, agricultural companies and other forms of agricultural association with legal personality, cooperative structures, financial and credit institutions, foundations, associations, as well as any entity having the legal status of a Romanian legal person and making a profit;
- Foreign legal and natural persons who carry out activities in Romania as a partner in an association that does not give birth to a legal person, for all revenues resulting from the activity carried out in Romania;
- Associations between Romanian natural persons and Romanian legal persons who do not give birth to a legal person, for the income realized in Romania and abroad. In this case, the due tax is calculated, retained and paid by legal persons;
- Public institutions, for extra-budgetary incomes from economic activities carried out under the law. The revenues of the budgets of public institutions, financed entirely or partially from extrabudgetary income, come from taxes, rents, cultural manifestations, product capitalization from own activities, artistic competitions, publications, impresario, film exploitation, editorial services, medical consultations and services, the provision of services, works and exploitation of goods they have in administration and others of this nature.

As exceptions to tax, we mention:

- state treasury, for the operations of public funds executed through the general treasury account;
- public institutions, for the public funds established according to the Law no. 500/2000 regarding the public finances;
- economic units without juridical personality of organizations of blind, disabled and disabled persons' associations;



- foundational foundations (a legal subject founded by one or more persons, which, on the basis of a legal act for the death cause, constitutes a patrimony permanently and irrevocably affected by the achievement of a general or community interest);
- cooperatives that act as protected units, specially organized according to the law;
- Religious denominations, for income earned from the production and use of objects and products necessary for worship;
- accredited private education institutions, as well as authorized ones, according to the law in certain cases;
- associations of owners, as legal entities, for income from economic activities, which are used to improve the comfort and efficiency of the building, to maintain and repair the common property.

Determining taxable profit

Taxable profit is determined as the difference between the income from the delivery of the movable goods, the rendered services and the executed works, from the sale of the immovable property, including the gains from any source and the expenses incurred for their realization, from a tax year from which the non-taxable incomes are deducted and add non-deductible expenses. From the value obtained, the tax loss still to be recovered from the previous years is also reduced, according to the legal provisions.

How is the corporate income tax calculated in public institutions calculated?

The formula is the same as in the economic entities:

Corporate tax = total income - total expenses recorded under accounting regulations - non-taxable income and tax deductions + non-deductible expenses

Another important aspect is the obligation to calculate the tax and the concession in the fiscal records, which can be both written and electronic.

III. Conclusions

The Romanian legislation is currently harmonised with the European Directive (Tabără, 2006).

Interestingly, over the last few years, some legislative proposals to change the VAT rules in the public sector have being discussed at European level.

The reasons behind these discussions is the failure to observe the principle of neutrality, considering the fact that, when public institutions do not recognise their capacity as a taxable persons, distortions of competition still arise.



Another issue raised at European level on this topic is the lack of clarity concerning the application of VAT exemptions in certain situations.

Following the debates held at European level, several alternative taxation models were suggested for further analysis, such as the full taxation of public interest activities conducted by state institutions.

The Tax Code, by Law 227/2015, requires public entities to observe the provisions on economic activity by registering as taxable persons.

In conclusion, the distinct emphasis in the accounting of the institutions of the economic activities is necessary for the way of determining the tax and the settlement of the value added tax.

Other notes

[1] *The credit release authorities who have competences and responsibilities in the preparation and appropriation of the budget and the way in which the assets of the institution are managed.*

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