LEGAL UPDATE

POPOVICI & ASOCIAȚII
Attorneys at Law

47 Alexandru Constantinescu St,
Bucharest, 1st District, Code 011472
Romania

Telephone: (0040) 21 224 79 19
Fax: (0040) 21 224 60 59 / 224 75 05

office@popovici-partners.ro
www.popovici-partners.ro

NOVEMBER 2004

NUMBER XI

IN THIS ISSUE:

FISCAL CODE

BANKING LAW

CIVIL PROCEDURE

REAL ESTATE PUBLICITY

PRIVATELY ADMINISTERED PENSION FUNDS

TEMPORAL MARK

LEGAL UPDATE

FISCAL CODE

Amendment of the Fiscal Code

The Law on the approval of the Government Ordinance no. 83/2004 amending and completing the Fiscal Code was recently adopted (Law no. 494/2004) and the Government Emergency Ordinance no. 123/2004 amending this law.

The enactments above mentioned shall enter into force on January 1st, 2005 at the same time with the other amendments and completions of the Fiscal Code set forth in the Government Ordinance no. 83/2004.

The main amendments and completions of the Fiscal Code, with significant and immediate consequences on the taxpayers, are as follows:

Regulation of the transactions with inactive taxpayers

The new law provides that the president of the National Fiscal Administration Agency is entitled to issue orders declaring certain taxpayers as inactive. The declaring procedure shall be established by an order and the list of inactive taxpayers shall be published in the Official Gazette.

The Fiscal Authorities are entitled not to take into account the transactions concluded by the inactive taxpayers.

Moreover, they shall not take into account the transactions concluded by other taxpayers with inactive taxpayers and shall consider non-deductible the expenses based on a document issued by an inactive taxpayer.

In this respect, it was provided that the beneficiaries of an invoice issued by an inactive taxpayer cannot deduct the value added tax (VAT) indicated in the respective invoice.

Regulation of the contract with payment in instalments

For the amounts obtained from the contracts with payment in instalments, the taxpayer may choose that the income related to the contract be taken into account when setting the profit in proportion as the instalments reach the maturity date.

Correspondingly, the expenses related to this income shall be deducted at the same maturity dates, in proportion with the amount of the respective instalment as compared to the contract total value.

Increase of the deductibility level of the interest expenses

The new legal provisions provide that the taxpayer's interest expenses are fully deductible if their indebtedness ratio is equal or less than three.

The indebtedness ratio is defined by the law as the ratio between the loans payable within more than one year and the own capital.

This amendment is significantly advantageous for the taxpayer, as the

previous indebtedness ratio up to which interest expenses were fully deductible was equal or less than one.

Extension of the exemption period from payment of succession duties

The exemption term from payment of succession duties, previously set to January 1st 2005, was extended up to December 31st 2005.

Therefore, the succession duty is not due if the succession procedure was concluded within one year from the death of the owner of the goods or, for the owners deceased before January 1st 2005, if the succession procedure was concluded before December 31st 2005 included.

Reduction of duties relating to notarisation of certain legal deeds concluded over lands

Upon the new legal provisions the stamp duties value due for notarisation of legal deeds concluded *inter vivos* whereupon is transferred the ownership right or other real rights over lands without constructions has been reduced to half.

Amendment of the methodological norms for applying the Fiscal Code

The methodological norms for applying the Fiscal Code, approved by Government Decision no. 44/2004 (the "Methodological Norms") have been recently amended and completed by the Government Decision no. 1.840/2004 (Official Gazette no. 1.074/18.11.2004).

This decision mainly clarifies the interpretation and application of the articles in the Fiscal Code.

Restrictive interpretation of the scope of dividend tax

The Fiscal Code provides for that distribution of assets by a Romanian legal entity to its shareholders, either as dividends or subsequent to the liquidation procedure, represents taxable transfers.

In this sense, the Methodological Norms list the elements that trigger the obligation to withhold and pay the dividend tax (thus including them in the category of dividend distribution), namely:

- share capital increased by using own capital financing (differences resulted from evaluation of fixed assets and stocks, amounts registered as reserves from exchange rate differences etc.);
- own capital established from gross profit, according to the legal provisions (legal reserves, profit tax reduction or exemption for reinvested profit etc.);
- own capital established in accordance with the legal provisions, the capital amounts not having been previously qualified as income (differences due to evaluation, differences of exchange rate, differences due to application of the reduced quota for exportation, subsidies for investments etc.).

As compared to the previous version, the profit resulting from the company liquidation is excluded and thus is no longer subject to dividend tax.

Limitation of the scope of application of royalty tax relating to know-how agreements

The new provisions set the limits within which royalties under know-how agreements should be assessed, depending on whether or not the know-how supplier is involved in applying the transferred knowledge.

Thus, it is considered a royalty and therefore accordingly subject to taxation, the amount received under a know-how agreement according to which the supplier agrees to share its expertise with the buyer, so that the buyer can use it to its own interest and not to disclose it to the public.

In this case, the law sets forth that the know-how provider should not play any role in implementing the knowledge granted to the buyer and should not guarantee the results of the implementation thereof.

Otherwise, in case of the conclusion of a service supply agreement under which one party undertakes to use its knowledge in order to carry out a certain work in favour of the other party, the amount received by the supplier is not considered to be a royalty and shall be subject to profit tax.

Methods to exercise fiscal authorities' assessment right

The Fiscal Code sets forth that the fiscal authorities, pursuant to their assessment right, may refuse to take into account certain transactions on the grounds that they have no economic purpose, may redefine their legal nature in accordance with their economic content or may adjust the incomes of the taxpayers as regards transactions between affiliated parties.

With a view to establish certain concrete ways to exercise this right and to limit the possible abuses of the control bodies, the Fiscal Code introduced, as methods to establish the real price of the transactions, the prices comparison, the cost-plus method and the resale price method.

It also set forth the possibility of the fiscal authorities to implement other methods established by the Cooperation and Economic Development Organisation.

In order to complete these provisions, the new provisions of the Methodological Norms further detail the operations carried out upon each method and set forth that out of the methods provided by the Cooperation and Economic Development Organisation in this respect, only the net margin method and the profit split method may be implemented.

Following a brief analysis of these methods, we should note that their implementation mainly entails the following:

(i). **Prices comparison method**

This method involves the comparison with the prices for similar transactions agreed by affiliated parties in relation with independent parties (internal comparison) or with the prices agreed by independent parties (external comparison).

(ii). **Cost-plus method**

By implementing this method, the setting of the price involves the increase of manufacturer or service provider costs with a profit margin corresponding to the business scope of the tax payer.

(iii). **Resale price method**

This method involves that the price of a product is set by calculating the price obtained for it in case of resale to an independent party, minus the sale expenses and other operation costs.

In setting the operation costs, are taken into account the assets used and the risk taken, as well as ensuring of an appropriate profit for the taxpayer.

(iv). **Net margin method**

Based on this method is carried out a comparison between the profit obtained by a party under the transactions with affiliated persons and the profit obtained by the same party under transactions with independent parties or in similar transactions concluded between independent parties.

(v). **Profit split method**

This method is used when it is impossible to identify transactions similar to those concluded by affiliated parties.

The calculation method involves the estimation of the profit obtained by affiliated parties under one or more transactions and the split of the profits among them, in proportion with the profit that would have been obtained by independent parties.

BANKING LAW

Amendments to the Banking Law

In keeping with Romania's endeavours to implement the *acquis communautaire* in the field of Free Movement of Services, following the amendment of the Banking Law no. 58/1998 in December 2003, new amendments became necessary, especially in order to entirely reflect the Directive 2000/12/CE relating to the taking up and pursuit of the business of credit institutions, entered into force by the recent Law no. 443/2004, published in the Official Gazette no. 1035 of November 9th, 2004.

Most amendments are linked to Chapter XIV[2] – "Member States" or to other provisions of the Banking Law regarding the status of the credit institutions in the European Union, including with respect to authorisation and operational requirements, provisions that shall anyway come into force at the time of Romania's accession to the EU and that aim to define such institutions against the credit institutions outside the European Union.

This amendment also resulted in the express insertion within the Banking Law of the requirement regarding the minimum level of the initial capital for a credit institution, set as the equivalent in national currency of EUR 5 million.

The Community regulations were also observed as regards the assessment of the requirements for authorising a credit institution and the conditions existing on the market (*economic need test*), the National Bank of Romania having the right to reject a request for authorisation upon assessment of the documents submitted considers that the bank cannot fulfil the objectives proposed, under such conditions as efficiency of the banking system and compliance with the rules of prudent banking practice so as to ensure the protection of the depositors and other creditors.

CIVIL PROCEDURE

Regulation of administrative actions to avoid court overloading

Following a recent amendment of the law on courts' certain subject matters jurisdiction and given the overloading of Romanian courts it was time for a new regulation to ease the work of the High Court of Cassation and Justice and of the courts of appeal.

Thus, by way of exemption from the Civil Procedure Code rule according to which the lawsuits in pending when the due courts' subject matter jurisdiction is amended shall proceed before the same courts, the Law no. 917/2004 on the approval of the Government Emergency Ordinance no. 65/2004 sets forth that, for the subject matters in which the courts' jurisdiction underwent amendments, all intermediate appeals pending with the courts of appeal at the Law entry into force date should be referred to lower courts and all final appeals pending with the High Court of Cassation and Justice at that time should be referred to the courts of appeal.

Moreover, the procedure of disputing jurisdiction shall be executed by means of irrevocable judgement, by way of exemption from the general legal framework that allows filing of the recourse against such judgements.

REAL ESTATE PUBLICITY

Following the extensive amendment of Law no. 7/1996 on the general cadastre and real estate publicity in May 2004 by the GEO no. 41/2004, aimed at organising a sole structure to coordinate the cadastre and real estate publicity activity, the recent Law no. 499/2004 on the approval of the said emergency ordinance sets forth certain amendments as well outlined below.

Thus, whereas initially it was set that any registration with the land book regarding the ownership right or other real rights over a real estate shall be performed exclusively based on a notarised deed, the Law no. 499/2004 amends this provision in the sense that the deeds necessary for the registration may either be notarised deeds or deeds issued by a public authority.

The Law no. 499/2004 also regulates another aspect regarding the notarisation of the deeds constituting, modifying or ceasing a real estate right, the notary public being bound to request, as the case may be, either

a land book excerpt or a certificate of charges. During the validity period of the land book excerpt it is forbidden to perform any registration except the one for the purpose of which the excerpt has been issued.

PRIVATELY ADMINISTERED PENSION FUNDS

Keeping with the efforts to improve the public pension system, the regulation of the optional occupational pension schemes was followed in November by the Law no. 411/2004 on privately administered pension funds (Official Gazette no. 1033), which shall enter into force on July 1st 2006.

The new Law sets forth the operation principles of a privately administered pension system, regulates its set up, organisation, operation and prudential supervision as well as the activity of the entities involved in this field.

The mechanism of the private pension system

The system provided by the Law no. 411/2004 supposes compulsory contributions to a privately administered pension fund, approved by the Supervision Commission of the Pension Funds (the "Commission"), from a number of categories of persons, insured within the public pension system.

This obligation is incumbent on persons up to 35 year-old that have taken out such insurance for the first time and that contribute to the public pension system; the contribution is optional for persons up to 45 year-old already insured and who contribute to the public pension system.

As per the said Law, privately administered pension funds are set up under a civil society agreement, concluded between at least 100 founding members and having at least 50,000 participants.

Administration of private pension funds

Private pension funds can only be administered by a joint stock company the exclusive business scope whereof is administration of pension funds and, optionally, providing private pensions, with a minimum share capital of 5 million euros (the equivalent in ROL thereof), entirely subscribed and paid-in, exclusively in cash, at the incorporation date.

The managing company is subject to authorization procedures conducted by the Commission before the setting-up (prior authorization), as well as before the commencement of the management activities (operational authorization), but also to prudential and transparency regulations, under the legal provisions.

The Commission is to be established by January 1st 2007, following the separation of a department from the Insurance Supervision Commission and shall have extensive regulatory, coordination and control powers over all entities involved in the field of privately administered pensions.

For the custody of the assets in the pension fund, the managing company may appoint a

sole credit institution – a Romanian legal entity or a branch of a foreign credit institution – that shall have the capacity of custodian and shall have to be approved by the Commission before the commencement of the activities. A sole custodian may keep the assets of several pension funds, provided that it records the operations and registrations of each pension fund separately.

Financial resources of the pension funds and status of the contributions

Financial resources of privately administered pension funds consist of participants' contributions, as well as of the amounts resulted from their further investment. The contributions to the privately administered pension funds, to be collected starting only with January 1st, 2008, shall have the same legal status as the contributions to the public pension system as regards the setting up, transfer and deduction from the gross income.

The legal status of the account of each participant is protected by imperative norms; thus, the Law no. 411/2004 sets forth that the participant owns the personal assets in its account, assets that may neither be assigned nor pledged and that can not be subject to enforcement or transaction, subject to cancellation.

Rights of the participants to privately administered funds

When meeting the retirement requirements for age limit under the public system, the paid contributions grant to the participant the right to a private pension. Under the Law, the right to a pension does not disappear if the participant changes job, domicile or residence in another country. The pension shall be paid in the respective state in the amount remaining after deducting all fees and expenses related to the payment.

Moreover, as from the retirement date for invalidity due to affections preventing the resuming of work, as defined under the general applicable rules, the participant may receive either a sole payment or a payment by instalments for a duration of maximum 5 years, or a private pension if his net personal assets are sufficient enough.

Within 2 years from the date when the Law no. 411/2004 comes into force, the Parliament shall decide on how the pension provider shall be authorised and organized, how it shall operate, on the categories of privately administered pensions, on the way they are set up and granted as well as on the Commission's competences in these fields.

TEMPORAL MARK

As a natural continuation of the Law on the electronic signature, a new enactment designed to facilitate the development of the electronically available services shall come into force at the beginning of December 2004. The Law no. 451/2004 on the temporal mark regulates the legal status of the temporal mark and its providing requirements.

The main points of the Law no. 451/2004 refer to the structure of the temporal mark,

its use, parties' obligations and systems' safety, provisions inspired from the applicable European directives.

The temporal mark is defined as a set of techniques enabling each person to locate the precise moment when a certain electronic document was drafted or signed, to receive a digital certification from the temporal mark service provider regarding the existence of an electronic document at a certain moment.

This enactment may be used especially for checking an electronic signature set on a document, the validity of the electronic signature certificate, for online auction systems or for firmly dating the works protected by copyright.

The persons interested in supplying temporal mark services shall notify the authorities, 30 days before starting to issue temporal marks, the date when they begin their activities and shall provide a series of information and documents provided by the Law no. 451/2004. Among these documents, there are: (i) the qualified certificate based on which the signature on the temporal mark may be checked; (ii) the policy regarding the protection of personal data, in accordance with the Romanian laws in force; (iii) any other information regarding the activity of providing temporal mark services required by the competent authority.

The providers of temporal mark services shall also have the obligation to create and maintain an operative electronic register indicating the time when the temporal marks were issued, the structure and exploitation conditions of which shall be set forth through norms issued by the competent authority.

Within three months from the publication (i.e. November 5th, 2004), the Regulatory and Supervisory Authority (the Ministry of Communication and Information Technology) shall draw up the technical and methodological norms enforcing the Law no. 451/2004.