REVALUATION OF ASSETS - ACCOUNTING AND FISCAL IMPLICATIONS

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ABSTRACT: *Starting May 2009, revaluation reverts unknown for taxation, in terms of tax the profit. This new tax rule shapes again the accounting behaviour. Thus, it is likely that most firms with revalued assets to choose for transfer from revaluation reserve from account 105 "Revaluation Reserves "into account 1065 "Reserves representing surplus achieved in the revaluation reserve" as damping assessed property depreciation, and not to remove it from book-keeping.*

KEY WORDS: *revaluation of fixed assets, current accounting, fiscal applications*

1. THEORETICAL ISSUES RELATED TO THE REVALUATION OF FIXED ASSETS

Revaluation issues represent the difference between the actual value or fair value accounting and the accounting value of items submitted for review, except tangible assets that have an important share of the patrimony active.

• ***Further evaluation to initial recognition***

After the initially accounting as asset, tangible assets must be accounted to his *cost decreased by accumulated depreciation*. IAS 16 standard makes from the assessment processing *the reference (base).* Alternative processing (other processing allowed) is revaluation, in which tangible assets must be charged to the value reassessed (revalued amount), of its *fair value on revaluation*, less subsequent accumulated depreciation and subsequent accumulated losses of value. *Revaluations* must be made with sufficient regularity so that the accounting value does not differ significant from those which were determined using the fair value on the closure of financial year.

The fair value of land and construction is naturally determined by qualified experts. This fair value is generally the market value.

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The fair value of the production facilities is usually determined by their market value estimated. For strictly specialized tangible assets species which are not subject to regular transactions, fair value is identified, most times, with replacement cost, less depreciation.

Frequency of revaluation depends on fluctuations in fair value of tangible assets were assessed. When the fair value of a revalued asset differs significantly from its accounting value, it is necessary a new review. Some tangible assets could know important developments and unsteady of their fair values, reason for requesting an annual review, clearly such frequent reassessment are not required for minor developments tangible recording of their fair value, in this case is sufficient/enough review every three to five years.

An asset can' be revaluated in isolation. Reassessment should apply *to all goods of the same class*, in the other hand, on all such assets and use the same. Land, buildings, machinery, equipment, vessels, aircraft, motor vehicles, office fixed assets represent different categories of assets which can be revalued independently of one another.

In principle, all the goods of that class must be reassessed simultaneously in order to avoid too great a disparity in the assessment of various items in the financial statements. When the carrying amount of an asset increases, following a revaluation, the increase has the effect of *increase equity* in case of *revaluation reserves* in extent offset a positive revaluation of that asset a negative review previously charged to expense positive revaluation should be charged to income. When the carrying/accounting amount of any asset is reduced, following a revaluation, the revaluation must be accounted *as expense*. However, it is a negative revaluation reserve is directly attributable to the revaluation corresponding to the extent such reduction does not exceed the size of the revaluation reserve relating to the same asset.

Revaluation reserve included in equity may be transferred directly to other retained earnings when the revaluation reserve is done the entire revaluation reserve is undertaken during decommissioning of the asset or transfer. However, some of the revaluation can be implemented, as the asset is used by the enterprise, in this case, the size of the revaluation reserves made the difference between depreciation based on revalued carrying amount of the asset and depreciation based on cost entry of the asset. Transfer from revaluation reserve to retained earnings does not pass through the income statement.

In order to account revaluations of tangible assets are using one of two processes: the process no.1: simultaneous re-evaluation of gross values and accumulated depreciation; the process no. 2: a reassessment only to net accounting value, determined by deducting depreciation from the cost of property.

2. EXAMPLES OF FISCAL AND ACCOUNTING MECHANISMS OF RECOGNITION THE CURRENT PROPERTY/ASSETS REVALUATION

We assume that in December 2004, the company operates a device whose input value is 360,000 lei and is amortized linearly to 10 years (annual depreciation is thus of 36,000 lei). According to accepted tax and accounting rules, depreciation is calculated from

January 2005. Assume that at the end of 2007 (after the entry into force of OMFP no. L.752/2005), the company decided to apply the fair value model for equipment with due and that on that date, the fair value amounts to 311,500 lei.

In this example we opt for the procedure to cancel the yearly accumulated depreciation and adding the difference in net book value before revaluation.

The calculations necessary for accounting revaluation are:

• the recording value (balance account of equipment): 360,000 RON;

• accumulated depreciation for the financial years 2005, 2006 and 2007: 36,000 x 3 = 108,000 Ron;

• net accounting value: 360,000 to 108,000 = 252,000 Ron;

• fair value was set at 311,500 Ron;

• clear difference in revaluation: 311,500 to 252,000 = 59,500 Ron.

The accounting record is easy to achieve:

- Cancellation of existing depreciation:

2813 “Depreciation of plant, motor vehicles, animals and plantations”	=	213 “Technical installations, vehicles, animals and plantations”	108,000

- Adding the net difference from revaluation to net accounting value :

213 “Technical installations, vehicles, animals and plantations”	=	105 “Revaluation reserve”	59,500

After these records, the account balance, that interest us are:

• Account balance 213 “Technical installations, vehicles, animals and plantations” 311,500 Ron (equal to fair value)

• Account balance 2813 “Depreciation of facilities, vehicles, animals and plantations” 0 (it cancelled the review)

• Account balance 105” Revaluation Reserves” 59,500 Ron

After re-evaluation, the depreciation is calculate again for the following year, like ratio between the amount remaining and the period remained (311,500 - 0) / 7 = 44,500 lei / year in 2008, the deductible depreciation expense of such equipment is 44,500 lei, equal to the expense accounts (we consider the fiscal rules described above). We simplify the example considering that we record only once the depreciation in 2008:

6811 “Operating expenditure of depreciation”	=	2813 “Depreciation of facilities, vehicles, animals and plantations”	44,500

However, we opt for the disposal of revaluation reserve on depreciation measure, which means that virtually assigned revaluation reserve on the remaining seven years of life: 59,500 / 7 = 8500 lei/year:

105 “Revaluation reserves “	=	1065 “Reserves representing surplus achieved in the revaluation reserve “	8,500

The amount made available in 2008 is not taxable (is not changed, in fiscal mean, the purpose reserve), which means that the revaluation has the fiscal advantage of additional expenditure deduction with depreciation exactly equal with 8,500 Ron (44,500 -36,000 = 8,500 Ron).

We further suppose that the company take the revaluation and that on 31.12.2008, the fair value is 299,520 Ron:

• the value registration (account balance of equipment): 311,500 Ron;

• accumulated depreciation: 44,500 Ron;

• net accounting value: 311,500 – 44,500 = 267,000 Ron;

• fair value: 299.520 Ron;

• clear difference in revaluation: 299,520 – 267,000 = 32,520 Ron.

The account registrations are:

- Remove the existing depreciation:

2813 “Depreciation of facilities, vehicles, animals and plantations”	=	105 “Revaluation reserves”	44,500

- Adding the net difference in net value accounting review

213 “Thermal installations, vehicles, animals and plantations”	=	105 “Revaluation reserves”	32,520

Thus, after the revaluation of 31.12.2008, account balances are:

• Account balance 213 “Plant, vehicles, animals and plantations” 299,520 Ron (again equal to fair value)

•Account balance 2813 “Depreciation of plant, vehicles, animals and plantations” 0;

• Account balance 105 “Revaluation Reserves” from 59,500 – 8,500 + 32,520 = 83,520 Ron.

Depreciation expense in 2009 is (299,520 - 0) / 6 = 49,920 lei (49,920/12 = 4,160 lei per month), expenditure deductible under normal conditions, while the difference from revaluation will be made available and it will be 83,520/6 = 13,920 Ron (1,160lei/ month).

However, in 2009, starting from May, revaluation reserve becomes taxable, which means that we have two periods in 2009 for tax purposes:

• until April including:

- deductible depreciation expense: 4,160 x 4 = 16,640 Ron;
- revaluation difference dismissed: 1,160 x 4 = 4,640 lei allowance;

• from May until December:

- deductible depreciation expense: 4,160 x 8 = 33,280 Ron;
- revaluation difference dismissed: 1,160 x 8 = 9,280 lei, taxable amount.

Thus, in the aftermath of the fiscal code changes, the net deduction is 33,280-9,280 = 24,000 lei, exactly how it was if there were no revaluated: 36,000 x (8/12) = 24,000 lei. To facilitate registration, is very useful that in the account 1065 “Reserves representing surplus achieved in the revaluation reserve “to go on the analytical accounts, in which is separate the taxable amounts from the untaxed amount of tax so that when change the reserve destination is known easily how must be taxed and which part must not to be taxed.

We continue the example, in order to highlight other aspects of accounting and fiscal aspects of revaluation, such us what would happen if the fair value would become smaller than the net accounting value before revaluation. For this, we suppose that the fair value at 31.12.2009 reaches 222,000 lei, so that:

- recording value (equipment account balance): 299,520 Ron;
- accumulated depreciation/amortization: 49,920 Ron;
- net accounting value: 299,520 - 49,920 = 249,600 Ron;
- fair value: 222,000 Ron;
- net difference in revaluation: 222,000 – 249,600 = -27,600 Ron

Revaluation difference is negative and is in fact an impairment. For accounting depreciation balance we need to check what balance we have to 105 account "Revaluation reserves" 83,520 -13,920 = 69,600 Ron. This balance is sufficient to cover depreciation found at 31.12.2009:

- Cancelling the existing depreciation:

2813 "Depreciation of facilities, vehicles, animals and plantations"	=	213 "Technical installations, vehicles, animals and plantations"	49,920

- Decreased net revaluation difference from net accounting value:

105 "Revaluation reserves"	=	213 "Technical installations, vehicles, animals and plantations"	27,600

Account balances reach to:

- Account balance 213 "Plant, vehicles, animals and plantations" 222,000 lei;
- Account balance in 2813 "Depreciation of facilities, vehicles, animals and plantations" 0;
- Account balance 105 "Revaluation reserves" from 83,520 – 13,920 – 27,600 = 42,000 Ron.

For 2010, the depreciation expense amounted to the level of (222,000 - 0) / 5 = 44,400 lei - deductible expense, while the stocks last taxable amount reached 42,000 / 5 = 8,400 lei. Once again is verified that the net deduction is at the depreciation level that would be calculated if there was no revaluation: 44,400 – 8,400 = 36,000 lei.

Assume at 31.12.2010 a fair value in amount of 127.000 Ron :

- recording value (account balance of equipment): 222,000 Ron;
- accumulated depreciation: 44,400 Ron;
- net accounting value: 222,000 – 44,400 = 177,600 Ron;
- fair value: 127,000 Ron;
- clear difference in revaluation: 127,000 – 176,600 = -50,600 Ron;
- differences from revaluation account balance: 42,000 – 8,400 = 33,600 Ron.

Impairment is greater than the revaluation of difference remained in balance, which means that if exhaustion revaluation difference will remain a part of depreciation that will be registered on expenses:

- Cancellation of the existing depreciation:

2813 "Depreciation of facilities, vehicles,	=	213 "Technical installations, vehicles,	44,400

animals and plantations” animals and plantations”

- Decreased net revaluation difference from net accounting value:

105	=	213	33,600
“Revaluation reserves”		“Technical installations, vehicles, animals and plantations”	

• Switching on expense the part of depreciation not covered by existing revaluation difference: 50.600 – 33.600 = 17.000 lei:

6813	=	2913	17,000
“Operating expenses for depreciation adjustment assets”		“Adjustments for depreciation of facilities, vehicles, animals and plantations”	

Balance accounts, after the records from 31.12.2010, are as follows:

• Account balance 213 “Plant, vehicles, animals and plantations”: 222,000 – 44.400 -33.600 = 144.000 Ron;

• Account balance 2813 “Depreciation of installations, facilities transport, animals and plantations“: 0,

• Account balance 105 “Revaluation reserves” 0;

• Account balance 2913 “Adjustments for depreciation facilities, vehicles, animals and plantations”: 17,000 Ron.

As the tax point of view, depreciation expense adjustment for property is not deductible when is calculate the income tax. This recognition of the depreciation of property tax is therefore interesting. We take again a new rule established in the fiscal code: if following the revaluation net new accounts that fall below the value would be reached only through depreciation of cost of acquisition or production, then the fiscal amount remaining outstanding shall be recalculated depreciation of fixed assets to the level of value based on initial input.

Translation of this rule is: in the event of a depreciation of fixed assets, depreciation expense after tax is equal to the depreciation would be calculated if there is any impairment. This is exactly the depreciation tax depreciation calculated on the basis of input (in our case, the acquisition cost of 360,000 lei), in these conditions, the calculations for depreciation in 2011 may be presented as follows:

• tax depreciation: 360,000/10 = 36,000 lei, or remaining fiscal amount reported in the remainder period (360,000-6 x 36,000)74 = 36,000 lei;

• calculate depreciation expense reporting accounting book value remaining to the remainder period (DR):

$$\frac{\text{sold 213-sold 2813-sold 2913}}{\text{DR}} = \frac{144.000\text{-}0\text{-}17.000}{4} = \frac{127.000}{4} = 31.750$$

Once you can see that if by the end depreciation would not record any review (positive or negative), then the accumulated depreciation account balance in 2813 “Depreciation of facilities, vehicles, animals and plantations “ would reach 4 x 31,750 = 127,000 lei, the account balance amount less than 213 “Plant, vehicles, animals and plantations “ (144,000 lei). However, Romania does not support the retention of residual values for depreciable property, which means that at the end of the depreciation, accumulated depreciation (account balance in 2813 “Depreciation of facilities, vehicles, animals and plantations”) must equals record value (account balance 213 “Plant, vehicles, animals and plantations”). To ensure that equality is necessary, since 2011, the credit in 2813 “Depreciation of facilities, vehicles, animals and plantations” to record 144,000/4 = 36,000 lei, and not 31,750 lei, as we saw that accounting expense amortization is.

The accounting article for depreciation record will appear as so:

%	=	2813	36,000
6811 “Operating expenditure of depreciation”		“Depreciation of facilities, vehicles, animals and plantations”	31,750
2913 “Adjustments for depreciation of facilities, vehicles, animals and plantations”			4,250

The amount of 4,250 lei that we fell for the impairment adjustment resulting from the distribution just on four years of adjustment recognized in late 2010: 17,000/4 = 4,250 lei. Summarize the situation in year 2011:

• accounting depreciation expense is 31,750 lei;

• tax depreciation expense is 36,000 lei;

• the amount recorded as depreciation is credited to the specific account of 36,000 lei.

3. CURRENT ACCOUNTING AND FISCAL APPLICATIONS IN ASSETS REVALUATION

Revaluation of assets is an option with significant accounting and fiscal implications. Revaluations that were required or which companies may wished to be recognized in 2003 were fiscal recognized and thanks to the obvious connection of Romanian accounting with the fiscal system, in present Romanian accounting rules are no longer aligned, at the level of principle, after the fiscal ones. This raises the possibility of depreciation accounts differ from tax records of it. When we say that differences arise, we refer to all three elements necessary to establish depreciation: the amortized amount, period of depreciation, amortization schedule. Moreover, current fiscal code is clear in this respect: the accounting expense depreciation is entirely non-deductible, following that fiscal deduction will be recognized on fiscal deductions. In this general framework of depreciation of assets, the revaluation is also located. However, we allow ourselves to suppose (without empirical confirmation) that to many Romanian enterprises (especially SMEs) accounting and fiscal evidence of depreciation are often identical.

This is due to the need for simplification. Some accountants believes - rightly, we tell- that there would always justify keeping different records regarding property, so they are retained in the accounts those elements valid for fiscal purposes in respect of revaluation, fiscal implications arise not only from income tax but also, for example, the tax on buildings: we know that local authorities require a much higher tax rate for those buildings which have not been revalued in the last three years, so that option revaluation of buildings is particularly timely. Revaluation accounts, as it is previewed in OMFP no.752/2005 it, takes many of general rules available in IAS / IFRS. This takeover is complete, which may lead to less bizarre situations such as the revaluation of fully depreciated fixed assets.

Another consequence of the revaluation is that if fair value falls below the net value that would be reached without revaluation, then the calculation of depreciation becomes more difficult, in that we have at least two rows of sums: amortization expense, calculated as relation between remaining value and the left duration on the one hand, and amortization of past credit amending account, set up so that at the end of depreciation, account balance restraining is equal to account balance of accumulated depreciation.

In terms of tax, in 2009 there are two periods:

- up to April 2009 inclusive, during which the revaluation is recognized for tax purposes, provided they have been made under the law and without obligation to tax revaluation reserve until the next change of it’s destination;
- in May 2009, depreciation expense from revaluation results is further fiscal recognized, but the revaluation reserve becomes assimilated to taxable income as recognition of that respective depreciation/amortization.

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