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FISCAL ASPECTS OF LOANS BETWEEN COMPANIES

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FISCAL ASPECTS OF LOANS BETWEEN COMPANIES

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Abstract

Most often the recipients of legal rules on loans between commercial companies are penalized by tax inspectors who consider such operations illegal.

At a deeper analysis it is apparent that in some circumstances such an operation is alloweditura Tax legislation - tax code and rules of procedure of their application - make such operations lawful, outlining the legal regime in order to determine the duties and taxes on loans between companies.

Our work will cover only the approach where the creditor company does not include in it's objects of activity the subject of lending and is not authorized to perform these operations on a commercial basis, whereas in the latter case the legality of lending to companies is outside the discussion.

Keywords:

loan, company, loan taxes between companies.

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The question that we want to hear answered is whether - in light of tax law, a company that has the objects of lending and is not authorized to conduct such an activity could borrow another company. We are interested on what will be the answer for the situation in which the two companies are members of the same group[2].

The main argument in support of the prohibition of such operations on the principle of usage specialty is the ability to use the legal person devoted to the article 34 par. 1 of Decree no. 31/1954 on natural and judicial persons[3] that a person can have only those rights which correspond to its goal, set by law, the act of setting or status. Penalty for breach of this occurring is the absolute nullity of the legal act done in contempt of legal prohibition, as expressly provided in paragraph 2 of the same article. Starting from this provision is estimated that as long lending operations are not in the objects of the company as it is indicated in the articles of incorporation means that the legal person is not able to use or to perform such an act . Consequently, the agreements under which a company would borrow another company would be in the outside limits of its ability to use making the loan contract void.

At the opposite pole stand theorists and practitioners, as the minority, who argue the legality of the rule of specialty operations chipping infringement theory by emphasizing the ability to use the confusion to be made between the statutory purpose of the company and its object of activity and the text and arguing interpretation derived from commercial matters, banking and tax.

As for us, not outside critics argued, we advocate the legality of credit transactions between companies in certain circumstances, for both the overall situation and the particular situation in which loan transaction parties are legal persons or members affiliated to the same group.

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[2] According to art.7 alin.1 pct.21 from Chapter III. "Definitions. Definitions of common terms" from the Fiscal Code "affiliated persons" – a person is affiliated with another person if the relationship between them is defined by at last one of the following cases: *a)* a natural person is affiliated with another natural person if these persons are husband/wife or relatives to the third degree. Among affiliates, price at which the transfer of tangible or intangible property or services are rendered is the transfer price; *b)* a natural person is affiliated with a legal person if the individual owns, directly or indirectly, including holdings of affiliated persons, at least 25% of the value / number of shares or voting rights in a legal person or if it controls the actually legal person; *c)* a legal person is affiliated with another legal person if at least: *(i)* first legal person owns, directly or indirectly, including holdings of affiliated persons, at least 25% of the value / number of shares or voting rights or other legal person if he controls the legal person; *(ii)* the second legal entity owns, directly or indirectly, including holdings of affiliated persons, at least 25% of the value / number of shares or voting rights in the first legal person; *(iii)* a third legal person owns, directly or indirectly, including holdings of affiliated persons, at least 25% of the value / number of shares or voting rights in both the first legal entity and as the second"

[3] Decree no. 31/1954 regarding natural and legal persons published inBuletinul Oficial al Romaniei nr.8 din 30.01.1954

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Fiscal Code and Fiscal Procedure Code govern tax aspect on loans between companies. As long as no law prohibits such operations either directly or indirectly, on the contrary, there are provisions contained in the organic law which outlines the legal (tax), means that such operations are legal. It could not shape the legal treatment of a transaction if it is prohibited by law.

Note that the loans granted by a company tax law are addressed from several perspectives.

a. Remunerative interest if the loan is between the companies. A first issue addressed by the tax laws in connection with credit transactions between companies is of interest to establish a loan between two companies.

Under the name "*Special provisions for the appliance of the tax code"* in art**.** 11 alin.1, the Tax Code recognizes that tax authorities have the power to determine the amount of tax or duty to disregard a transaction that has no economic purpose or a form can restore a transaction to reflect the economic substance of the transaction.

Later consecration of that power, the Tax Code and its implementing rules, referring to transactions between affiliated entities or between legal entities, which represent loans indicates loan pricing criteria.

The purpose of regulation is to impose a minimum level of interest should be taken into account both in the intra-group loan contract and the loan of two affiliated companies.

Point 38 of the norms of appliance of article 11 from the Tax Code regulates the situation governing the loan contract between affiliated businesses. The text of the law shows that when a taxpayer makes a loan (credit) to a person affiliated, or when it receives such a loan (credit), regardless of the purpose and destination, the market price[4] for such loan is made up of interest that would have agreed between independent persons and approved by such a loan under comparable conditions, including loan administration fee or borrow fee[5].

We observe, first, that unequivocally establishes the possibility that a company can borrow another company (corporate) affiliateditura Second, the law is establishing the legal provision to be applicable to such a loan interest where the parties have not provided a loan agreement with an interest rate. In other words, the amount of interest established under the provisions of section 38 of the Implementing Rules of the Tax Code will be applicable whenever the

[4] In general terms the market price is determined by comparing to similar uncontrolled transactions. A transaction is uncontrolled if it takes place between independent persons.

[5] Still at pct. 38 from the implementing rules of article 11 of the Tax Code it sais that: "In the case of services of financing between affiliated persons for the allocation of revenues we analise: a) if the given loan is in the interest of the activity of the beneficiary and has been used in this purpose; b) if a scheme of profit sharing existed. The inclusion of the loan in the profit distribution scheme will be supposed if at the date of the loan the repay is nat expected or it the contract has unfavorable clauses for the payer".

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credit transaction parties - companies - have not been sufficiently diligent and did not provide a conventional interest.

It should be made a loan to reflect the interest of the economic content of such operations and, consequently, to be subject to taxation.

With regard to paragraph 2 of art. 11 of the Tax Code that the person in a transaction between non-resident persons and Romanian persons, Romanian tax authorities may adjust the amount of income or expense of any person, as necessary, to reflect the market price of goods or services supplied in the transaction meaning that interest will be established under the provisions of section 38 of the implementing rules - and not as established in the loan contract whenever the interest rate set by the contracting parties will be very small compared with rate prevailing on the market for the same credit operations. In the case of a derisory interest on a loan between corporate affiliates, the tax authorities will not give effect to art. 11 paragraph 1 of the tax code - the general rule - and will not ignore the debt and will not retrain loan of affiliated companies as the other operation. They are required to give effect to the special rule contained in Art. 11 paragraph 2 of the tax code - the situation of affiliated companies - as a loan transaction requires the maintenance and alteration of interest under the provisions of section 38 of Methodological norms for Fiscal Code.

The implementing Rules of the Tax Code, in section 38 indicates the criteria to be taken into account when setting or examining the interest: the amount and duration of the loan, the nature and purpose of the loan, the security involved, the currency involved, the risks of exchange and insurance costs of measures exchange rate and other circumstances to grant the loan. Reporting of loan conditions is considering the interest rates applied in comparable circumstances in the same area by an independent currency and independent persons measures would be taken to divide the exchange risk[6].

Therefore the minimum interest on a loan between corporate affiliates will determine on a case by case basis taking into account the parameters listed above.

In view of economics is that if the loan is granted to companies affiliated to the company's business for support, the crediting company may take zero interest.

In contrast, for companies not affiliated interest can never be zero.

The establishing of a minimum level of interest in the case of loans between two affiliated companies is less restrictive than for companies within the same group. The taxpayer must prove only that provide a level of interest "economic purpose" the transaction is not obliged to respective pct.38 all the criteria in Article 11 of methodological rules listed above. The need however to

[6] For example: clauses that mantain the value of the loan in real terms, a contract term of currencies to pay on the lender's expense.

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ensure that a minimum interest amount to an economic purpose is required by the fact that art. 11 paragraph 1 of the tax code provides that tax authorities otherwise might not consider the transaction (which has no economic purpose) or could retrain loan transaction ("transaction") to reflect the economic substance of the transaction . In this situation will not apply the minimum amount of interest determined under the provisions of section 38 of the implementing rules (which only cover credit if membership portion of the operation - art. 11 paragraph 2 of the Tax Code), but the penalties will occur one enshrined in Article . 11 paragraph 1 of the Tax Code: the removal operation, or its revision.

Section 38 of the Rules are given in the application of art. 11 of the Tax Code in order to quantify a tax: it requires a minimum amount of interest just to be able to determine the appropriate minimum tax. Setting the minimum amount of interest income that the company must obtain *a fortiori* creditor engages and legality of the loan.

b. Another aspect covered by the tax legislation on operations relates to the deductibility of loan interest loans from companies other than those also running credit operations with a professional (and have another procedure on deductibility).

Thus, art. 48 paragraph (5) of the Tax Code shows that "there are limited deductible expenses: .... "k) interest on loans from private individuals and legal persons, other than credit institutions operating in a professional capacity, used in the activity, based on agreement between the parties, interest level within the norms of the National Bank of Romania."

Therefore, regardless of the amount of interest - determined by the parties in the loan agreement or by the application of section 38 of the implementing rules of the Tax Code - it will be deductible only in the interest of reference of the National Bank of Romania.

As shown, the Tax Procedure Code, Tax Code, not only does not prohibit loans between companies but more so, sets out the deductibility of interest paid on loan contracts between companies not engaged in a professional credit . Legislature could not impose a minimum threshold of income earned by a company from another company loan and to cover expenses incurred deductibility in such operations if such a transaction would be unlawful.

c. As regards value added tax (VAT) in relation to interest company loans (which represents income), where the companies are registered for VAT purposes the question is whether the income for the company is obliged to collect VAT or to make any adjustment to tax. Since interest is not charging a delivery of goods or service, consider that the conditions set out in paragraph

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126. (1). a) of the Tax Code[7], so this operation is not taxable regarding value added tax.

Analysis of lending operations of a company by another company in terms of tax legislation revealed the extent permitted depth of our research, that there would be no reason for that could be questioned the legality of a loan as accidental by a company.

In light of the subject we believe that in terms of tax loans between two companies, affiliated or not, are possible and there is a legal basis for not sanctioning the credit company by tax inspectors.

[7] Art. 126 alin.1 from the Tax code has the following content: "In terms of duty are taxed in Romania operations that meet the following conditions: a) the operations that the meaning of Art. 128-130, constitute or be treated as a supply of goods or provision of services in the sphere of duty, made the payment, b) the place of delivery or of performance is considered to be in Romania, in accordance with the provisions Art. 132 and 133, c) the supply of goods or services is made by a taxable person as defined in art.127 par. (1), acting as such; d) the supply of goods or services result from a planned economic activity of the art. 127 paragraph (2)"

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