RESEARCH PAPER | Accounting | Volume : 3 | Issue : 12 | Dec 2013 | ISSN - 2249-555X

Re-Treatment of Real Estate Investments, According to the International Standards of Financial Reporting (IRFS). Case Study, Romania

KEYWORDS accounting treatment, evaluation, re-evaluation, real estate investment, tax treatment, tangible assets.

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ABSTRACT *The re-evaluation of the assets is a solution to reduce the effects of inflation in terms of accounting information, but it has significant accounting and tax implications in Romania. All these refer to the recognition or the re-evaluation of depreciable fixed assets for tax purposes with implications on profit tax and building tax. The evaluation and re-evaluation of the property elements is an important problem both for the accounting and for the tax and implicitly regarding their role in the enterprise management and also in terms of the accuracy of the information obtained through the annual financial statements.*

INTRODUCTION

According to IAS 40 "Real estate Investments", the real estate investment is "that property (land and/or building) held for rent or for capital appreciation and not for the use in the production of goods, provision of services, for administrative purposes or to be sold during the normal course of activity". So when procuring goods, such as assets, their destination determines placing it into a corresponding category. The main criterion of differentiation of real estate investments used by the owner is represented by the independent cash flows generated by this asset category.

CASE STUDY

In the present study, we proposed the re-treatment of the real estate investments, from tax and accounting point of view, according to IRFS.

In the group 21 "tangible assets" the real estate investments are recorded separately (account 215 "Real estate investments"). The real estate investments evaluated at the fair value follow separately from those evaluated at cost. In the account plan in OMFP 1286/2012 the accounts were included: 2151. Real estate investments evaluated at the fair value (A); 2152. Real estate investments evaluated at cost (A); 2815. Amortization of real estate investments evaluated at cost (P) (for the amortization of real estate investment ***evaluated at cost***); 2915. Adjustments for the real estate investments depreciation evaluated at cost (P) (for the depreciation of the real estate investments **evaluated at cost**).

EXEMPLIFICATION-

The company has an accounting value of land evaluated at 300,000 lei. On January 1st, 2011. The land is classified as real estate investment evaluated at the fair value on the date of transition to IFRS. The Fair value at the date of transition to IFRS is 320,000 lei. The fair value on 1.01.2012 is 350,000 lei. For the comparative amounts (from 01.01.2011 and 31.12.2011) amounts re-stated in accordance with IFRS are as follows:

On 1.01.2011

		Balance IFRS	
		D	C
2151	Real estate investments evaluated at the fair value	320,000	
1177	Reported result derived from the application of IFRS, less IAS 29		316,800
4412	Delayed profit tax		3,200

On 31.12.2011 (1.01.2012)

		Balance IFRS	
		D	C
2151	Real estate investments evaluated at the fair value	350,000	
1177	Reported result derived from the application of IFRS, less IAS 29		342,000
4412	Delayed profit tax		8,000

For the situation of the global result of the year 2011

		Turnover IFRS	
		D	C
7561	Gains from evaluation of the real estate investments at the fair value		30,000
692	Cost with delayed tax	4,800	

ACCOUNTING TREATMENT

The company uses the cost based model according to IAS 40. *Operations recorded in accounting*: • record of amortization costs; • record of adjustments costs for real estate investments depreciation; • resuming (cancellation/reduction) of adjustments for real estate depreciation.

b. The company uses the fair value based model according to IAS 40,. *Operations recorded in accountancy*: - record of incomes from fair value adjustments (positive differences resulted from the re-evaluation of all elements of real estate investments type to the fair value); -record of costs with fair value adjustments (negative differences resulted from the re-evaluation of all elements of real estate investments type at the fair value).

TAX TREATMENT

According to Tax Code for real estate properties classified as real estate investments, the tax value is the acquisition cost, the production cost or the market value of real estate investments acquired free of charge or made as a contribution to the assets of the taxpayer patrimony, used to calculate the

Volume : 3 | Issue : 12 | Dec 2013 | ISSN - 2249-555X

tax depreciation as appropriate. The amount also includes tax evaluations made according to the accounting regulations.

EXEMPLIFICATION

a) the company uses the fair value model. After initial recognition, an entity that chooses the fair value model will measure all of its investment property at the fair value. A gain or loss (a) a change in fair value of real estate investment will be recognized (a) profit or loss in the period when it occurs. If a property used by the owner (a fixed asset) is transferred to real estate investments that will be used for the fair value model, the company will apply IAS 16 until the date of change of use and will treat any difference at that date between the accounting value and its fair value as a re-evaluation in accordance with IAS 16.

Situation. Building A is considered tangible asset in the period 01.01.2009 – 31.12.2012 for which IAS 16 is applied, practiced a linear amortization over a period of 40 years. Annual amortization of 60,000 /40 = 1,500 lei. The accounting value on 31.12.2012 is of 60,000 – 1,500 (2009) – 1,500 (2010) –1,500 (2011)- 1,500 (2012) = 54,000 lei. On 31.12.2012, the building is transferred to the category of real estate investments, and the difference between the fair value (62,000 lei) and the accounting value (54,000 lei.) will be treated as a re-evaluation.

2812 = 212 6,000
Amortization of buildings Buildings

Record of added value:

212 = 1052 8000
Buildings Re-evaluation reserves of tangible assets

The asset transfer from tangible assets to real estate investments is recoded as follows:

2151 = 212 62,000
Real estate investments Buildings Evaluated at fair value

The record of corresponding deferred tax. Supposing that the accounting amortization is equal, in this case, with the tax deduction for the amortization it results a temporarily taxable difference of 11,600 lei. Deferred tax liability =16% x 8,000=1,280 is recorded as follows:

1034.distinct analytic = 4412 1,280
Current profit tax deferred profit tax

b) the company uses the cost model. If a company uses the cost model, the transfers between the real estate investments, the owner-occupied real estate and the stocks do not change the accounting value of the property transferred and they do not change the cost of that property for evaluation or information release purposes.

Building is considered owner-occupied asset in the period 01.01.2009 - 31.12.2012 and IAS 16 applies. On 31/12/2012, the building is transferred to real estate investment, at the cost level. The transfer of assets is recorded as follows:

2152 = 212 60,000
Real estate investments Buildings evaluated at cost

Transfer of cumulated amortization:

2812 = 2815 6,000
Amortization of buildings Amortization of real estate investments evaluated at cost

CONCLUSIONS

In order to evaluate the real estate investments, cost model can be used (the real estate investment is measured in the balance sheet at cost minus cumulated depreciation) or the fair value model (the real estate investment is measured at the fair value without recording depreciation) with changes within result account.

The tax value includes also the evaluations made according to the accounting regulations. -In case evaluations of the real estate investments are carried out leading to a decrease of their value below the value remained undepreciated, the tax value remained undepreciated of the real estate investments is re-calculated based on the level of cost of acquisition / production or market value of the real estate investments, if appropriate. The incomes representing the modification of the fair value of the real estate investments as a result of further evaluation using the fair value model are non taxable incomes. These amounts are taxable simultaneously with the tax depreciation deduction.

For the amounts charged to the reported result from the re-treatment of the real estate investments, the following rules apply: - the amounts which represent elements of incomes recorded additionally according to IFRS are elements similar to expenses.

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