

Romania
Fiscal Council

***Impact of the change in taxation of
company earnings in Romania between
2015-2018***

Study

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- *Bogdan Dumitrescu*
 - *Filip Iorgulescu*
 - *Iuliana Dascălu*
 - *Andreea Draghia*
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Fiscal Council

Casa Academiei Române, 13 Calea 13 Septembrie, Bucharest, Romania

Telephone/fax. +40 21 318 48 26

Website: <http://www.consiliulfiscal.ro>

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Summary

In the period 2015-2018, Romania's economy was characterized by a sustained economic growth, which coincided with a significant increase in the profitability of companies. However, the budget revenues from the corporate income tax have generally been below expectations, and this has to be correlated with the extensive legislative changes in the way business earnings are taxed during this period. In the light of these issues, the present study aims to analyze the impact of each change in the legislative framework related to the budget revenues, including an *ex-ante* evaluation of the consequences of the legislative changes applicable starting 2018 and the evolution of the average corporate income tax rate in the period 2015 - 2017.

The study is based on the annual financial statements sent to the MPF by the firms of the non-financial sector operating in Romania.

In the period 2015-2018 there were major legislative changes in the taxation regime of the Romanian companies' earnings. The annual revenue threshold up to which a firm is considered a microenterprise has increased more than 15 times, and the tax rates have been significantly reduced and differentiated according to the number of employees.

In the period 2015 - 2018, extensive legislative changes were made in the tax regime for Romanian companies' earnings. The maximum threshold of the annual income to which a company is included in the microenterprise category has been increased by more than 15 times, from 65,000 euro in 2015 to 100,000 euro in 2016, 500,000 euro in 2017 reaching 1,000,000 euro in 2018. Concerning the tax rates applied to the microenterprises' income, these have been reduced and differentiated according to the number of employees starting with 2016. From the 3% single rate in 2015, in 2016 the tax rate was differentiated at 3% applied to microenterprises without employees, 2% for microenterprises with one full-time employee and 1% for microenterprises with at least two full-time employees. In 2017 the number of tax rates was reduced to two: 1% for microenterprises with at least one full-time employee and 3% for microenterprises without employees. Moreover, small companies were also enabled to opt for income tax or profit tax, the capital requirements needed to exercise this option being significantly reduced, respectively from the equivalent of 25,000 euro in 2015 and 2016 to 45,000 lei starting with 2017.

Also, in 2017, for certain categories of companies, the profit tax was replaced by a lump sum.

Also, starting January 1, 2017, the companies operating in the tourism sector, restaurants and catering subject to profit tax became payers of a specific tax, the newly introduced tax having the characteristics of a lump tax.

As a result of the successive increases in the maximum threshold up to which a firm is considered a microenterprise, their number and contribution to the economic activity have seen a spectacular growth.

As a result of the significant increases in the maximum threshold for the microenterprise's income, in 2017 about 90% of the analyzed companies have obtained operating revenues falling under this limit (representing an extension of the sample by about 25 pp or over 161 thousand companies compared to 2015), and the contribution of this segment to the economic activity has seen spectacular growth: aggregated operating revenues represents 10.2% of the total (from 2.2% in 2015), and the positive gross profits 22.9% (compared to 7.2% in 2015). Continuing the process of extending the ceiling on microenterprise revenues in 2018 will result in an even greater increase in these weights, emphasizing the shift of taxing from profit to income

The income tax regime proved to be more advantageous for microenterprises at the aggregate level. However, the advantage has been concentrated among those with high profit rates, those having losses or low profitability being disadvantaged. The share of the underprivileged companies, even if it has become a minority since 2016, remains still significant.

Analyzing the average tax rates of profit-earning companies, it is noted that for each year of the 2015-2017 period, the microenterprises benefited from a much lower tax rate on gross profits than companies subject to corporate income tax, the difference reaching even 8 pp. It should be noted, however, that this advantage is not evenly distributed among microenterprises, the main beneficiaries of the business income tax regime being firms with high rates of profit, while firms with low profitability and loss-making companies were disadvantaged by this tax regime. Thus, the firms that were disadvantaged by this tax regime have made important contributions to economic activity, accounting for 60% of the aggregate revenues of microenterprises in 2015, 41% in 2016 and 44% respectively in 2017.

Regarding the large companies, the average tax rate on their earnings recorded decreases during the period under review reaching 13.5% at the end of 2017 and on the background of the specific tax introduction.

If the profit tax regime had been applied to the microenterprises as well, higher budget revenues might have been collected. This situation is also due to the fact that the income tax

Under the circumstances that the profit tax regime had been applied to the microenterprises too, the amounts paid by these companies to the budget would have been significantly higher than those reported in their annual financial statements (+18% in 2015, +93% in 2016, respectively +122% in 2017, representing an increase in budgetary revenues of over 3 billion lei over the three years). It should be noted, however, that these higher values are due, on one

regime appears to have led to bringing out supplementary profits for the microenterprises.

hand, to the advantages of the income tax regime and, on the other hand, to the fact that in the years when the taxation of profits shifted to income taxation, the gross profits of these companies have seen spectacular increases. Thus, the extension of the income tax regime seems to have determined bringing out supplementary profits, but without generating additional budgetary revenue.

The major legislative changes concerning the taxation of earnings also had important consequences on the general budget revenues. Although the aggregate gross profits had registered significant increases each year, the number of profit tax payers declined considerably over the last four years, and the loss of revenue for this budget aggregate was not offset by the increases in the receipts coming from the microenterprise's income tax or from the specific tax.

The major changes in the taxation regime of earnings in Romania had important consequences on the general government revenues. Despite the constant advance of the gross profits obtained at the level of the entire economy by the companies with a positive level of this indicator, namely 15.8% in 2016 and 16.6% in 2017, the budgetary revenues did not follow this evolution, as the aggregate "Taxes on income, profit and capital earnings from legal persons" increased by 10.8% in 2016 and decreased by 1.5% in 2017. Given the significant reduction in the number of the profit tax payers, it can be estimated, using prudent assumptions, that the aggregate budget receipts were negatively affected, amounting to 1.5-2 billion lei over the last 4 years. Considering the structure of the budgetary sub-chapters, the receipts from the profit tax were negatively affected by about 2.7-3.3 billion lei, and this amount could not be compensated by the increase in the revenues from the income tax of the microenterprises estimated at about 1.2 billion lei. This transition from the profit taxation to income taxation has taken place during a period of economic expansion when firms' profitability is even higher, and that increased the amplitude of the revenue loss. Moreover, the possibility for companies to opt for profit tax or income tax allows companies to optimize their tax obligations, with additional negative consequences on the budget revenues.

I. Introduction

The taxation of earnings is a particularly important component of any tax system. Between 2015 and 2018, there were major legislative changes in Romania regarding the way in which corporate earnings were taxed, which resulted in changing the focus on income taxation instead of profit taxation, the rates applied being reconsidered and now depending on the number of employees, while for certain categories of activities the profit tax was replaced by a specific tax.

This rethinking of the corporate income tax system has been achieved through the massive expansion of the firms categorized as microenterprises, the annual revenue threshold to which a company is included in this category being increased more than 15 times between 2015-2018. Developed from the perspective of the fiscal easing process associated with the proposal to amend the Fiscal Code in 2015, this new tax regime has profound implications for the level of the tax rates applied to corporate income, the budgetary revenues, and, ultimately, to the added value formation process in these enterprises.

In many countries, small firms benefit from a simplified income tax system, which is based on several arguments. First, the literature has shown that for small businesses the administrative costs, including, among others, the costs of accounting reporting, determination of fiscal obligations and regulatory compliance obligations, are higher in relation to their income or assets compared to large firms. Secondly, small firms are disadvantaged in the competition with larger firms by the more limited access to financing, and the inability to compete in research and innovation. In addition, a simplified tax system applicable to small firms can help to reduce tax evasion in their case.

The goal of any entrepreneur is to maximize profit. Thus, the tax burden from the perspective of income taxation will be represented by the share of the business income tax paid in the gross profit. From this perspective, it is more natural that the income taxation to be made through profit tax or through a "real" system in which taxation is made on the difference between income and expenditure. However, many countries have decided to apply the taxation on "presumed" earnings for the small firms, namely by applying a tax on income or assets, precisely to promote a simple tax system and to reduce the phenomenon of tax evasion.

Therefore, the identification of an optimal balance in the classification of small firms to which "presumed" taxation is applied, as well as the choice of the tax rates leading to increased voluntary compliance and fiscal equity, respectively, ensuring a competitive environment for the small businesses is an approach characterized by multiple challenges.

The extensive legislative changes operated in Romania regarding the corporate income tax regime were implemented in the period 2016-2018, characterized by a high rate of economic growth and, implicitly, a strong growth for the firms' profitability. However, at least in the year 2017, this massive improvement in company profitability was not found at the level of budget revenues, the receipts from income tax, profit and capital earnings from legal entities being about 2 billion lei lower than those estimated in the initial budgetary projection and even lower in nominal terms as compared to 2016. However, the causes of this surprising evolution were not identified in an analysis.

In the light of all above, the present study aims to identify the impact of legislative changes concerning the taxation of company earnings on their tax rate as well as on the budget revenues. Using data at macroeconomic level, respectively information from the financial statements submitted by Romanian companies to MPF, the study will provide an *ex-post* evaluation of the impact of the measures implemented during the period 2015-2017, as well as an *ex-ante* evaluation of the consequences of the changes applicable in 2018 on the budget receipts for this year.

The corporate earnings tax rate will be studied in evolution, while a comparison is made between the tax determined for microenterprises and the one calculated for larger firms. Moreover, microenterprises will be divided into several subgroups according to the profitability rate to determine the proportion of companies benefiting from income tax instead of profit tax. The budgetary impact of the legislative changes will be individually identified for each fiscal policy measure, considering both the impact on the general consolidated budget and separated for the receipts from profit tax and income tax for microenterprises. Also, the impact determined on the basis of *ex-post* data will be compared with the initial estimate of the budgetary impact.

The study is structured as follows: it begins by presenting the evolution of the corporate income tax regime in the period 2015-2018, followed by the presentation of the data and methodology used. Subsequent, the evolution of the tax rate on the business income of the Romanian firms in the period 2015-2017, and the impact of the change in the taxation regime on the budget revenues are analyzed in detail. Finally, the conclusions and implications for economic policy makers are formulated.

II. The evolution of the tax regime for companies' earnings in the period 2015-2018

In the period 2015-2018, major legislative changes were made in the tax regime for the Romanian companies' earnings both in terms of the scope of those considered to be microenterprises and in terms of tax rates applied or the possibility to opt for one system or another regarding the taxation of earnings. In addition, for those companies operating in some areas of activity, a specific tax was introduced instead of the profit tax. Next are briefly presented the main legislative changes in the Romanian corporate income tax regime that generated a significant impact on the tax rates and implicitly on the budget revenues.

At the level of the year 2015, in the microenterprises category were considered the companies with annual incomes lower than the equivalent in lei of 65,000 euro, and the tax rate was 3% applied to the revenues. Additionally, companies with a share capital higher than the equivalent of 25,000 euro in lei could choose to be a profit tax payer, the option being final. There were also some limitations on the possibility to be classified as a microenterprise and implicitly to pay a tax on income, a notable example being the companies that obtained revenues from consultancy and management activities in a proportion of over 20% of the total annual income.

Starting with January 2016, the annual income threshold up to which a firm is considered a micro enterprise was increased to the equivalent in lei of 100,000 euro. In addition, the tax rates have been differentiated according to the number of employees as follows: 3% for companies without employees, 2% for those with one full-time employee and 1% for those with 2 or more full-time employees. Newly established enterprises with one full-time employee also benefited from the 1% tax rate in the first two years of operation. The possibility to opt for the profit tax remained conditional on a share capital higher than the level of 25,000 euro, as in the previous year. Essentially, in 2016 the scope of companies considered as microenterprises increased moderately and the tax rates were reduced, in some cases quite significant.

Starting February 2017, the annual income threshold up to which a firm is considered as a microenterprise was again increased, this time even more substantially, to the equivalent in lei of 500,000 euro and the number of tax rates decreased, as the 2% for companies with one employee was eliminated, and replaced by a 1% tax rate. Thus, for this category of companies the taxation was significantly reduced. The possibility to opt for the profit tax became conditional on a share capital higher than 45,000 lei, this threshold being considerably diminished compared to the previous year. Moreover, as from 1 January 2017, the companies operating in the tourism, restaurants and catering sector and paying profit tax became payers of a specific tax, the new tax having the characteristics of a lump tax depending on several variables such as: the rank of the

locality where the firm functioned, its surface or seasonality. Microenterprises operating in these sectors remain income tax payers. In essence, in 2017, the scope of companies considered as microenterprises increased significantly, the tax rates were reduced for companies with one employee, the possibility to opt between the profit tax and the income tax became subject to a lower level of the share capital of the microenterprises, and for those operating in certain economic sectors, the profit tax was replaced by the specific tax.

Starting February 2018, the annual income threshold up to which a firm is considered a microenterprise was again significantly increased, to the equivalent in lei of 1,000,000 euro, and in order to benefit from the possibility to opt for the profit or income tax, two conditions must now be met, namely a minimum share capital of 45,000 lei, as in the previous year, as well as a minimum number of 2 full-time employees. Moreover, the firms that earn more than 20% of their total revenue from consultancy and management activities, formerly excluded from the microenterprises' category, being automatically profit tax payers, now benefit from the same status as the other microenterprises. In essence, in 2018, the scope of the companies considered as microenterprises was again substantially increased, and the possibility to choose between the profit tax and the income tax for microenterprises became conditional on a number of employees at least equal to 2.

In addition, although it does not refer to the taxation of the company earnings *per se*, in the view of the attractiveness of doing business through a microenterprise regime, we mention the measures to reduce the dividend tax rate from 16% to 5% starting with 1 February 2017 and the possibility to grant interim dividends from the profit of the current year starting with the third quarter of 2018. Associated with the measures aiming to reduce the tax rates applicable to microenterprises and extending the annual income threshold up to which a firm is included in this category, the current legislative provisions may also generate a reorientation of the organizational form for the economic agents on the purpose of tax optimization.

III. Description of the data and methodology used

The analysis of the impact of the change in the taxation regime in the period 2015-2017 was made on the basis of the annual financial statements submitted by the non-financial firms operating on the territory of Romania¹. Thus, the database for the three years considered includes the information stated in the forms: F10 (Balance sheet), F20 (Income statement), F30 (Informative data) and F40 (Statement for fixed assets). Taking into account the objectives of this study, which look at the evolution of the corporate income tax for the Romanian companies and the impact of the change in the taxation regime on the budgetary revenues, the analysis was structured in the following manner:

- First, only the **companies with economic activities during the period 2015-2017 were included in the analysis**, eliminating the companies with a very small volume of activity (the condition that the annual operating income must have a minimum level of 1,000 lei was applied). This condition determined a significant reduction in the number of firms included in the study, the size of the samples being set for each year decreasing by more than 25%;
- Secondly, since the regulations on the taxation of microenterprises' income define a threshold of their revenues (in case of exceeding this threshold the companies become subject to the profit tax), **the companies were sorted by income series related to the changes made to the threshold up to which a firm may be considered a microenterprise** as follows: annual revenue of maximum 65,000 euro (threshold applied in 2015), annual revenue ranging from 65,000 to 100,000 euro (threshold applied in 2016), annual revenue ranging between 100,000 and 500,000 euro (threshold applied in 2017); annual revenue over 500,000 euro. At the same time, it should be noted that the verification of compliance with the threshold and the calculation of the tax on the income of microenterprises is made in relation to a tax base which consists of the total income adjusted by deducting or adding some elements mentioned in the tax regulations. In order to ensure the comparability of the results, since the tax base was slightly changed from one year to the other and because information was not available to allow it to be calculated accurately, **the taxable income was approximated by the operating income**;
- Although the firms were divided into income series, **within each interval can be found both tax payers for the income of microenterprises as well as profit tax payers and/or specific tax payers**. This is due to a number of factors such as the existence of additional criteria for microenterprise (for example, at least 80% of revenue should come from

¹ The study includes only the financial statements submitted to the MPF within the legal deadlines for reporting.

activities other than consultancy and management, share capital must be owned by persons other than the state and the administrative-territorial units, etc.), the possibility of companies having a share capital higher than the threshold defined by the law to opt for the payment of profit tax, but also the effects of approximating the tax base through the operating income. **Because the information needed to accurately identify the companies which are subject to profit tax, or income tax payers as microenterprises and those subject to specific tax was not available, the data reported by the firms in the profit and loss account were used as follows: profit taxes are paid in the account 691, respectively payments related to microenterprise income tax and specific tax (other taxes) recorded cumulatively in the account 698.** At the same time, it should be noted that some companies made simultaneous payments in both accounts, the most common situation being the case when the firm changed the taxation regime from one year to the other (the transition being made as of February 1, according to the law) or in the course of a fiscal year, but it is also the case of the companies that pay both profit and specific tax for some activities. Therefore, **if the tax regime of a company could not be identified with certainty and some companies applied a mixed tax regime during the fiscal year, the tax rates used in this study were calculated on the basis of the total taxes paid by a firm in the accounts 691 and 698;**

- Moreover, **in order to highlight as accurately as possible, the fiscal burden of the Romanian companies, regardless of their tax regime, the tax rates were calculated both in relation to the gross profit and in relation to the operating revenues.** In this context, the analysis on taxation using income breakdown has proved to be insufficient because the aggregation of gross profits and losses recorded by firms in each range led to a reduction of the tax base and to unrealistic profit tax rates. As a result, **at the level of each income interval, there was a separate analysis of the companies that registered profit, respectively of those who registered a loss;**
- Subsequently, the **analysis on taxation of the companies that recorded profit during the period under review was extended to capture the tax advantages/disadvantages generated by each tax regime based on the gross profit ratio recorded.** For example, in the context of 2015 tax regime (when the tax rate on microenterprise income was 3%), a company with a gross profit margin on operating income of 18.75% would have been indifferent between the payment of profit tax and income tax on microenterprises. In relation to this benchmark, firms with a gross profit ratio below 18.75% would have benefited from paying profit tax, while firms with a gross profit ratio higher than 18.75% would have benefited from paying income tax as microenterprises. For the years 2016 and 2017, identifying this point of indifference is more difficult because the change in tax regulations for the microenterprises' income tax led to the application of differentiated tax rates in relation to the number of employees of the firm. Thus, if in 2015 only a unique

3% tax rate was applied, in 2016, reduced tax rates of 1% and 2% respectively were introduced for companies with employees, and in 2017 the unique tax rate of 1% for companies with at least one employee was set. Since companies with a 1% tax rate (firms with at least two employees in 2016 and at least one employee in 2017 respectively) recorded the highest levels of operating income and gross profits, compared to the firms that were taxed differently, the tax analysis for the companies that made profit in the period 2016-2017 was based on a gross profit margin of 6.25% related to the operating income (this represents the point of indifference between the tax regime of microenterprises income and the profit tax payers, under the condition of 1% tax rate on the microenterprise's income);

- Last but not least, **in order to estimate the impact of the change in the tax regime of the Romanian firms' earnings on the budget revenues, the companies from the database were categorized both on income intervals and in relation to the number of employees** because the main legislative changes to the taxation on the income of microenterprises between 2015 and 2017 aimed at increasing successively the thresholds up to which a firm can be considered a microenterprise, as well as the gradual reduction of the tax rate according to the number of employees. Thus, through an incremental approach from one year to the other, *the ex-post* estimation of the impact of each legislative measure that modified the tax regime on the total level of taxes paid by the Romanian companies and the results obtained were correlated with the evolution of the receipts from the profit tax. Also, having in view the announced increasing of the threshold for microenterprise revenues in this year, an *ex-ante* assessment of the impact of this measure on the budget revenues in 2018 was made.

IV. The evolution of the tax rate on earnings for the Romanian companies during the period 2015-2017

Prior to analyzing the taxation rate on corporate income for the Romanian companies, *Table 1* gives an overview of the database used in this study. As mentioned in the previous section, the database was built using the information reported in the financial statements submitted to the MPF by the non-financial firms operating in Romania, including only those companies that have complied with the statutory reporting deadlines.

Thus, it can be noticed that in the three years considered, about 650,000 - 700,000 companies submitted annual financial statements, their number registering a growing trend from one year to the other. However, a significant part of companies that have submitted financial statements have a low volume of activity or are even completely inactive. As a result, the initial database was adjusted by eliminating companies with lower operating revenues than the 1,000 lei threshold, which resulted in a reduction of the sample size by more than 25%, the most significant decrease occurring in 2015².

In order to check whether the elimination of such a large number of firms is likely to affect the results of the study, *Table 1* compares the levels of operating income and total taxes paid by all companies that have submitted financial statements, respectively by the companies remaining in the analysis after adjusting the database. Thus, it can be noticed that the firms remaining in the analysis are particularly representative for the original database, the total operating income and tax paid being almost identical (the coverage rate is over 99% in all three years considered, and on the background of negative operating income, there are situations where the operating income of firms remaining in the analysis slightly exceeds the aggregate value of total companies).

Therefore, the database used and the results of its processing recorded in this study refer only to companies with operating revenues of at least equal to 1,000 lei, which are found in *Table 1* under the name of "companies included in the analysis".

² It should be noted that in 2015 there were found errors in the database which were manifested by the lack of information regarding the gross profit, respectively the net profit for more than 5,000 companies. Thus, the adjustment of the database implied the elimination of both the companies with operating incomes lower than 1,000 lei, and also those with the aforementioned errors.

Table 1: Comparative analysis of the initial database with the adjusted database containing only the companies included in the study (million lei)			
Year	2015	2016	2017
Total number of companies that submitted financial statements	647,872	677,843	692,968
Aggregate operating income - total	1,229,760	1,314,012	1,417,447
The aggregate amount of taxes paid by total companies	13,041	14,030	14,264
Number of companies included in the analysis (in brackets percentage of total)	464,277 (71.7%)	497,242 (73.4%)	513,420 (74.1%)
Aggregate operating income of companies included in the analysis (in brackets percentage of total)	1,226,631 (99.8%)	1,314,135 (100.01%)	1,417,780 (100.02%)
The aggregate amount of taxes paid by the companies included in the analysis (in brackets percentage of total)	12,964 (99.4%)	14,004 (99.8%)	14,248 (99.9%)

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

According to the study methodology presented in the previous section, the evolution of the tax rates on income during the period 2015-2017 was realized through the average tax rates calculated both on the gross profit and on the operating income. Further, the results obtained will be presented and analyzed at the level of each year considered, taking into account the amendment of the legislative guidelines from one year to the other. This issue will be further developed in the section aimed at estimating the budgetary impact of these changes.

IV.1. Analysis of taxation on companies' earnings in Romania in 2015

Considering that the ceiling for microenterprise income was 65,000 euro in 2015, *Table 2* shows the tax rates for all companies, as well as the difference between firms with lower operating revenues, respectively, above this ceiling. Moreover, since the aggregation of gross profits and losses is likely to diminish the tax base, affecting the tax rates calculated for gross profit, we proceed to separate the profit and loss-making companies.

Table 2: Analysis of earnings' taxation of companies in Romania in 2015 on the basis of the operating revenues and the gross result (profit / loss) (mil. euro)				
Calculated indicators / Categories	Companies with annual operating income (euro):	Total,	Out of which:	
			Gross profit	Gross loss
Number of companies	Aggregate level, out of which:	464,277	317,867	146,410
	<= 65,000	300,681	185,120	115,561
	> 65,000	163,596	132,747	30,849
Profit tax (account 691)	Aggregate level, out of which:	12,128.5	12,251.8	-123.3
	<= 65,000	104.2	91.4	12.8
	> 65,000	12,024.2	12,160.4	-136.2
Tax on microenterprise income (account 698)	Aggregate level, out of which:	835.4	631.3	204.2
	<= 65,000	676.5	494.3	182.2
	> 65,000	159.0	137.0	22.0
Total taxes (691 account + 698 account)	Aggregate level, out of which:	12,963.9	12,883.0	80.8
	<= 65,000	780.7	585.7	195.0
	> 65,000	12,183.2	12,297.4	-114.2
Total gross profit	Aggregate level, out of which:	52,659.9	87,691.8	-35,031.8
	<= 65,000	1,083.4	6,282.7	-5,199.3
	> 65,000	51,576.5	81,409.0	-29,832.6
Total operating income	Aggregate level, out of which:	1,226,630.5	1,015,660.8	210,969.8
	<= 65,000	27,418.0	19,399.1	8,018.9
	> 65,000	1,199,212.5	996,261.7	202,950.9
Average rate of taxation calculated on gross profit	Aggregate level, out of which:	24.6%	14.7%	-0.2%
	<= 65,000	72.1%	9.3%	-3.8%
	> 65,000	23.6%	15.1%	0.4%³
Average tax rate calculated on operating income	Aggregate level, out of which:	1.1%	1.3%	0.0%
	<= 65,000	2.9%	3.0%	2.4%
	> 65,000	1.0%	1.2%	-0.1%

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

³ For companies with operating incomes above the threshold of 65,000 euro that recorded losses, the average tax rate on gross profit has a positive value because the total tax paid by this category of companies is, in turn, negative. This atypical situation is due to the corporate income tax declared by these companies, which had an aggregate value of -136.2 million lei.

Analyzing the results obtained at the level of all the companies included in the analysis, it is noticed that the majority of them (68.5%) completed the financial year with profit, generating over 80% of the aggregate value of operating income. On the other hand, the level of gross losses was quite high, so that, although the profitable companies achieved an aggregate profit of 87.7 billion lei, by adding the losses this value decreased by about 40% to 52.7 billion lei. Compensation of profits with losses for the total companies has a significant impact on the rate of taxation calculated on gross profit, which reaches the value of 24.6%, while the tax rate calculated only for companies with profit reaches a much more realistic level, of 14.7%. This confirms the need to differentiate the analysis according to the companies that have registered profit or loss, in order to increase the relevance of the results attained.

From the perspective of the structure of taxes paid, the profit tax is prevailing, while the tax on the income of microenterprises represents less than 7% of the total. Thus, at the level of 2015, the impact of the tax on microenterprises income on the budget revenues is quite limited, a conclusion also confirmed by the fact that the average rate of taxation for all profitable companies (14.7%) is close to the legal tax rate.

Companies with operating revenues less than or equal to the ceiling of 65,000 euro have a significant share in the total number of firms (almost 65%), but their diminished size makes their generated gross profit and operating income to represent about 2% of the total. From the perspective of the tax structure on earnings, it is noticed that firms in this range predominantly pay microenterprise income tax (accounting for almost 81% of the total payments for this category), while corporate income tax payments are very low (less than 1% of total payments for this category). On the whole, the **taxes paid by companies with operating incomes lower than or equal to the 65,000 euro threshold, accounted for only 6% of the total taxes paid by the firms included in the analysis, highlighting the reduced impact of this category on budget revenues.**

Almost 62% of companies with operating income up to 65,000 euro ended the financial year with profit and were taxed at an average tax rate of 9.3% on the gross profit. In terms of the tax rate calculated on operating income, this is similar to the legal tax rate of 3% for profit-making companies, while loss-making firms were charged at an average tax rate of 2.4%. Thus, the income tax regime for microenterprises has clear disadvantages for the loss-making firms, but seems to offer more favorable conditions to profitable firms whose average rate of taxation in relation to gross profit (9.3%) was much more advantageous than the standard tax rate applicable to the profit tax payers (16%).

Therefore, the impact of this tax regime requires a deeper analysis to determine under what conditions its application has favorable/unfavorable consequences for microenterprises. The assumption used is that, in the context of a uniform tax rate on microenterprise income of 3%, firms with a gross profit ratio of over 18.75% benefit from this tax regime, while firms with lower

gross profit ratio would benefit from paying profit tax. In order to verify this hypothesis, *Table 3* shows the average tax rates for companies with operating income of less than or equal to 65,000 euro and with positive gross profits, differentiated according to the 18.75% threshold for the gross profit ratio.

Table 3: The analysis of the taxation on earnings obtained by companies with operating income less than or equal to 65,000 euro which recorded profit, according to the gross profit ratio (million lei)			
Indicator/Category	Total, Out of which:	Gross profit ratio	
		<= 18,75%	> 18,75%
Number of companies	185,120	74,578	110,542
Profit tax (account 691)	91.4	23.1	68.3
Tax on microenterprise income (account 698)	494.3	203.0	291.3
Total taxes (account 691+ account 698)	585.7	226.1	359.6
Total gross profit	6,282.7	688.3	5,594.4
Total operating income	19,399.1	8,407.1	10,992.0
<i>Average rate of taxation calculated on gross profit</i>	9.3%	32.8%	6.4%
<i>Average rate of taxation calculated on operating income</i>	3.0%	2.7%	3.3%

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

The results show that about 60% of the companies that made profit also registered gross profit ratios over 18.75%. These companies definitely dominated in terms of the gross profit, which amounted to 5.6 billion lei, compared to a gross profit of only 0.7 billion lei obtained by firms with profit rates up to 18.75%, although they registered operating income by only 30% higher. From the perspective of the impact of the tax regime, the advantage of taxing microenterprise income for the firms with profit rates of over 18.75% is confirmed, registering an average tax rate in relation to gross profit of only 6.4%, while the average tax rate in relation to operating income was 3.3%. On the other hand, firms with profit rates less or equal to 18.75% have experienced an average tax rate almost 33% in relation to their gross profit and 2.7% in relation to the operating income.

In conclusion, although microenterprises are subject to a legal tax rate on income (3%), this tax regime creates a number of advantages/disadvantages for them, such as: loss-making firms (about 38% of companies with operating incomes up to 65,000 euro, accounting for 29% of the total operating income) are disadvantaged by the fact that they are taxed even in this situation, companies that have registered gross profit ratios less than 18.75% (about 25% of the companies, which generate 31% of the total operating income) would have been advantaged by paying profit tax, while highly profitable firms (around 37% of companies, which generate

40% of total operating income) are advantaged by paying income tax, as their effective tax on profits is much lower than the 16% legal tax rate.

As for the companies with operating income higher than the ceiling of 65,000 euro (see [Table 2](#)), they have a lower share in the total number of firms (about 35%), but generated the largest part of the operating revenues and gross profits (about 98% of the total for both indicators) because the interval includes large firms in the Romanian economy. As expected, these companies pay mainly profit tax (12 billion lei, representing more than 99% of total payments for this category), the value of the tax due on micro enterprises' incomes being only 159 million lei (19% of the total payments for this category). **It is notable that firms with operating revenues higher than 65,000 euro are the main contributors to the budget, with taxes paid accounting for almost 94% of the total tax on corporate earnings. More than 81% of these companies ended the financial year with profit and were taxed with a 15.1% average tax rate on the gross profit (close to the 16% statutory tax rate), while the average tax rate on operating income was 1.2%.**

IV.2. Analysis of taxation on companies' earnings in Romania in 2016

The year 2016 marked two important changes regarding the taxation of microenterprises revenue: increasing the ceiling on their annual revenue from 65,000 to 100,000 euro and reducing the tax rate relative to their number of employees. To begin with, [Table 4](#) shows the average tax rates for all companies, as well as differentiated according to the operating income (relative to the ceiling of 100,000 euro) and the type of the result obtained (profit or loss).

Analyzing the results obtained by all companies, there is an increase in their operating income (+87.5 billion lei, representing an advance of 7.1%), as well as the gross profit obtained by the profitable firms (+13.8 billion lei, respectively an advance of almost 16%) compared to 2015. The ascending evolution of the earnings was also found in the total paid taxes, which in turn increased by over 1 billion lei (representing an advance of about 8%) compared to the previous year.

From the perspective of the tax structure, the corporate income tax strengthened its majority position, while the tax on microenterprises' revenues accounted for 5.6% of the total, down by almost one percentage point from the previous year.

Table 4: Analysis of earnings' taxation of companies in Romania in 2016 on the basis of the operating revenues and the gross result (profit / loss) (mil. euro)				
Calculated indicators / Categories	Companies with annual operating income (euro):	Total,	Out of which:	
			Gross profit	Gross loss
Number of companies	Aggregate level, out of which:	497,242	350,974	146,268
	<= 100,000	358,715	234,636	124,079
	> 100,000	138,527	116,338	22,189
Profit tax (account 691)	Aggregate level, out of which:	13,225.6	13,004.4	221.2
	<= 100,000	134.4	124.2	10.1
	> 100,000	13,091.3	12,880.2	211.1
Tax on microenterprise income (account 698)	Aggregate level, out of which:	778.7	630.0	148.6
	<= 100,000	644.5	510.0	134.4
	> 100,000	134.2	120.0	14.2
Total taxes (691 account + 698 account)	Aggregate level, out of which:	14,004.3	13,634.4	369.9
	<= 100,000	778.8	634.3	144.5
	> 100,000	13,225.5	13,000.2	225.3
Total gross profit	Aggregate level, out of which:	68,052.3	101,505.6	-33,453.2
	<= 100,000	3,518.4	10,239.7	-6,7210.3
	> 100,000	64,534.0	91,265.9	-26,731.9
Total operating income	Aggregate level, out of which:	1,314,135.5	1,139,381.2	174,754.3
	<= 100,000	43,330.6	32,130.7	11,199.9
	> 100,000	1,270,804.8	1,107,250.5	163,554.4
Average rate of taxation calculated on gross profit	Aggregate level, out of which:	20.6%	13.4%	-1.1%
	<= 100,000	22.1%	6.2%	-2.2%
	> 100,000	20.5%	14.2%	-0.8%
Average tax rate calculated on operating income	Aggregate level, out of which:	1.1%	1.2%	0.2%
	<= 100,000	1.8%	2.0%	1.3%
	> 100,000	1.0%	1.2%	0.1%

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

Due to the increase of microenterprises income ceiling to 100,000 euro, more than 72% of the firms surveyed have achieved operating revenue that fall within this limit, but their size is still negligible: aggregate operating revenue represents 3.3% of the total and gross profits 5.2%. As expected, this firms preponderantly pay microenterprises income tax (accounting for almost 83% from the total payments of this category), while the corporate income tax payments represented only 1% of the total payments for this category. **The reduced share of these companies on the level of whole economy is also manifested in the case of paid taxes, which represents only 5.6% of the total taxes paid by the companies included in the analysis (-0.4 pp compared to 2015).**

It is noteworthy that, although the number of the firms that achieved operating revenue which fall within the ceiling applicable for microenterprises increased by more than 19% compared to the previous year (following the increase of the ceiling), the aggregate value of the tax on microenterprises revenue decreased by 32 million lei (-4.7%). **Therefore, the impact of the rate reduction depending on the number of employees (3% for the firms without employees, 2% for the firms with 1 employee and 1% for the firms who have at least 2 employees) from a uniform rate of 3% in 2015, exceeded the effect of widening the scope of coverage of the tax by increasing the ceiling applied on revenues. This aspect is also visible from the perspective of average tax rate calculated on the level of operating revenue, which decreased from 2.9% in 2015 to 1.8% in 2016.**

Out of the companies which obtained operating revenues less than or equal to the ceiling of 100,000 euro, about 35% registered losses, but due to the revenues taxation regime they incurred an average tax rate of 1.3% reported to the operating revenues (decreasing by 1.1 pp compared to the previous year). On the other, the firms which obtained profit⁴ have registered an average tax rate of about 2% reported to operating revenue, respectively 6.2% reported to gross profit, both values being significantly lower than in 2015. Thus, there is a similar situation to the previous year in which the profitable companies seem to be advantaged by the taxation regime on microenterprises revenue, and that's why it is necessary to conduct a more detailed analysis related to their profit margin.

Considering that in 2016 the tax rate on microenterprises revenue has varied depending on number of employees, the analysis was realized to the level of 1%, because the firms with at least two employees (to which this rate is applied) dominate the sample, both numerically and in terms of operating revenues and aggregate gross profit. In the context of a tax rate on revenues of 1%, it is expected to be advantaged by this taxation regime the firms with a profit margin of above 6.25%, while the other firms would be advantaged to pay corporate income tax. To verify this hypothesis, [Table 5](#) presents the average tax rates for the firms which obtained operating

⁴ It is noted that their aggregate gross profit increased by almost 63% compared to 2015.

revenues less than or equal to 100,000 euro and positive gross profits, differentiated according to the 6.25% threshold for gross profit margin.

Table 5: The analysis of the taxation on earnings obtained by companies with operating income less than or equal to 100,000 euro which recorded profit, according to the gross profit ratio (million lei)			
Indicator/Category	Total, Out of which	Gross profit rate	
		<= 6.25%	> 6.25%
Number of companies	234,636	39,721	194,915
Profit tax (account 691)	124,2	10,6	113,6
Tax on microenterprise income (account 698)	510,0	77,5	432,5
Total taxes (account 691+ account 698)	634,3	88,1	546,1
Total gross profit	10,239.7	202.2	10,037.5
Total operating income	32,130.7	6,723.9	25,406.8
<i>Average rate of taxation calculated on gross profit</i>	6.2%	43.6%	5.4%
<i>Average rate of taxation calculated on operating income</i>	2.0%	1.3%	2.2%

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

The results show that the majority of the firms (54.3%) with operating revenues less than 100,000 euro registered profit rates above the threshold of 6.25%, these categorically dominating the sample from the perspective of gross profit and aggregate operating revenues. On the average, these companies incurred a tax rate of 2.2% reported to operating revenues, respectively of 5.4% reported to gross profit. Thus, it is noted a clear advantage for the firms which exceed the profitability threshold of 6.25%, the average tax rates being inferior to those calculated for the previous year and more favorable than the corporate income tax system. On the other hand, the companies with profit margins less than or equal to 6.25% (representing 11.1% of the total firms from this interval) have incurred an average tax rate of 1.3% reported to operating revenues, but a tax rate of 43.6% reported to gross profit. **In conclusion, the tax rates on microenterprises revenue differentiated according to the number of employees had a reduction effect of average tax rates for this category of firms, whether they were calculated related to gross profit or operating revenue. Another effect of this measure was the decrease of the profitability threshold from which microenterprises are advantaged by the revenues tax system in comparison to the corporate income tax system. Therefore, 54.3% of firms with operating revenues less than or equal to 100,000 euro (these generating 58.6% of total operating revenues) registered profit margins above 6.25%, benefiting from an effective taxation on the obtained gross profits at a lower level than the legal tax rate of 16%. By opposition, the companies with lower profitability than the ceiling of 6.25% (11.1% of these firms, generating**

15.5% of total operating revenues) and those which registered losses (34.6% of firms, generating 25.9% of the total operating revenues) would have been favored by the profit tax system.

Regarding the companies which achieved operating revenues above the ceiling of 100,000 euro (see [Table 4](#)), these represents only 27.9% of firms surveyed, but they generated over 94% of the aggregate value of operating revenues and gross profits. The majority of the firms from this interval are profit tax payers (13.1 billion lei, representing 99% of the total payments corresponding to this category), the value of tax on microenterprises income being only 134 million lei (representing 17.2% of the total payments for this category). **It is noted that the firms with operating revenues more than 100,000 euro remain the principal contributors to the budget, the taxes paid by them representing 94.4% of the total taxes on the earnings obtained. Almost 84% of these firms ended the financial year on profit (higher share than in 2015), being subject to an average tax rate of 14.24% in relation to the gross profit, respectively of 1.2% related to operating revenues.**

IV.3. Analysis of taxation on companies' earnings in Romania in 2017

In 2017 new legislative changes were implemented regarding the taxation on microenterprises income (increasing their revenue ceiling from 100,000 to 500,000 euro, respectively eliminating the tax rate of 2%, so as the microenterprises with one employee applied a tax rate of 1%) and the introduction of a specific tax on some activities conducted by companies that paid corporate income tax.⁵ To offer an overview on the evolution of earnings taxation, [Table 6](#) presents the average tax rates calculated for the entire sample of firms included in the analysis, but also differentiated depending on operating revenue (in relation to the new ceiling of 500,000 euro) and on type of the achieved result (profit or loss).

⁵ The specific tax does not appear separately in the financial statements of the firms, being aggregate in the 698 account together with the microenterprises income tax, so the differentiation between the two categories was made by the following manner: the firms with operating income lower than 500,000 euro were assimilated to revenue tax payers microenterprises, while the firms with operating revenues above the ceiling of 500,000 euro were considered profit tax payers, and the amounts reported in the 698 account were assimilated to specific tax. In the absence of some information regarding the type of tax paid by every entity, this methodology allows a reasonable approximation of the biases in taxing the earnings obtained by Romanian companies.

Table 6: Analysis of earnings' taxation of companies in Romania in 2017 on the basis of the operating revenues and the gross result (profit / loss) (mil. euro)				
Calculated indicators / Categories	Companies with annual operating income (euro):	Total,	Out of which:	
			Gross profit	Gross loss
Number of companies	Aggregate level, out of which:	513,420	365,963	147,457
	<= 500,000	462,480	321,047	141,433
	> 500,000	50,940	44,916	6,024
Profit tax (account 691)	Aggregate level, out of which:	12,634.6	12,434.7	199.9
	<= 500,000	412.6	375.8	36.9
	> 500,000	12,221.9	12,058.9	163.0
Tax on microenterprise income (account 698)	Aggregate level, out of which:	1,613.0	1,352.0	261.1
	<= 500,000	1,380.8	1,141.5	239.2
	> 500,000	232.3	210.4	21.9
Total taxes (691 account + 698 account)	Aggregate level, out of which:	14,247.6	13,786.7	460.9
	<= 500,000	1,793.4	1,517.3	276.1
	> 500,000	12,454.2	12,269.3	184.9
Total gross profit	Aggregate level, out of which:	87,719.3	118,318.0	-30,598.6
	<= 500,000	15,014.9	27,143.6	-12,128.7
	> 500,000	72,704.4	91,174.3	-18,469.9
Total operating income	Aggregate level, out of which:	1,417,780.3	1,244,451.4	173,328.9
	<= 500,000	144,642.2	116,963.8	27,678.4
	> 500,000	1,273,138.1	1,127,487.6	145,650.5
<i>Average rate of taxation calculated on gross profit</i>	<i>Aggregate level, out of which:</i>	16.2%	11.7%	-1.5%
	<= 500,000	11.9%	5.6%	-2.3%
	> 500,000	17.1%	13.5%	-1.0%
<i>Average tax rate calculated on operating income</i>	<i>Aggregate level, out of which:</i>	1.0%	1.1%	0.3%
	<= 500,000	1.2%	1.3%	1.0%
	> 500,000	1.0%	1.1%	0.1%

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

The evolution of the indicators computed for all the companies included in the analysis shows that, although the aggregate level of operating revenues increased by 103.6 billion lei (+7.9% compared to the previous year) and the level of gross profits achieved by the profitable firms increased by 16.8 billion lei (+16.6% compared to the previous year)⁶, the taxes paid on earnings have advanced by only 243.3 million lei, representing an increase of 1.7% compared to 2016. **Also, due to the important changes suffered by the legal framework of the earnings taxation, it is noted a rearrangement of the main tax categories as follow: the aggregate value of the profit tax payments decreased by almost 0.6 billion lei compared to 2016 (representing 88.7% of total tax), while the aggregate value of the other tax⁷ payments increased by almost 0.8 billion lei (reaching a share of 11.3% in total tax).**

On the basis of increasing the ceiling on microenterprises income, about 90% of the analyzed firms achieved operating revenues which fall within this limit (a sample size widening of over 100,000 firms compared to 2016), and the contribution of this section at the economic activity met a spectacular growth: the aggregate operating revenues represent 10.2% of total (compared to 3.3% in 2016), and the gross profits 17.1% (compared to 5.2% in 2016). The companies from this interval are preponderantly paying tax on microenterprises income (1.38 billion lei, being almost 86% of the total amounts from the 698 account), while the corporate income tax payments represent only 3.3% of the total payments for this category. **The taxes paid by the firms with operating revenues up to 500,000 euro accounted for 12.6% of the total taxes paid by the firms included in the analysis. This share denotes a significant growth compared to 2016 (+7 pp), being also a result of the increase in the ceiling for microenterprises income.**

Analyzing the effects of the taxation system on firms with operating revenues less than or equal to 500,000 euro, it is noticed that almost 31% of them registered losses, but were exposed to an average tax rate on operating revenues of 1%. On the other hand, the companies which obtained profit have incurred an average tax rate of 1.3% related to operating income, respectively 5.6% related to gross profit, both values being lower than those from 2016. Further we will proceed to the detailed analysis of the tax rates in relation with profit margin registered by these firms in order to highlight to what extent the advantages/disadvantages caused by the taxation system on revenues have been manifested. Given that in 2017 were applied two tax rates depending on number of employees, the analysis retained the rate of 1%, applied for microenterprises with at least 1 employee, because these dominate the sample, both numerically and from the perspective of operating revenues and aggregate gross profit. Thus, in the context of revenues taxation with a rate of 1%, it is expected that firms with a profit rate of over 6.25% will benefit from this taxation system, while the rest of the companies would be more advantaged to pay

⁶ On the basis of the high pace of economic increase from 2017.

⁷ Tax payments on microenterprises revenue and specific tax, found cumulatively in the account 698.

corporate income tax. To investigate this hypothesis, *Table 7* presents the average tax rates of the firms which registered operating revenues less than or equal to 500,000 euro and positive gross profits, differentiated on the basis of 6.25% threshold for profit margin.

Table 7: The analysis of the taxation on earnings obtained by companies with operating income less than or equal to 500,000 euro which recorded profit, according to the gross profit ratio (million lei)			
Indicator/Category	Total, out of which:	Gross profit rate:	
		<= 6.25%	> 6.25%
Number of companies	321,047	66,155	254,892
Profit tax (account 691)	375.8	59.8	315.9
Tax on microenterprise income (account 698)	19,141.5	263.0	878.6
Total taxes (account 691+ account 698)	1,517.3	322.8	1,194.5
Total gross profit	27,143.6	1,039.7	26,103.9
Total operating income	116,963.8	36,558.6	80,405.2
<i>Average rate of taxation calculated on gross profit</i>	5.6%	31.1%	4.6%
<i>Average rate of taxation calculated on operating income</i>	1.3%	0.9%	1.5%

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

The results show that the majority (55.1%) of the firms with operating revenues up to 500,000 euro registered gross profit rates above the threshold of 6.25%, these incurring an average tax rate of 1.5% reported to operating income, respectively 4.6% reported to gross profit. Therefore, it is noted a clear advantage for the firms which exceed the profitability threshold of 6.25%, the taxation on revenues for them being more favorable than the corporate income tax system. On the other hand, the firms with profit margins lower than 6.25% (accounted for 14.3% of the total firms within the interval) incurred an average tax rate of 0.88% reported to operating revenues, but 31.1% reported to gross profit. **In conclusion, 55.1% of the firms with incomes less than or equal to 500,000 euro (generating 55.6% of the total operating revenues) achieved profit margins of over 6.25%, benefiting from an effective taxation on gross profits at a level much lower than the legal rate of 16%. By opposition, the firms with a lower profitability than 6.25% (14.3% of firms, generating 25.3% of the total operating revenues) and those which registered losses (30.6% of firms, generating 19.1% of the total operating revenues) would have been advantaged by the corporate income tax system.**

Concerning the firms which achieved operating revenues higher than the ceiling of 500,000 euro (see *Table 6*), these represent less than 10% of the firms included in the analysis, but they have generated almost 90% of operating income aggregate value and almost 83% of gross profit aggregate value. The majority of the firms located within this range are profit tax payers (12.2

billion lei, representing 96.7% of the total payments for this category), but the value of these payments is decreasing by about 0.9 billion lei compared to 2016. On the other hand, the aggregate value of other tax payments increased by 100 million lei, reaching the level of 232.3 million lei (representing 14.4% of the total payments for this category). **The rearrangement of the pattern of taxes paid by these firms is the consequence of increasing the ceiling on microenterprises revenue, but also of specific tax introduction, both measures are likely to reduce the scope of profit tax in favor of the other taxes' categories. Another possible effect of the above measures is the reduction of average tax rate reported to gross profit (considering only the firms that achieved profit), which reaches the level of 13.5% in 2017, compared to 14.2% in 2016. Although the firms with operating revenues higher than 500,000 euro are still the main contributors to the state budget, the share of the taxes paid by them, being 87.4% of total taxes on earnings, decreased by 7 pp in 2017 due to the changes on legal framework.**

From the analysis of the evolution of taxation on earnings achieved by the firms from Romania, it is noted a gradual reduction of the scope of the corporate income tax during the period 2015-2017, which was partially replaced by the tax on microenterprises revenues and specific tax. Considering the aggregate level, the average tax rates calculated during the study show that, these alternative taxation regimes proved to be more favorable for firms, with a potential negative impact on budget receipts. At the firm level, the detailed analysis turned out that the alternative systems to corporate income tax favor the entities with high profitability rates which are in the situation to pay a much lower percent of profit as tax than the legal rate of 16%, with a significant negative impact on budgetary revenues. On the other side are the firms with low profitability rates and the firms with losses that are significantly disadvantaged by the **taxation on income system**. Starting with the main conclusions of the firm earnings taxation analysis, the following section sets out to estimate the impact on budgetary revenues of the changes on legal framework.

V. The impact of changes in the taxation of earnings on budgetary revenues

From the perspective of budgetary revenues, the receipts from corporate income tax are found within the “Taxes on income, profit and capital earnings from legal entities” chapter, which includes receipts from corporate income tax as well as from income tax on microenterprises, the latter accounting for most of the receipts in the subchapter “Other taxes on income, profit and capital earnings from legal entities”. Starting with 2017, the specific tax was introduced and it was included in the “Other Taxes” chapter, although it represents another way of taxing corporate earnings, replacing the corporate income tax for the categories of activities covered by it.

The budgetary revenues from the 2015-2017 period belonging to the “Taxes on income, profit and capital earnings from legal entities” chapter, together with their division on subchapters are found in *Table 8*:

Table 8: Budgetary revenues from taxes on corporate earnings between 2015-2017 (billion lei)					
Chapter/Subchapter	2015	2016	2017	Percentage change from previous year	
				2016/2015	2017/2016
Taxes on income, profit and capital earnings from legal entities:	14.75	16.35	16.11	10.84%	-1.46%
Corporate income tax, out of which:	13.77	15.39	14.69	11.78%	-4.57%
- Corporate income tax from firms in the non-financial sector	13.25	15.09	14.00	13.88%	-7.18%
- Corporate income tax from commercial banks	0.52	0.31	0.69	-41.44%	124.10%
Other taxes on income:	0.98	0.96	1.42	-2.35%	48.65%
- Income tax on microenterprises	0.87	0.83	1.32	-4.71%	59.10%
Specific tax*	-	-	0.1	-	-
The percentage change of nominal GDP from the previous year	-	-	-	7.37%	12.22%

Source: MPF, Eurostat

*The receipts from specific tax in 2017 belong only to the first semester of the year because the tax is due for payment in the first month of the following semester

In 2016, the proceeds from taxes on corporate earnings in Romania amounted to about 16.35 billion lei, up by 10.8% compared to the previous year. This evolution was supported by an increase of 11.8% in proceeds from corporate income tax (a 13.9% increase in the taxes paid by firms from the non-financial sector) while receipts from “Other taxes on income, profit and capital earnings from legal entities” decreased by 2.3%, being negatively impacted by the 4.7% drop in the income tax paid by microenterprises. It is worth noting that the increase in aggregate revenues was higher than the 7.4% dynamics of nominal GDP while also being about 1 billion lei higher than estimated in the initial budget.

In 2017, despite a 12.2% increase in nominal GDP, the receipts from “Taxes on income, profit and capital from legal entities” decreased by 1.5% because the proceeds from corporate income tax dropped by 4.6% (approximately – 700 mil. lei) and this negative evolution could not be offset by the 59.1% increase (around +490 mil. lei) in the income tax paid by microenterprises. Moreover, the amounts estimated to be collected from corporate income tax in the draft budget for 2017 proved to be more optimistic than the actual achievements by approximately 2 billion lei.

These developments are closely related to the extensive changes operated on the taxation regime of corporate earnings that were described in the first part of this study. Subsequently, employing the same microeconomic data as in the previous chapter, the impact of each fiscal policy measure on budgetary revenues will be evaluated *ex-post* and the result will be compared to the initial projection of budgetary impact. In addition, based on the data from the 2017 firm's financial statements, the impact of the changes in the taxation of corporate earnings that become applicable in 2018 will also be estimated.

Prior to determining the budgetary impact of fiscal policy measures that altered the taxation of corporate earnings in Romania during the 2015-2017 period, [Table 9](#) presents a selection of relevant indicators in order to assess if the sample of firms is representative for the analysis.

Table 9: Aggregate indicators for the sample of firms that was considered in the analysis			
Indicator	2015	2016	2017
Number of firms in the sample	464,277	497,242	513,420
% of firms with revenues <= microenterprise ceiling	64.8%	72.1%	90.1%
% of revenues generate by firms with revenues <= microenterprise ceiling in total economy	2.2%	3.3%	10.2%
Corporate income tax from the sample (mil. lei)	12,128.46	13,225.62	12,634.56
% of total corporate income tax paid by firms from the non-financial sector according to the budget execution	91.5%	87.7%	90.2%
Other taxes form the sample (mil. lei)	835.42	778.67	1,613.05
% of total income tax paid by microenterprises	96.1%	94.0%	122.3%
Total taxes from the sample (mil. lei)	12,963.88	14,004.29	14,247.60
% of total taxes on income, profit and capital earnings from legal entities according to the budget execution	87.9%	85.6%	88.4%
Total positive gross profit from the sample (mil. lei)	87,691.77	101,505.56	118,317.96
Percentage change of gross profit	-	15.8%	16.6%
Total operating income from the sample (mil. lei)	1,226,630.53	1,314,135.46	1,417,780.29
Percentage change of total operating income	-	7.1%	7.9%

Source: FC computations based on data from annual budget executions and from the financial statements submitted to MPF by firms from the non-financial sector

Thus, summing the amounts declared in the balance sheets in the account 691 “Corporate income tax” and comparing them with those from the budgetary execution for non-bank economic agents resulted in a coverage level of about 90%. Moreover, in the case of the receipts from microenterprises tax the correspondence between budgetary execution and the amounts declared in the account 698 exceeds 95%, with the mention that in 2017 the specific tax, found in the chapter “Other tax revenue” in budgetary execution, is also declared by the firms in this account, which explains the value over 100% from the table. Furthermore, there cannot exist a precise correspondence between the declared amounts by the firms in balance sheets and those from budgetary execution because of time differences between the moment when the tax is declared and its actual payment. **Another relevant element to note is that, despite the significant advance of the gross profits achieved by the firms with positive level of this indicator at aggregate level, respectively 15.8% in 2016 and 16.6% in 2017, the budgetary revenues did not follow this evolution, the aggregate “Taxes on income, profit and capital earnings from legal entities” increased by 10.8% in 2016 and decreased by 1.5% in 2017.**

In 2016, the fiscal measures regarding the modification of tax system on firms’ earnings were represented by:

- The differentiation according to the number of employees of the tax rate applied on microenterprises turnover (from a generalized rate of 3% in 2015), such that it has become 1% for the firms with at least 2 employees, 2% for the firms with 1 employee and 3% for those with no employees, concomitant with applying a tax rate of 1% for newly established microenterprises in the first two years of operation if they have at least one employee.

Generally speaking, the budgetary impact of a fiscal policy measure is determined by the difference between what would have been collected in the absence of the measure and what is being collected after the measure was implemented. To assess this impact, in the below table are presented data corresponding to the year 2016 regarding the firms with annual operating revenues between 0 and 65,000 euro at an aggregate level, as well as differentiated according to the number of employees.

Table 10: Financial data of the firms with annual operating revenue less 65,000 euro (mil. lei)					
Indicator	Year	Total	Number of employees		
			0	1	> 1
Number of companies	2015	300,681	101,156	107,271	92,254
	2016	321,761	109,879	115,720	96,162
Profit tax (account 691)	2015	104.2	35.8	32.1	36.4
	2016	72.2	27.0	24.2	21.0
Tax on microenterprises income (account 698)	2015	676.5	144.4	227.3	304.7
	2016	501.8	149.1	201.8	151.0
Total taxes (account 691+account 698)	2015	780.7	180.2	259.4	341.1
	2016	574.0	176.0	225.9	172.1
Total gross profit	2015	6,282.7	2,081.1	2,259.9	1,941.8
	2016	7,393.8	2,489.8	2,636.7	2,267.4
Total operating income	2015	27,418.0	6,013.4	8,892.8	12,511.8
	2016	29,650.1	6,407.8	9,660.1	13,582.2

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

At the aggregate level the tax on microenterprises revenue collected from this category of firms decreased in 2016 by almost 25.8% or 175 million lei, whereas the taxation basis, represented by the operating revenues advanced by 8.1%. Thus, the difference between what would have been collected, respectively higher taxes with this value and what was actually collected is of 230 million lei.

Analyzing differently depending on the number of employees, it is noticed how the budgetary impact of this measure comes from the companies with 1 employee (-50 million lei) and especially from those with 2 or more employees (-180 million lei).

- The increase of the annual income ceiling up to which a firm is considered microenterprise from the equivalent in lei of 65,000 euro in 2015 to the equivalent in lei of 100,000 euro in 2016.

Table 11: Financial data of the firms with operating income within the range 65,000-100,000 (mil. lei)					
Indicator	Year	Total	Number of employees		
			0	1	> 1
Number of companies	2015	31,000	3,504	5,658	21,838
	2016	36,954	4,023	7,194	25,737
Profit tax (account 691)	2015	140.9	22.9	33.2	84.8
	2016	62.2	11.0	16.1	35.1
Tax on microenterprises income (account 698)	2015	77.3	8.8	16.3	52.2
	2016	142.6	23.8	42.7	76.2
Total taxes (account 691+account 698)	2015	218.2	31.6	49.5	137.1
	2016	204.8	34.8	58.8	111.3
Total gross profit	2015	1,516.0	246.8	398.0	871.3
	2016	2,845.9	330.1	663.8	983.9
Total operating income	2015	11,331.5	1,268.3	2,035.6	8,027.5
	2016	13,680.5	1,478.2	2,637.7	9,564.7

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

At the level of firms with annual revenues in the above mentioned range this measure led to the reduction of the collected tax on earnings achieved by them (corporate income tax + tax on microenterprises income) from 218 million in 2015 to approximately 205 million lei, given that the aggregate revenues of the firms with earnings between the equivalent in lei of 65,000 euro and equivalent in lei of 100,000 euro increased by 20.7%. **In the same time, the cumulated gross profits of the firms with a positive value of this indicator from this category, increased by 87.7%, while at the level of whole economy these advanced by approximately 15.7%, the dynamics corresponding to all other groups of companies being close to the aggregate dynamics. In fact, in the year that it passed from the profit taxation to revenue taxation for this category of firms, the profits advanced spectacularly, which is suggesting a bringing out of supplementary profits without generating additional budgetary proceeds.** This idea is also supported by the evolutions

from 2017 when the aggregate profits of the firms with positive gross profits increased by 10.4%, whereas the revenues increased by 5%, value close to those recorded at the level of whole economy.

Table 12: The change of the positive gross profit and total operating income in 2016 for every category of firms according to operating income (%)					
	Operating income (euro)				
	Total	<= 65,000	€ (65,000; 100,000]	€ (100,000; 500,000]	> 500,000
Positive gross profit change (%)	15.8	17.7	87.7	11.5	14.6
Change of operating income for firms with positive gross (%)	7.1	8.1	20.7	4.4	7.2

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

Concerning the budgetary impact of this measure given by the difference between what would have been collected and what have been collected after the implementation, the evaluation is depending on the considered growth rate of the aggregate profit generated by the firms with a positive value of this indicator. If we consider what actually happened, respectively the profit's increase of 87.7%, the revenue loss would be about 150 million lei. Instead, **if we consider the situation in which the maintaining of the taxation system would have been accompanied by a profit increase similar to the one on the aggregate level of 15.7%, the loss of revenue is considerably reduced, respectively until a level of about 50 million lei. In this context, can be noted o revenue loss fall within the range 50 million lei – 150 million lei.** Considering the structure of budgetary revenues, this loss is equivalent to a minus of 100-200 million lei at the level of the tax on profit in conjunction with an advance of the tax on microenterprises revenues of 50 million lei.

At budget drafting from the year 2016, the budgetary impact for these two measures was assessed at almost -300 million lei. This evaluation was confirmed *ex-post*, except for the part related to bringing out previously untaxed profits, which however, did not generate additional budgetary revenues as a result of switching to income taxation for this category of firms. The increase from 2016 of the annual revenue ceiling up to which a firm is considered microenterprise led to the increase of the number of these firms by 19.3% compared to the previous year, respectively from a share of total firms included in analysis of 64.8% in 2015 to a share of 72.1%. **However, these changes have not modified substantially the ratio microenterprises - big firms from the economy and the budgetary revenues from the tax on firms' earnings were not severely affected.**

In 2017 the fiscal policy measures regarding the change of the taxation regime on earnings' firms were represented by:

- The reduction of the number of tax rates on turnover of the microenterprises to two, respectively 3% for those without employees and 1% for those with at least one employee. In fact, compared to the previous situation was eliminated the 2% tax rate for microenterprises with one employee. The measure was implemented from 1st February 2017, so it has affected the budgetary proceeds for 11 months from that year.

At the level of 2016 the firms with annual revenues less than equivalent in lei of 100,000 euro and with one employee have paid in the account 698 – the account where is reflected the tax on microenterprises revenue - about 244 million lei. **Considering the halving of the tax rate, the increase of the operating revenues of 1.28% registered in 2017 by the microenterprises with employees in those 11 months of measure implementation, the budgetary impact can be evaluated at -115 million lei.** The actual receipts from the year 2017 coming from the microenterprises' income tax for the firms with employees and revenues below the ceiling of 100,000 euro decreased to about 418 million lei from 472 million lei in the previous year. The slightly lower reduction than the assessment is not likely to invalid it as there may be grounds for such an evolution; for example, the case of those enterprises which in the first part of the year did not have employees and have paid a tax of 3% and which have ended the year with employees, a situation that would generate higher payments compared to the initial level of 1% on turnover.

Table 13: Financial data of the firms with annual operating income less than 100,000 euro in 2016 (mil. lei)					
Indicator	Total	Number of employees			
		0	> 0,	out of which:	
				1	> 1
Number of companies	358,715	113,902	244,813	122,914	121,899
Profit tax (account 691)	134.4	38.0	96.4	40.3	56.1
Tax on microenterprises income (account 698)	644.5	172.8	471.6	244.4	227.2
Total taxes (account 691+account 698)	778.8	210.8	568.0	284.7	283.3
Total positive gross profit	10,239.7	2,962.1	7,277.6	3,411.1	3,866.5
Total operating income	43,330.6	7,886.0	35,444.6	12,297.8	23,146.9

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

Table 14: Financial data of the firms with annual operating income less than 100,000 euro in 2017 (mil. lei)

Indicator	Total	Number of employees	
		0	> 0
Number of companies	366,026	122,253	243,773
Profit tax (account 691)	97.0	41.3	55.7
Tax on microenterprises income (account 698)	604.9	187.1	417.8
Total taxes (account 691+account 698)	701.8	228.4	473.5
Total positive gross profit	11,158.3	3,278.1	7,880.2
Total operating income	44,153.3	8,256.5	35,896.8

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

- The increase of the annual income ceiling up to a which a firm is considered microenterprise from the equivalent in lei of 100,000 euro in 2016 to the equivalent in lei of 500,000 euro in 2017. To evaluate the budgetary impact of this measure will be considered the indicators on the aggregate level of the firms with annual revenues between 100,000 and 500,000 euro. In fact, these firms shifted from the tax on profit - applicable to the firms with positive gross profit –to the taxation on operating revenues achieved.

Table 15: Financial data of the firms with annual operating income within the range 100,000-500,000 euro (mil. lei)

Indicator	Year	Total	Number of employees	
			0	> 0
Number of companies	2016	89,912	6,511	83,401
	2017	96,454	6,396	90,058
Profit tax (account 691)	2016	1,350.4	115.5	1,234.9
	2017	315.7	35.1	280.6
Tax on microenterprises income (account 698)	2016	92.4	13.3	79.1
	2017	775.9	63.5	712.5
Total taxes (account 691+account 698)	2016	1,442.8	128.8	1,314.0
	2017	1,091.6	98.6	993.0
Total gross profit	2016	10,345.8	1,042.6	9,303.1
	2017	15,985.3	1,349.1	14,636.2
Total operating income	2016	93,284.8	6,293.0	86,991.8
	2017	100,488.9	6,198.9	94,290.0

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

At the level of the firms with annual revenues falling within the above-mentioned range this measure led to the reduction of the receipts from the tax on their gains (tax on profit + tax on microenterprises revenues) from approximatively 1.44 billion lei in 2016 to 1.09 billion lei, in the context of an advance of the aggregate incomes of 7.7%. **In the same period, the cumulative gross profits of the firms with a positive value of this indicator increased by 54.5%, while at the level of the entire economy this raised by almost 16.6%, the afferent dynamics of the other groups of firms did not go up more than 7.7 pp from the dynamics at the aggregate level. Similar to the evolution from the previous year, also in 2017, when it shifted from the profit taxation to the revenue taxation for this category of firms, the profits advanced in a spectacular way, which is likely to suggest a bringing out of the profits, without generating supplementary budgetary revenues.**

Table 16: The change of the positive gross profit and total operating income in 2017 for every category of firms according to operating income (%)					
	Operating income (euro)				
	Total	<= 100,000	€ (100,000; 500,000]	€ (500,000; 1,000,000]	> 1,000,000
Positive gross profit change (%)	16.6	9.0	54.5	11.7	12.8
Change of operating income for firms with positive gross (%)	7.9	1.9	7.7	3.3	8.4

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

Similar to the year 2016, the budgetary impact assessment of this fiscal policy measure is different if we consider what actually happened, respectively the profit increase of 54.5%, the revenues loss being in this case of 1.05 billion lei. Instead, if we consider the situation in which maintaining of the taxation system would have been accompanied by a profit increase similar to the one from the aggregate level of 16.6%, the loss of revenue is considerably reduced, respectively to a level of about 550 million lei. **In these conditions it can be noted a revenue loss between 550-1,050 million lei.** Considering the structure of the budgetary revenues, this loss is equivalent to a minus of 1.25-1.75 billion lei at the level of the tax on profit in conjunction with an advance of the tax on microenterprises revenues of almost 0.7 billion lei.

When drafting the budget for the year 2017, the budgetary impact considered by the MPF for these two measures was evaluated at about -430 million lei, whereas the Fiscal Council has a different estimation, respectively an impact of -662 million lei. This last assessment is closer to what really happened, with the mention that the measure generated a bringing out of the previously untaxed profits, which however, did not generate additional budgetary revenues, as a

result of the switch to income taxation for this category of firms. **The increase in 2017 of the annual revenue ceiling up to which a firm is considered microenterprise led to the growth of the number of these firms of 28.9% compared to the previous year, from a share of 72.1% to a share of 90.1% of the total firms surveyed. On this time, both the ratio microenterprises -big firms from the economy, and budgetary receipts from the tax on firm earnings have been affected in a relevant way.**

- Starting with 1st January 2017 was introduced the specific tax which replace the corporate income tax for the firms which are operating in tourism, restaurants and public alimentation, the new tax having the characteristics of a lump tax and depending on many variables such as the rank of the locality where is located the branch, its surface or the seasonality. The microenterprises which are operating in these sectors are still paying tax on income. MPF, however, did not provided an estimate of the budgetary impact that this measure would generate.

An analysis of the budgetary impact of this measure will be carried out, respectively on the database at the level of 2017 regarding the firms with annual revenues higher than 500,000 euro because the specific tax is applicable only to firms from the above mentioned sectors which are profit tax payers. The analysis will be realized on the level of the entire economy and is challenging, on the one hand as a result of this aspect, but also as a result of the fact that specific tax is declared in the 698 account, which is the same as in the case of tax on microenterprises revenue, could not be made a differentiation between them. Should be mentioned also that the below analysis is realized under the uncertainties concerning the modification of the efficiency of the profit tax collection. A more detailed analysis based on the NACE codes is not possible because many large companies are operating activities corresponding to several NACE codes and therefore are paying a mixed tax.

To evaluate the budgetary impact of this measure, the firms with annual income above the ceiling of 500,000 euro, have been divided into two categories, respectively tax payers on profit (those which did not declared amounts into the 698 account) and firms which paid specific tax or mixed tax (those which declared amounts into the 698 account). Further, for these two groups were calculated the financial indicators relevant for the year 2016, previous to the implementation of the specific tax, to assess their time evolution. The results are presented in the following tables:

Table 17: Financial data of the specific tax payers or mixed tax payers in 2017 (mil. lei)				
Indicator	Year	Total,	out of which:	
			Gross profit	Gross loss
Number of companies	2016	7,620	6,471	1,149
	2017	8,160	7,393	767
Profit tax (account 691)	2016	487.3	476.6	10.8
	2017	431.1	422.0	9.1
Tax on microenterprises income (account 698)	2016	17.5	15.5	2.0
	2017	232.3	210.4	21.9
Total taxes (account 691+account 698)	2016	504.9	492.1	12.8
	2017	663.4	632.5	30.9
Total gross profit	2016	3,120.9	3,120.9	-797.5
	2017	6,040.5	6,040.5	-825.1
Total operating income	2016	41,119.6	37,923.8	3,195.8
	2017	58,317.5	53,029.4	5,288.1
<i>Average tax rate related to gross profit</i>	2016	21.73%	15.77%	-1.60%
	2017	12.72%	10.47%	-3.75%

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

Table 18: Financial data of the profit tax payers in 2017 (mil. lei)				
Indicator	Year	Total,	out of which:	
			Gross profit	Gross loss
Number of companies	2016	42,173	37,595	4,578
	2017	42,780	37,523	5,257
Profit tax (account 691)	2016	10,814.8	10,689.8	125.0
	2017	11,790.8	11,636.9	154.0
Tax on microenterprises income (account 698)	2016	28.0	27.6	0.4
	2017	-0.0076	-0.0076	0.0000
Total taxes (account 691+account 698)	2016	10,842.8	10,717.4	125.4
	2017	11,790.8	11,636.9	154.0
Total gross profit	2016	73,984.1	73,984.1	-17,001.3
	2017	85,133.9	85,133.9	-17,644.9
Total operating income	2016	1,085.4	957.5	127.9
	2017	1,214.8	1,074.5	140.4
<i>Average tax rate related to gross profit</i>	2016	19.03%	14.49%	-0.74%
	2017	17.47%	13.67%	-0.87%

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

In the case of the firms which are profit tax payers, in 2017 compared to the previous year the operating revenues increased by about 12%, the gross profits of the firms with a positive value of this indicator increased by 8.9%, and the average tax rate related to their gross profit decreased by 0.82 pp, respectively from 14.49% to 13.67%. In the case of the firms which paid specific tax or mixed tax, in 2017 compared to the previous year the operating revenues increased by about 41.8%, the gross profits of the firms with a positive value of this indicator increased by 93.5%, and the average tax rate related to their gross profit significantly decreased by 5.3 pp, respectively from 15.77% to 10.47%. There can be noted how the tax rate decreased much more for the specific or mixed tax payers firms, suggesting a favorable impact of the modification of the taxation system for these firms. Considering the difference of 4.48 pp regarding the reduction of the profit effective tax rate compared to the profit tax payers and applying this to the gross profit actually registered in 2017 it can be noticed that the revenue loss at the level of the general consolidated budget was approximatively 250 million lei. In the structure of budgetary receipts, the revenue loss can be associated to a minus of 450 million lei at the level of the revenue from corporate income tax concomitant with additional receipts from the newly-introduced specific tax of 200 million lei. It should also be mentioned that, at the moment when the specific tax was introduced, it was not expected that its implementation would generate a negative impact on the level of budgetary revenues.

During the year 2017, the evolution of the receipts from the taxation on profit raised many questions because, although the GDP evolution was strongly ascending, the sums collected amount to only 14.69 billion lei, respectively by 5% less than in 2016, also being with 2 billion lei lower than those from the initial budget draft. The above analysis suggests that the explanation for these evolutions is also tied to the adopted policy fiscal measures, the calculations indicating a cumulative minus of 1.7-2.2 billion lei at the level of the receipts from corporate income tax, compensated only partially by an increase of 0.5 billion lei at the level of the microenterprises revenues tax and an increase of 100 million lei at the level of specific tax⁸. From the estimated minus of 1.7-2.2 billion lei at the level of receipts from corporate income tax, it can be appreciated that only about 1 billion lei was considered in the initial budgetary construction.

⁸ Although the receipts from the specific tax corresponding to 2017 were estimated to almost 200 million lei, considering its collection in the month following the semester for which it is computed, the cash budgetary execution for the year 2017 includes only half of this amount.

In 2018 became operational a new increase of the annual revenue ceiling up to which a firm is considered microenterprise from the equivalent in lei of 500,000 euro to the equivalent of 1,000,000 euro.

Table 19: Financial data of the firms with annual operating income within the range 500,000-1,000,000 euro in 2017 (mil. lei) and relative change compared to the previous year			
Indicator	Total	Number of employees	
		0	> 0
Number of companies	22.196 (3.1%)	1.132 (0.4%)	21.064 (3.3%)
Profit tax (account 691)	806.9 (-21.3%)	43.1 (-28.6%)	763.8 (-20.8%)
Tax on microenterprises income (account 698)	134.9 (1560.5%)	9.0 (624.3%)	125.8 (1730%)
Total taxes (account 691+account 698)	941.8 (-8.8%)	52.1 (-15.5%)	889.7 (-8.4%)
Total gross profit	7,693.0 (11.7%)	461.0 (4.4%)	7,232.0 (12.2%)
Total operating income	71,844.4 (3.3%)	3,627.0 (1.3%)	68,217.4 (3.5%)

Source: FC computations based on data from the financial statements submitted to MPF by firms from the non-financial sector

In 2017, before the raising of the ceiling, the share of the collected tax on earnings in operating revenue was 1.31% for this category of firms and it is expected to fall below 1%, given that firms can opt to pay tax on profit if this option favors them. **By extrapolating for the year 2018 the dynamics actually registered by the relevant indicators in 2017 - respectively the positive gross profit and operating revenues – the budgetary receipts coming from the taxation of the earnings for these firms’ category would be around 1.05 billion lei, while from applying a tax rate of 1% on revenues would result in budgetary receipts of 800 billion lei. Thus, the budgetary impact of the ceiling increase in 2018 would be -250 million lei, compounded from a minus of 900 million lei at the level of profit taxation and a plus of 650 million lei at the level of microenterprises revenues taxation.** In practice, due to the transition from one tax system to the other and the difference between the moment of declaration and the moment of payment of the tax, the impact will be felt gradually in the period 2018-2019.

The budgetary impact of the fiscal policy measures that modified the corporate income tax regime during the period analyzed is summarized in *Table 20*, both separately for tax categories and for the general consolidated budget:

Table 20: The impact of the fiscal policy measures implemented during the period 2015-2018 on the proceeds of the general consolidated budget				
Year	Fiscal policy measures	Corporate income tax	Tax on microenterprises income and specific tax	Total General Consolidated Budget
2016	Differentiation of the tax rate according to number of employees	-	-230	-230
	Increase the annual income ceiling to 100,000 euro	[-100;-200]	50	[-50;-150]
2017	Reduction of the number of tax rate to two	-	-115	-115
	Increase the annual income ceiling to 500,000 euro	[-1.250;-1.750]	700	[-550;-1050]
	Introduction of the specific tax	-450	200	-250
2018	Increase the annual income ceiling to 1,000,000 euro	-900	650	-250

Source: FC computations based on data from annual budget executions and from the financial statements submitted to MPF by firms from the non-financial sector

VI. Conclusions

Between 2015 and 2018, there were considerable legislative changes in Romania related to the tax system for the companies' earnings that substantially changed the scope of firms included in the microenterprises' category, the tax rate applied to them and, implicitly, the budget receipts coming from this type of taxes. Thus, the **threshold for the annual income up to which a company is included in the microenterprises' category has been increased by more than 15 times between 2015 and 2018**, which is equivalent to the tax base shifting towards revenues rather than profits, while diminishing and differentiating the tax rates, based on the number of employees. In addition, for companies operating in hotels, restaurants, cafes, a specific tax was introduced, replacing the profit tax.

The present study had two major objectives, namely to identify the impact of legislative changes to the corporate income tax regime on the average tax rate and, also on the budget receipts.

As regards the tax rate on the companies' earnings in Romania, **the starting point was 2015** when the companies classified as microenterprises with positive gross profit were characterized by an **average tax rate of 9.3% while for the profit tax payers the level of this indicator was 15.1%**. Thus, microenterprises are generally advantaged compared to larger firms, as the 3% tax rate on revenue at that time generates lower taxation compared to their gross profit. However, this advantage is not evenly distributed amongst this category of companies. By analyzing the structure of microenterprises, the disadvantaged companies accounted for 60% of the total revenues for this category, out of which 29 pp represent the firms with losses and 31 pp are represented by the firms with a profit rate below the 18.75% indifference level. Under the hypothesis of taxing the profits for this category of companies with a tax rate equal to the average tax rate for profits of 14.65% in the period 2015-2016, **the amounts paid to the budget would have been higher by 18% or about 140 million lei.**

In 2016, following the legislative changes, the companies listed in the category of **microenterprises with positive gross profit were characterized by an average tax rate of 6.2%, while for profit tax payers the level of this indicator was of 14.2%**. Thus, at the aggregate level, the advantage of the tax regime for the microenterprises is increasing as compared to the previous year as a result of the reduction of the tax rates according to the number of employees. But again, this advantage is not evenly distributed among this category of companies. Analyzing the structure of microenterprises, the disadvantaged firms now account for only about 41% of the total revenues for this category, out of which 26 pp represent firms with losses and 15 pp represent firms with a profit rate below the level of indifference of 6.25%. Under the hypothetical

circumstances of taxing the profits for this category of companies, with a tax rate equal to the average tax rate for profits in the period 2015-2016 of 14.65%, **the amounts paid to the budget would have been higher by 93% or about 721 million lei.**

However, it should also be noted that **for companies with annual income ranging from 65,000 to 100,000 euro, who now become microenterprises, gross profits have advanced by 87,7%**, while at the level of the whole economy they have increased by approximately 15,7%, the dynamics of all other groups of firms being close to the aggregate dynamics. In fact, in the year when the taxation was shifted from taxing profits to income for this category of companies, their gross profits outstandingly increased, which is likely to suggest that **their profits were revealed but without generating additional budget revenue.**

In 2017, as a result of the legislative changes, the companies classified as **microenterprises with positive gross profit were characterized by an average tax rate of 5.6%, while for large companies the level of this indicator was 13.5%**. Thus, at the aggregate level, the microenterprises are again advantaged compared to the larger firms, but this advantage is not evenly distributed among this category of companies. By analyzing the structure of microenterprises, disadvantaged companies accumulate 44% of the total revenues for this category, out of which 19 pp are for firms with losses and 25 pp are for the companies with a profit rate below the level of indifference of 6.25%. Under the hypothetical conditions of taxing the profits for this category of companies, with a tax rate equal to the average tax rate for profits in the period 2015-2016 of 14.65%, **the amounts paid to the budget would have been higher by about 122% or by approximately 2.183 million lei.** This difference can also be explained by the uncovering of the extra profits for the new entrants in the microenterprise category, which recorded an increase of 54.5%, well above the 16.6% growth rate for the profits in the whole the economy. Moreover, in 2017, even the tax rate for the large companies' earnings, fell to 13.5% from 14.2% in the previous year, the reason being the introduction of the specific tax that led to a lower taxation for the companies that applied it.

Thus, on the background of the **successive increases of the income threshold for the microenterprises in the period 2015-2017**, about 90% of the analyzed companies have obtained operating revenues falling within this limit (an increase by about 25 pp or over 161 thousand companies of the size of the sample compared to 2015), and the contribution of this segment to the economic activity registered a spectacular growth: the aggregate operating income representing 10.2% of the total (compared with 2.2% in 2015) and the gross positive profits rising to 22.9 % (compared with 7.2% in 2015). Doubling in 2018 the annual income threshold up to which a firm is classified as a microenterprise will result in an even greater increase in these weights.

Assessing the costs and benefits of a simplified income tax system, such as the one based on the firms' income, is a challenge for the economic policy makers. On one hand, the intention to reduce the costs of accounting reporting and the setting of tax obligations, as well as those related to compliance with the regulations in force for small firms and to counterbalancing their limited access to financing compared to large firms should be analyzed in correlation to the relative disadvantage of applying the income tax system for the firms in the investment phase as well as with the ratio between those who lose and benefit in this tax system. At present, there are microenterprises that have greatly benefited from this system, but the ratio of beneficiaries - losers is relatively balanced. Moreover, budget receipts are negatively affected by this system, the taxation of profits being likely to generate significant additional budget revenues. Ultimately, the analysis should focus on the definition of the microenterprise, namely on the revenue threshold up to which a firm is considered within this category. A basic element of this analysis should be the extent to which the costs of accounting reporting and the setting of tax liabilities are constraining in relation to the annual revenues achieved by a firm.

Important consequences of the major changes in the corporate income tax system in Romania were registered at the level of the general consolidated budget. Thus, the number of profit tax payers has decreased considerably in the last 4 years, and the budget receipts have been negatively affected by amounts of 1.5-2 billion lei. The budgetary impact of these measures proved to be difficult to estimate *ex-ante* and the observed *ex-post* microeconomic data generally showed higher revenue losses than originally anticipated. This massive transfer from profit taxation to income taxation was achieved in a period of economic boom when the firms' profitability is high, which is likely to have increased the loss in the budget revenues. The succession of tax changes has also revealed extra profits for those firms that are now paying income tax, without generating additional budget receipts. Moreover, the possibility for companies to opt for profit tax or income tax allows companies to optimize their tax obligations, with additional negative consequences on the budget revenues.

A reversal of the income tax system for the firms with annual revenues of more than 100,000 euro, coupled with the removal of the specific tax and the strengthening of the fiscal control so that profits brought to light are taxed, could result in **additional amounts to the general government consolidated budget of over 2.5 billion lei.**