# FISCAL MANAGEMENT BASED ON KNOWLEDGE - FISCAL IMPLICATIONS OF SOCIAL CAPITAL DECREASE THROUGH THE BUY BACK OF OWN STOCKS

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**Abstract:** *EU integration has imposed upon Romania, modifications and supplement the current internal legislation, the most important are the modifications brought to law 31/1990 regarding commercial companies and those regarding the regulations in fiscal problems. In current practice there are many cases of increasing or decreasing the social capital and also very often theses action are undertook without knowing or respecting the proper accounting or fiscal regulations. The corporate governance imposes the transparency of fiscal and accounting information, because they are the corner stone of every decision and must help different categories of users in choosing the optimal solutions, especially for the fiscal management of every company. Recent reality certifies the fact that Romania has achieved progress in company administration and the implemented reforms have improved the judicial and reglementation system. This study wants to present some legislative aspects regarding the decrease in social capital and propose directions for solving or preventing the fiscal risks that are implied.*

## A) LEGAL REGULATIONS:

**a1)Law 31/1990** republished mentions at **article 103, line (1)** that "a company cannot acquire her own shares, either direct, either through persons who act in their own name but for the companies benefit, except the case in which the shareholders extraordinary general assembly decides otherwise, respecting the following dispositions**".** At the same article line (5), it is mentioned that "payment of these shares will be made only from dividends or from available reserves of the company, excepting the legal reserves, declared at the last annual approved finance situation"

Still at **article 104**, **it is said that "restrictions from article 103 are not applicable** when the company obtains a majoritary number of its own shares, free of all constrains if done in one of the following situations: ***a) with the purpose of reducing social capital, according to article 207, by rendering out of use a number of its own shares equal to the value of the reduction".***

Article 207, line (1), letter (c), stipulates "social capital may be reduced ***by acquiring own shares and taking them off the market***". Also, at line 2 "social capital may be reduced, only when this reduction is not motivated by losses by […] giving back to shareholders a quota from their shares, proportional with the capital reduction and equally calculated for every share or social part"

In conformity with article 158, law 31/1990 republished, if managers receive information that, after a severe loss, the ***net active***, calculated as a difference between the total of actives and the companies' debt, ***represents less then half of the value of the social capital***, they will call for an extraordinary general assembly in order to either re-create the capital, reduce it to its present value or dissolving the company. **This is why it is recommended to verify this condition, before reducing the social capital**.

**a2) Law 571/2003** regarding the fiscal code defines the **dividend** in title I "General dispositions", at chapter III "Definitions", as being "a distribution in money or in products, made by a company to a participant to that company, due to the fact that this persons owns shares of that company, except the following : **[…] b)** a distribution in money or in products, made in connection with the buy back of shares, other then the buy back that is not part of any plan, that does not modify the percentage of shares of any share holders **[…]**"

***Interpretation: In the situation in which a buy back of own shares occurs, in order to reduce social capital, this has <u>fiscal implications regarding the taxation of dividends if the society does not buy back shares from all the share holders in equal measure.</u>***

**B) Accounting registration linked to the operation of buying back own shareholders, at a higher price then their nominal value**

**b1)** Reducing social capital according to taking of the market these shares**, in the variant of maintaining the proportion.**

There are two accounting techniques to register this; one is based on admitting financial expenses the other on reducing other reserves as follows:

**b1.1) accounting treatment means admitting some expenses:**

a) buying back shares at a price bigger then their nominal value**:**

**109** **=** **5121** buy back price

b) Taking of the market bought shares at their nominal value:

**%** **=** **109** <u>buy back price</u>
**1012** nominal value of shares
**668** difference between reburying price and nominal value

**b1.2) accounting treatment means utilizing resources**:

a) buying back shares at a price bigger then their nominal value**:**

**109** **=** **5121** buy back price

b) Taking of the market bought shares at their nominal value:

**%** **=** **109** buy back price
**1012** nominal value of shares
**1068** difference between reburying price and nominal value

**Interpretation of the two accounting techniques used:**

In case the company has admitted to fiscal expenses, **from a fiscal point of view the will be considered fiscal non-deductible**, because it is considered they must be supported from the accounting profit distributed. If the reserves of the entity are used, in the limit of the law, the size of its own capital decreases, like in the case mentioned and interpreted before, **the fiscal incidence appears only if the reserve must be submitted to fiscal taxation**.

**b2)** Reducing the social capital accordingly to taking of the market those shares**, in the variant in which the proportion is not kept:**

From an accounting point of view, the registrations are identical with the one presented at point b1), using the two accounting techniques mentioned before.

**From a fiscal point of view**, **the difference** between the buy back price and the nominal value of the shares bought back and taken of the market **is considered a dividend**. Thus we must calculate and register the taxation on dividends, with the help of the formula of reduced hundred. The obligation of declaring the taxes on dividends goes to the company for the shareholders that have left the company.

**635** **=** **446** taxing dividends

From a fiscal point of view, this expense in non deductible when calculating the taxes on income.

**The names of the used accounts:**
1012 Social capital submitted
109 Own shares
1068 Other reserves
446 Other taxes and taxation
5121 Reserves in lei at banks
635 Expenses with other taxes and taxation
668 Other financial expenses

**C) Accounting registrations of the operation of buying back own shares, at a lower price then their actual nominal value**

**c1)** Reducing social capital according to taking of the market these shares**, in the variant of maintaining the proportion.**

From an accounting point of view, the two techniques of registrations refer to admitting a fiscal income, or making new reserves like this:

**c1.1) Admitting a financial income**:

a) buying back shares, at a lower price then their actual nominal value**:**

**109** = **5121** buy back price

b) Taking of the market bought back shares, at their nominal value:

**1012** = **%** nominal value of shares
**109** buy back price
**768** difference between the buy back price and their nominal value

**From a fiscal point of view, the income is non taxable when calculating profit income.**

**c1.2) making up new reserves**:

a) Buying back shares, at a lower value then their actual nominal value:
**109** = **5121** buy back price

b) Taking of the market bought back shares, at their nominal value:

**1012** = **%** nominal value of shares
**109** buy back price
**1068** difference between the buy back price and their nominal value

**c2)** Reducing the social capital accordingly to taking of the market those shares**, in the variant in which the proportion is not kept**:

The accounting treatment is the same as the one presented at point c1), in the two other variants:

**From a fiscal point of view we also consider that** the difference between the nominal value of shares and the buy back price **is considered a dividend and the expenses is non deductible when calculating the taxation on profit.**

**635** = **446** taxation on dividends

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