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INTRODUCTION.
RESEARCH OBJECTIVE AND RESEARCH METHODS

The main aim of the present scientific research is to highlight various aspects about the fiscal balance and fiscal policies that converted in the practical experience of the Romanian economy before Romania joined the European Union. The frequent question to which an answer is currently sought both in the speciality literature and the economic practice is "Do we have an economic balance or an imbalance?"

Since I am a specialist in the field of finance, I have been equally concerned with the experience of other countries in the field of taxation, and with the answer to the following question: "What was the lesson that Romania drew from other countries' experience?"; I was also interested in the effect of fiscality upon the economic balance at national level, and – why not? – as perspective, at the level of the European Union.

With the research syntheses that I carried out about the scientific and practical fundamentals of the economic balance, I intended set up the bases of a real understanding of the phenomena that actually occurred in the Romanian economy between 1989 and 2007. Once Romania's accession to the European Union was accepted (the document was signed on 1 February 1993), the Romanian government practically took upon itself the structural reforms in the field of fiscal policy and, implicitly, in the field of financial intercessions, i.e. the laws in the field of fee and fiscality were meant to gradually increase the fiscality mass and to apply indirect taxes easily to be drawn. We agree with the fact that, for example, the introduction of the VAT on 1 July 1993 determined both the fiscality increase (its application framework was more clearly stated), and a revenue increase to the state budget due to this indirect tax. If we take into account the main content of the public resources (mainly consisting in amounts of money coming from indirect taxation), mention should be made about the fact that they were highly ranked in the fiscal policy throughout the period under analysis.

The research encompasses the period between 1989 and 2007, characterised by a shifting to a new economic system and by the fact that Romania joined the European Union on 1 January 2007. The economic processes and phenomena that characterise the above mentioned period of time represent a challenge from the point of view of the financial steadiness/unsteadiness, balance/imbalance both at national and international level.

We tend to believe that “the compulsory stipulations” that Romania took upon itself once the accession to the European Union became a fact had two significant outcomes:

a) the re-setting of the taxes and duties within the Romanian fiscal system (typologically speaking);
b) the gradual modernization of the Romanian tax system by means of laws and formalization.

Research Methodology

Our endeavour was to highlight the main issues about the balance and the fiscality system by using the comparative method. We wanted to compare a balance, in general, with economic balances, and to employ several relations existing between the measurable quantities of a budget, i.e. its revenues and expenses on a large scale, and less the import and export of a trade balance. The synthesis of the statistical information provided by the general budget of the Romanian state (public data available on the web site www.mfinante.ro) was attained in order to analyse the comparative evolution of several significant budget indicators that reflect the economic gearshift that generates the development, the balance, imbalance or the economic crisis. We believe that the decisions, at macroeconomic level, are made after the tax capacity of the country is verified since it ensures the resources able to fulfil the social promises of the past and – eventually- to produce political success.

The present study attempts to focus on the long term balance, and it encompasses the period between 1989 and 2007.

The research methodology consists of various theoretical approaches in the field of balance and taxation. I tried to explain what balance is and to define the concept of taxation, in general. I was inspired in my endeavour by authors highly ranked at international level; further on, I tried to find the way in which these concepts actually function within the Romanian economy. The research procedure makes reference to a methodology involving data collection and statistical information transposed into graphics and mathematical figures in order to get a successive and a scientific demonstration. At the same time, the graphics with statistical information were used to carry out a comparative analysis concerned with the evolution of several indicators (the same indicator and its referential yearly evolution); the texts corresponding to the graphics included logical and critical deduction, and deductions of synthesis (see the author's commentaries/opinion about the budget analysis).

THE ECONOMIC BALANCE: DEFINITION, CONTENT, AND THEORIES

The Concept of Balance

The interest in the economic balance was present throughout history but it was emphasized once the economic imbalance became more intense and manifested itself as crises of different type, and the microeconomic thinking advanced to the macroeconomic level. The complex and continuously changing character of the economic needs and resources, the imbalance phenomenon at international level, and the problem of balance and economic growth represent the main concerns of the governmental management in any country.

The economic balance became central issue, starting point and, at the same time, the end of the economic theory and practice. "*It is surprisingly to notice that the major part of the contemporary works include in their title the word balance*", asserted Henri Guitton[1].

If one notices the evolution of the concept of balance, one might conclude that the economic field provides a multitude of opinions, many of them being contradictory and drawn from various schools and trends, all of them trying to provide answers to a series of questions such as: "What does the economic balance mean? What are the conditions and processes necessary in order to ensure the balance? What is the relation between balance and imbalance? What is the characteristic of the evolution of the national economy? What measures should be taken by the (public and private) economic providers in order to ensure and maintain the economic balance? What is the connection between the economic balance and economic optimal performance?" etc.

The concept of *balance* (*equilibrium*) comes from Latin terms*:* *aequilibrium* (*aegus*= equal and *libra*=balance), and it generally indicates the equality of two measurable sizes.

The concept has a secular value as well, since it was initially employed in natural sciences, and - later on - in the field of economics.

As far as the **natural sciences** are concerned, they define the term *balance* as follows: "the state of recumbence of a thing; the stationary state, as moment of steadiness within

[1]Henri Guitton, *De l'imperfection en économie (About Imperfection in Economics)*, Calman-Levy, Paris, 1979, p. 204.

dynamic systems"[2] or "a macroscopic state of the material systems (things able to transform themselves) formed under the auspices of the reciprocal action of some external, respectively internal forces, i.e. a state that remains invariable in time[3].

The **economic** balance is defined as follows: "a state of immobility of an economic entity or a situation when the forces that act upon the respective entity are balanced, and there is no tendency to be changed" [4] or "a situation when the economic agents or the generating acts that accompany them, i. e. the markets, do not get motivated in any way with a view to changing their economic behaviour" [5].

In *The Encyclopaedic Dictionary*, the economic balance is defined as follows: "that state of correspondence between the interdependent elements and all the variables needed in order to be correlated with the social and economic activity... It is therefore the result of a system determined by the existing relations between technical, economic, social and political factors that ensure the price stability, i.e. the correspondence between the supply and demand, revenues and expenses, the commodity circulation and money, the dynamics of job employment, on the one hand, and the numerical growth and training of the labour force, on the other hand, the equivalence between the level of economies and investments"[6].

The first mode to approach the understanding and usage of the concept of economic balance is connected with its **semantic meaning**[7]. The starting point is the phrase of equal weights (for balance) and non-equal weights (for imbalance) put on balance pans; in this situation, we have a relation between two measurable quantities: the budget revenues and the budget expenses, the situation of import and export in a trade balance, etc.

Taking into account the content of the economic balance, the economic theory and practice makes reference to and analyses three types of balance: the **material** balance, the **account** balance, and **labour force** equilibrium, all of them making up a dialectic unit.

As far as the meaning of equality of two measurable sizes is concerned, the concept of balance is employed in order to designate the various states through which the national

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[2]Iulian Ceauşu, *Dicţionar enciclopedic managerial (Managerial Encyclopaedic Dictionary)*, Academic Publishing House of Management, Bucharest, vol. l, 2000, p. 301.

[3] *Encyclopaedia of Natural Sciences*, vol. 2, p. 212.

[4]Paul A. Samuelson, *Economics*, Teora, Bucharest, 2000, p.893

[5]*Macmillan Dictionary of Modern Economics*, Codecs, Bucharest, 1999, p. 132.

[6]*Encyclopaedic Dictionary*, vol. II, Enciclopaedical Publishing House, Bucharest, 1996, p. 171.

[7] *** *Political Economics*, Porto-Franco, Galaţi, 1991, p. 32.

economy undergoes at microeconomic level (microeconomic balance), mesoeconomic balance (mesoeconomic balance), and macroeconomic balance (macroeconomic balance).

The **microeconomic balance** is concerned with the level of the primary links, economic agents (producers and consumers); **the mesoeconomic balance** is related to the branch structures and territorial zones, and **the macroeconomic balance** systemically integrates the two above mentioned forms of balance at national economic and territorial level.

The macroeconomic balance indicates a state of relative correspondence between the global supply and demand for various segments of the market or between the needs and resources at national economic level, and it depends upon the allotment and reasonable use of the resources, the normal functioning of the capacity of production and circulation, and upon all the elements of the economic mechanism[8].

The general economic balance is the outcome of several ***partial balances***, such as the production balance, balance of repartition, exchange balance, monetary and budgetary balance, etc. that make up *a system* of economic balances. There is - in this case - a relation similar to that existing between an object and one of its elements: the maintenance of the above mentioned balances in a dynamical position has favourable consequences upon the general economic state of balance. Their possible deficiencies affect the good functioning of the national economy. The rhythm of improvement within the partial balance gets reflected in the general rhythm of the economic development.

The general economic balance is primarily a **structural** type of balance, and, secondly, a **functional** balance[9]. The structural balance, i.e. the expression of the system of proportions between various economic zones, sectors, branches, and activities, represents a combination between technological, technical, economical, and social structures. The structural economic balance presumes the concurrent implementation of the material, accountable (as far as the labour force is concerned), and ecological balances as well.

The functional balance is "the expression of the system of dependencies between the factors that develop, manage, organise and obtain the functioning of the national economy"[10].

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[8]Constantin Popescu, *Echilibrul înaintării* (*Advance Balance*), Efficient Publishing House, Bucharest, 1998, pp.121-122.

[9]N. Gh. Niculescu, *Legităţi ale economiei de piaţă (Laws of Market Economy)*, "Gheorghe Asachi" Printing Press, Iaşi, 1992, p. 278.

[10] N. Gh. Niculescu, *Cited work*, p. 278.

Mention should also be made about the **short term** balance, i. e. the relation between needs and resources from an immediate perspective, when it is favourable to get a more precise quantification of the influences exerted by the conditioning factors of the balance, and about the **long term** balance, when the correspondence between the two terms of the functional balance and the economic structures are stable for a longer period of time, overcoming the problems of several short term imbalances. The quantification of the factors that exert their influence upon the long term balance is more difficult, especially when subjective forces, external to the market interfere and do not have the power to detect the whole "gear" of the long term economic functioning.

The second way to approach the economic balance intends to capture this concept from the point of view of an economic science conceived by **imitating mechanics**. Henri Guitton clearly stated that "*a balanced system is a system that is not changed, that remains similar to itself*"[11], i.e. we say that a thing is balanced when the forces that determine it to leave its position are compensated by ones that make it to turn back to them again and again.

As many terms in the field of economics, the concept of balance was introduced from the field of mechanics. This science has employed it for a long time, and Adam Smith was the one who introduced this notion in his work, *The Wealth of Nations* (1776), in order to get an analogy between some of his ideas about the economy functioning and the mechanical phenomena.

From this perspective, the economic balance might be **stable** or **unstable**. The stable balance might be defined "*as a situation in which there are forces that automatically compensate the digression, and allow the re-establishment of the balance on all markets, i.e., briefly speaking, the restoration of the general balance*"[12]. The immutability of the general balance means "*the maintenance of the balance within certain limits (margins of variance) accepted with a view to ensuring the qualitative identity of the mechanism of economic functioning*"[13] or a situation in which even if the system discards from the balance point, it contains the conditions needed with a view to recovering its balance. Thus, "*the steadiness of*

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[11]Henri Guitton, *De l'imperfection en economie (About Imperfection in Economics)*, Calman Levy, Paris, 1979, p. 51.

[12] Gilbert Abraham -Frois*, Economia politică (Political Economics)*, Humanitas, Bucharest, 1998, p. 100.

[13]Marius Băcescu, Angelica Băcescu-Cărbunaru, *Macroeconomie şi politici macroeconomice* (*Macroeconomics and Macroeconomic Policies*), Educational All, Bucharest, 1998, p. 10.

the economic balance ... implies a dynamic and not a static balance"[14]. For example, if the supply overcomes the demand, producers' stocks increase and signal out the excess supply. Prices will decrease until supply and demand register equal values again.

Under the direct influence of several specific factors, the economic balance might acquire a dynamic character. Among these factors that manifest themselves along as tendencies, mention should be made about the following ones:

- population: its number, structure according to age and social and professional criteria, employees' qualification level, etc. in a continuous change draw corresponding changes in the whole demand;
- the technical and scientific progress that determines the emergence of new needs, and sub-branches, to structural and level changes, and, implicitly, to modifications as far as the supply and global demand are concerned, to attempts meant to adapt their relations to the changes;
- changes in the economic agents' behaviour that determines new types of trends in the usage of revenue – for consumption and investment – and in the structure of the economic branches and sub-branches concerned with the business stock placement;
- the limits of the natural resources that act in a restrictive manner and impose the reorganisation of the production factors as far as their allotment and combination is concerned, as well as the rethinking of the entire supply and demand process.

It is significant to note that the understanding of the concept of balance also depends upon the fact that we are aware of its **relative** character. Economy is a complex concept, and there is no **absolute** balance in reality. There is no ideal balance; the perfect competition between supply and demand does not exist. Under real economic circumstances, the incertitude and imbalance seem to be more appropriate terms to be used when we characterise the state and evolution of an economic system; nevertheless, partial balances represent a reality.

In the beginning, the **classical and neoclassical (marginal)** economics advanced the idea that an economic balanced is automatically obtained, i.e. "*there is an invisible hand*" (concept introduced by Adam Smith) that determines "the economic system that is dynamic

[14]Marius Băcescu, Angelica Băcescu-Cărbunaru, *Cited work*, 1998, p. l 0.

by the means of several independent actions that analyse some provided variables"[15] "to eventually get a stationary balance".

Some specialists in the field of economics consider that during the economic liberalism, the phrase *economic balance* was introduced in the theory of value and resource allotment by Adam Smith, and its usage was continued by Alfred Marshall, Leon Walras, etc.

A significant step in defining the concept of balance is represented by the shifting from the opinion according to which the general balance is the result of producers' and consumers' individual actions to the principle that defines the general balance starting from global, macroeconomic terms.

The first economist who introduced the notion of **dynamic balance** in the field of economics was John von Neumann (1932). Starting from Walras's balance and transforming the system equalities into disparities, within the theory of games, he made a mathematical generalisation of macroeconomic correlations. The practical insufficiency of Von Neumann's model is eliminated by Leontief's input-output model.

The American economist of Romanian origin **Anghel Rugină** took into consideration these ideas accepted by most of the economists, and outlined a unique synthesis of the main theories about the economic balance. He formulated 12 conditions needed in order to reach the state of general and stable balance:

1. *The effective demand = the real supply of goods and services, capital, factors of production, public goods and services and foreign bills;*
2. *The prices for (public and private) goods and services- the lowest total average cost per production unit = marginal cost=marginal revenue= marginal usage;*
3. *The prices of the factors of production (paid or imputable); annuity= marginal productivity of the land; salaries=marginal work productivity; profit=marginal management/leadership productivity; taxes=marginal use of public goods and services;*
4. *New investments= voluntary savings;*
5. *The credit employed by the system= the real income saved in economy and allotted for this purpose;*
6. *In the field of economics, there should exist no debt and bank loan monetisation;*
7. *The fundamental law in the field of finance: first, revenues, then expenses; this rule is applicable both in the private and the public sector;*

[15]Emil Scarlat, Nora Chiriță, *Cited work*, p. 171.

8. *Pecuniary income (annuity, wages, etc.)= the real revenue;*
9. *Capital formation in the field of economics should be exclusively based upon voluntary savings;*
10. *Both public and private budgets should be generally balanced by current real revenues;*
11. *Internal value of currency= external value;*
12. *Currency exchange rate =official parity"*[16].

Balance and economic optimality

The tendency towards optimality was and still is a main concern for the researchers interested in the economic processes and phenomena. It is part of our human nature, of people's wish to achieve better things; it is the outcome of *homo sapiens*'s endeavour to accomplish his goals with a minimum effort once he turned to *homo economicus*. The economic content of the category called optimality started to be outlined when the economic science began to be connected with the field of mathematics, and quantification became possible due to the use of the infinitesimal calculus discovered by Newton and Leibniz in the end of the 17th century.

"*Economic optimality means that situation or state of the economy that ensures the best economic efficiency, and best corresponds to the economic interest*"[17].

The economic optimality had multiple meanings; yet, the economic theory considers that **Pareto's optimality** is very significant. It might be defined as that balance position determined by the fact that all the economic agents benefit from the highest satisfaction, and it is impossible to make one individual better off without making at least another individual worse off. Pareto's optimality means that it is impossible to improve the situation of all the individuals within the same society simultaneously. "It is said that an economic system is balanced if the changing of one of its conditions brings other changes that will produce an opposite action. This balance is stable in case of a finite change. It is unstable on the edge when the balance conditions are valid only for an infinitely small change"[18].

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[16]Anghel Rugină, *Principia oeconomica (Economic Principles)*, Bucharest, 1993.

[17]Iulian Ceauşu, *Dicţionar enciclopedic managerial (Managerial Encyclopaedic Dictionary)*, Academic Publishing House of Management, Bucharest, vol. l, 2000, p. 556.

[18]Vilfredo Pareto, *Cours d'economie politique* (*Course of Economic Politics*), vol. I, Lausanne, 1896, p.18 *apud* Victor Stoica, *Modul economic de gândire* (*The Economic Pattern of Thinking*), Economic Tribune, Bucharest, 1998, p. 42.

Optimality means[19]:

a) to establish its aims and criteria;
b) to become aware of the limits (restrictions) of its framework by taking into account the resource scantiness and therefore obtaining a conditioned optimality that expresses the best state that might be reached by using the available resources;
c) to fundament the decision making mechanism (we consider that the aims had in view are provided).

If there are more optimality criteria or more decision makers, the decision making problems are complex.

The study of the economic optimality can be carried out only in accordance to the limits of the economic science. It involves the simultaneous approach of the issue from two different directions: the economic direction establishes the economic content of the optimality function and the restrictions, and the mathematical direction fundaments the problem solving mathematical patterns.

From this point of view, economic optimality "*represents the extreme (maximal or minimal) value of a mathematical function with more variables defined in a field of economic activity if there is a restriction of the equation type and a disparities of imposed on the values of these variables*"[20].

Taking into account the complexity and interdependences of the economic processes, the transposition into practice of the results obtained draws the need to discover and to put into function a system of economic efficient factors meant to harmonise the partial optimality and the accomplishment of the global optimality of the national economy.

"*The optimal economic system means to provide the maximum out of what people need*"[21]. Since the man, with his possibilities and especially his needs, is the centre of its concerns, the theory of economic optimality studies both the production area (the producer), as far as the resource allotment and its optimal usage are concerned) and the consumption area (the consumer) since men are both providers (a quality consisting in the pursue of maximum economic efficiency), and consumers (tend to satisfy their spiritual and material needs as

[19] Iulian Ceauşu, *Cited work*, vol. l, 2000, p. 557.

[20] Marcu Horovitz, *Modelul economic optim (Optimal Economic Model)*, Academy Printing Press, Bucharest, 1970, p. 32.

[21] J. K Galbraith, *Ştiinţa economică şi interesul public (Economic Science and Public Interest)*, Political Publishing House, Bucharest, 1982, p. l l.

much as possible). For this reason, the problems of economic optimality were developed by the theorists of "**the economic welfare**"[22].

Starting from a valid and universal criterion, from the natural and essential aim of every economy, the welfare maximization of the entire population – **the global (social) economic optimality –** can be reached when the relative balance between the society's needs and resources will become a reality, and the most efficient allotment and usage of the entire material, accountable and human potential will be ensured.

In Pareto's opinion, the knowledge of the efficiency maximal value is not enough to determine the optimal public solutions since Pareto's optimality cannot point out only one optimal solution. It should establish an assembly of solutions out of which we should be able to make a choice.

Starting from the fact that the economic balance reflects the capacity of the economic system and of its sub-systems to function but it does not show how well it actually functions, we may assert that the economic optimality brings forward the measurement of the economic balance, i.e. the balance obtained under maximum conditions of efficiency.

Economic balance or imbalance?

We cannot talk about balance if we do not attempt to identify the specific characteristics of the various markets that undergo the state of economic imbalance, respectively, the significance and consequences of this positioning.

On the market, one might register a series of similarities between consumer's and producer's behaviour, and they all derive from the fact that each of them wants to get more and more satisfaction as far as the price is concerned (higher and higher price). Yet, their motifs are different: consumers' options are stimulated by the lower prices, and the producers are stimulated by the price raise.

If the commodity price and quantity corresponds both to the consumers' and providers' wishes, and there is no discrepancy between the real quantities and prices, on the one hand, and those that are expected, one can talk about a situation of economic balance; on

[22] *"welfare economics deals with the knowledge of the circumstances under which the highest level of satisfaction of the individuals from a society might be ensured"* (Jacques Genereux, *Political Economics. Microeconomics*, ALLBeck, Bucharest, 2000, p. 167).

the contrary, when we have "*a situation in which neither the consumers' expectations, nor the providers' wishes are fulfilled, there is economic imbalance on the market*"[23].

The market of a product (or the market of more products) might undergo different forms of imbalance, such as absorption and pressure. Absorption[24] means an excess demand (D>S) and it might track down the consumers' lack of satisfaction. Consumers cannot get what they want with fixed prices or they can get it "only if they allot a supplementary cost, that is to say a ballast cost (queuing, tips, good turns, etc.)"[25]. A free market with insufficient goods and services will stimulate the capital investors to raise their supply until it corresponds with the demand. Producers choose their consumers and they are not interested to produce commodity of a high quality with small costs.

The opposite situation, the pressure (S>D), is considered a normal state of imbalance (excess supply). Consumers enjoy more advantages since they are perceived as "*consumer kings*". They choose the quality of a product and the best offer since the provider is interested to reduce the costs and to invest in quality when the economy is about to undergo from one imbalance to the other[26] (absorption-pressure situation); there is an intermediate state of imbalance – **false pressure** – when the sales difficulties are determined by a low purchasing power.

These forms of imbalance produce various **consequences** as far as the economic evolution is concerned.

One should take into account the fact that nowadays the economic theory shares the opinion that the economic life, just like any other life of a natural system, is generally characterised by imbalance, not by balance. There is a tendency to increase entropy by moving towards imbalance, not towards balance, by moving towards imperfection, not towards perfection. Henri Guitton said that "the only real thing is a mixture of order and disorder"[27].

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[23]Philip Hardwick, Bahadur Khan, *Introducere în economia politică modernă (Introduction to Modern Political Economics)*, Polirom, Iaşi, 2002, p. 131.
[24]Imbalance associated with a centralised economy, in most of the cases, that might be caused by rigid prices, and the excessive centralisation of the decisions in the field of investment, etc.
[25] Ioan Mihuţ, Marius Pop, *Consumatorul şi managementul ofertei (Consumer and Supply Management)*, Dacia, Cluj-Napoca, 1996, p. 59.
[26]Transitional economies (Romanian economy included).
[27]Henri Guitton, *Cited work*, p. 202.

Fiscal Policy

The notion of fiscal policy

Fiscal policy is defined as all fiscal decisions taken by public decision makers in order to ensure financial resources to finance public needs and for social and economic reasons, considering that the economy is influenced by real or objective factors. This is the result of fiscal policy decisions and the lever by which these decisions are implemented. Consequently, we believe that fiscal policy is one of the variables that governments have at their disposal[28].

We believe that fiscal policy includes all decisions by which the structure of the fiscal system is created and its functioning is ensured in order to achieve the results sought by the governmental factor[29].

Fiscal policy decisions and regulation of the fiscal system

The characteristics of fiscal policy decisions influence the structural evolution of fiscal systems, attributing them a dynamic character. There are two types of fiscal decisions: micro and macro.

Fiscal micro decisions are taken by government structures that manage taxes and monitor for compliance with the tax law while macro decisions are taken by the governmental decision maker.

Structural fiscal policy decisions have the effect of adjusting the fiscal system by means of the feed-before mechanism, aimed at:

- correcting and/or preventing unexpected effects;
- monitoring new effects;
- increasing the role of the fiscal system in achieving economic stability;
- Fiscal harmonisation of the countries participating in regional or international agreements;
- A correlation between the fiscal systems and political changes that alter social relations;
- influencing some decision-making behaviours of economic actors.

Structural or strategic macro decisions[30] are connected to the bigger picture, to an assessment of future effects.

[28] Stancu I, Finanțe (Finance), Economic Publishing House, Bucharest, 1996

[29] Manolescu G, Politici economice (Economic Policies), Economică Publishing House, Bucharest, 1997

[30] Bulborea I, coord., Microeconomie și macroeconomie (Microeconomy and macroeconomy), part I, Pro Universitaria Publishing, Bucharest, 2007

The spatial dimension of a fiscal policy

Macro decisions that influence a fiscal policy show the fiscal independence available to the decision maker in each country, based on the constitutional right to set taxes. Therefore, the spatial dimension of a fiscal policy is important as it is indicative of the right to introduce fiscal taxes, to amend certain legislative items and procedures to eliminate or mitigate the effects of double taxation.

From a political perspective, there are two categories of states – unitary or federal. In the case of unitary states, the central government issues tax laws that are valid in all the administrative territory while federal governments are usually constitutionally compelled to delegate powers (including fiscal powers) to regional or local sub-governments. Basically, fiscal policies of states are unitary on national territory, acting within regulated margins.

Decentralisation of decisions determines the birth of competences at local, regional and central level as concerns the government administration with the power to make fiscal decisions.

The neutral character of taxes on trade between union countries is a fiscal policy condition of integration of national markets into the regional markets concerned.

Harmonizing the government’s decisions

The geographical area influences the degree of decentralization of decisions and division of fiscal competences within a country. In our opinion, governments should have power over redistribution and stabilization policies, because, as we reported in this study, we believe that there cannot be a "self-regulation" of the market. We find that free economies, although aiming for a perfect competition, are far from attaining it. But sometimes, macro-structural decisions can cause distortions in the economic and fiscal policies of a country.

The government’s decisions and their effects for the fiscal system

Decisions issued by governments are directly correlated with the expected utility of a fiscal policy. Opinions about the utility of a fiscal policy have created various trends of thought that have influenced the decisions of administrative powers. The state's role is influenced by the rapidly changing social and economic environment. It was found in practice that fiscal objectives are concrete and not always neutral. Basically, fiscal finalities seem to be more important than socio-economic ones, since the latter can also be achieved through fiscal leverage.

To avoid the risk of making decisions too late, the governmental factor must observe the optimal timing of intervention through fiscal leverage, and the timeframe for this decision.

We consider that reducing the level of taxation in the economy of a country leads to an increase in the neutrality of the fiscal system (of course, this is conditioned by macroeconomic policies of public power).

We believe that the supply of public goods, such investment and opportunities is inextricably linked with public power behaviour, which, through administrative decisions clearly affects public supply.

Efficiency of the fiscal system

The magnitude of fiscal policy decisions that change taxation techniques depends not only on how much importance the public decision-maker assigns the relative neutrality of the fiscal system in relation to the socio-economic environment, but also on how revenue is formed, accumulated, distributed and spent by a society. As a result, financial efficiency, that is the efficiency of the fiscal system, is important for the administrative decision-maker. It affects the budget balance, fiscal balance and public debt.

Fiscal efficiency depends on the public decision, and on the decisions of subjects working in the economy, plus the structural development of the economy, the population growth rate, and fiscal education that influences the collective behaviour.

FISCAL BURDEN AND TAX REVENUE (ARTHUR B. LAFFER'S CURVE)

The debates generated by excessive state intervention in the economy, considered to be the cause of discouraging personal initiative and risk taking, of periods of recession, stagnation and decline in economic growth, of the accumulation of huge deficits and of inflation, have generated a new momentum of liberal economic thought. Prioritizing the individual and entrepreneurship, Laffer seeks to find solutions to elaborate a policy able to better solve the problems of contemporary economies.

Using the market economy in the U.S.A. as basis for analysis and mathematical reasoning, the American economist Arthur B. Laffer represents through a curve, the connection between fiscal burden and the flow of tax revenue, currently known as the Laffer curve. It quickly became the theoretical foundation and reference for supply economy theoreticians.

THE FISCAL RELAXATION POLICY TO STIMULATE SUPPLY

There were some old concerns to develop policies to support supply dynamics. Rejecting the mercantile views to support global demand, the physiocrats paved the way for a new approach to the economy, showing the link between tax rates and production, rejecting excessive fiscal burden and supporting the need to stimulate productive effort.

In their work, D. Hume, A. Smith[31] and J. B. Say[32] argued that a big fiscal burden was counter-productive, highlighting the relationship between tax rates and tax revenues, along with the importance of incentives for work. Therefore, they are considered the founders of the policy of fiscal relaxation.

The "pure tax cut" policy is based on relative prices, the elasticity of supply and on the "deviation pattern" developed by Laffer.

Reducing fiscal burden

If the public decision-maker chooses to increase the fiscal burden in order to have more tax revenues, there are two possible effects. On a short term, additional tax revenue is obtained but at a later stage, they drop due to less taxable matter. Therefore, on the long-term, tax revenue decreases when the fiscal burden constantly increases.

Reducing public expenses

[31] Adam Smith, An Inquiry into the Nature and Causes of the Wealth of Nations, 1776, London

[32] Jean-Baptiste Say, *Traité d'économie politique, 1803, Paris*

Some supply economists, among whom Laffer, neglect public expenditure. In fact, the neglect of the aggregate demand is a weakness of the supply theory.

Public expenditures are poorly compressible. Their stabilization or reduction requires procedures and a relatively long time. On the other hand, the effect of reduction may be short-lived, because of upcoming economic, social and political events.

The hostility of the population whose income depends directly or indirectly on maintaining public expenditure can generate either political instability or the change of programmes implemented by the public decision-maker or both.

Budget balance

For the supply economists, the budget deficit ceases to be an instrument of economic policy. They support a pure tax cut policy and return to budget balance.

Laffer believes that easing the fiscal burden[33] will generate an increase of taxable matter to such extent that any increase in deficit on a short-term and its financing without inflationary pressures is not a problem. But this would imply that the elasticity of labour supply and saving is higher than unity. His arguments, however, are far from economic reality, as they are based on specific conditions rarely present in the economy.

The Central Bank and the money supply control

Funding the budget deficit from the existing savings in the household sector does not generate new inflationist tensions. However, it deprives competitive economy of the resources used by the public economy. The funding by the Central Bank of the deficit creates the danger of inflation. Commercial banks can underwrite when public titles are issued. Mobilising financial securities underwritten by commercial banks at the Central Bank when the latter relaxes the conditions for distribution of loans fuels inflation.

Deficit financing results in increased market interest rates[34]. Monetary policy operates simultaneously on interest rates on both public and private loans. Central Bank decisions are

[33] Șaguna D.D, (2001), Tratat de drept fiscal și financiar (A Treatise on Fiscal and Financial Law), Bucharest, Oscar Print Publishing House

[34] Roşca T., Monedă şi credit (Currency and Loans), (2001), Altip Publishing House, Alba Iulia

influenced by international relations and exchange rate fluctuations. The monetary decision-maker is in an uncomfortable position.

Fiscal policy and budget flexibility

Budget flexibility is an effort of synthesis and of finding original solutions aimed to mitigate economic fluctuations. It cannot be included in the policies to stimulate demand or in those to stimulate supply or in monetary policies.

It is an original combination of automatic fiscal stabilization within an active neo-Keynesian compensation policy whose principle is the countervailing budgetary imbalance and the search for a specific balanced budget supported by liberal policies. This reserves an important role to the monetary regularisation preferred by monetarists. Correcting monetary imbalances implies a gradual response from the monetary policymaker according to the growth theories.

Fiscal mechanisms to stimulate the economy

Fiscal means are the most commonly used by public authorities for the purpose of economic recovery or in order to eliminate or mitigate the consequences of disruptive factors. Thus, in the opinion of some contemporary economists, tax becomes an essential tool of economic policy of the state and namely of its social policy. This tool serves to balance the power of owners of private companies in a capitalist economy. Tax empowers the state over private entrepreneurs by limiting their own powers. This is its deep significance: the taxation power of the state opposing "the capitalists’ power to enterprise."

The way in which various tax mechanisms work (i.e. entrepreneur’s income taxes, consumption taxes, customs duties, etc.) differs from one country to another and from one time period to another. In general, to some extent, the state can influence, by taxation, all the phases of social reproduction.

Financial decisions or financial policies?

The concept of financial policy

Political parties come up with their own agenda setting their guidelines in order to come to power, or to preserve and strengthen it. The political agenda of a party defines the objectives, the means and methods which it intends to use to achieve them, the social categories (groups) they addresses and whose interests they defend, and its look on the current major domestic and international issues.

The author expresses his view that the term "financial policy" is not supported by science or by economic practice. Therefore the answer to the question "financial policy or financial decisions?" is "financial decisions" because governments do not develop *financial* but *fiscal* policies. We also ascertain that the logical connection between "budgetary" and "financial" does not necessarily imply the existence of a distinct financial policy at government level. Realistically, financial decisions are subordinate to fiscal policy.

The policy of public expenditure must determine the size, destination and the optimal structure of these expenses. It must define the objectives to be achieved by various expense categories, to specify the ways, methods and tools that should be used for these objectives to be achieved by a minimum financial effort.

Setting the extent of public expenditure implies setting their absolute extent (total in local currency) and their relative extent (percentage in gross domestic product).

A concern of utmost importance for policymakers in the state's financial decisions must be to keep the society's total expenditures within the resources that can be mobilized nationally.

THE NEED TO REFORM THE ROMANIAN FISCAL SYSTEM

References to the fiscal system inherited from the past socialist economy

In a centrally planned system, the attitude towards taxes was inconsistent. They were either ignored or downplayed or the subject of heated debate. Initially, it was considered that taxes can never change or alter distribution relationships or that they do insignificantly. Later it was argued that taxes should be used to transform the mode of production. Therefore, by progressive taxes on income and wealth, the aim was to confiscate all private capital and eliminate resources for any private property.

The views of Karl Marx and Friedrich Engels, supporters of capital taxation, are significant. Theoretically, in countries with classical socialist political regimes and economic and social structures, there should have been no taxes.

The fiscal system reform

The transition from a planned centralized economy to one based on the market forces required a redefinition of property rights and the creation of production factor market. It also required a series of economic reforms. The fiscal reform had to be applied at the same time as the price reform, the microeconomic management system reform, the financial sector reform, the reform of foreign trade to support the transition.

The year 1990 brought no structural changes to the fiscal system. Decisions had a marginal character in the first year. Their focus was on adjusting levying techniques, respectively disbursement of benefits, the tax rates on wages, the exemption of private farmers from income tax.

The important reform in the field of taxation occurred in 2003 when the Fiscal Code Law 571 was adopted.

The main guidelines of the Romanian fiscal system reform after 1989

- Restructuring of taxes on revenue and assets
- Introduction of dividend tax
- Personal income tax

Taxation techniques under the circumstances of a global economic reform

The experience of countries with advanced fiscal systems was needed and used to restructure the Romanian fiscal system, but it was not enough. Economic and social structures generated revenue flows incomparable in terms of nature, size and stability. Government structures were underdeveloped, lacking information and specialists.

In order not to adversely affect the development of the global reform, the priority was to ensure financial finality of taxes and to sacrifice economic and social finalities. Harmonisation of the fiscal reform with the public expenditure reform and the social transfer reform was a must. To support economic reform and social protection measures, actions were required that were precisely targeted through public spending, especially through social transfers.

The characteristics of taxation techniques were influenced by the evolution of socio-economic structures, by the income distribution, by the level of public utilities to be financed and by the public decision-maker’s options. Their complexity required long time frames either to amend or to develop new fiscal products, or to get parliamentary approval and prepare for their implementation.

THE MAIN CONTENTS OF THE ROMANIAN FISCAL SYSTEM

In what follows I shall speak about indirect tax reform in Romania because indirect tax is the main content of the Romanian fiscal system, both in how it is regulated, but also because it has an important share in the total consolidated budget revenues of the state. The irrelevant exception is customs and excise duties, which, after Romania's accession to the European Union had a decrease tendency (in 2007 they decreased by more than 2.8 times as compared to the year 2003). It is explained by the liberalization of capital, goods and services movements. Logically, VAT increased significantly after Romania joined the European Union. These issues are clearly reflected in the tables in Chapter 8 of this study. I refer specifically to the following main indirect tax sources of the state budget: the value added tax, excise duties and customs duties.

They are characterized mainly by:

- The introduction of excise taxes;
- The introduction of VAT

The introduction of VAT (as a consumption tax) on 1 July 1993, the destination principle, the invoicing method (or lending) allowed complete exemption of export tax incurred on exported goods and services.

- **The new regulation on customs duties**

Customs duties from the import customs tariff apply to the customs value[35] of goods imported by traders, converted into RON at the rate of exchange. After the implementation of the drawback customs regime, import duties levied have been totally or partially refunded whether imported goods are re-exported in the same shape, incorporated into exported products or converted, processed or repaired for export. Goods in transit in Romania are exempt from customs duties.

Joining the EU required the removal of restrictions on the free movement of goods (Duties are a restriction). The harmonisation of Romanian legislation has not been completed but the removal of EU supervision meant acceptable disparities.

[35] The Fiscal Code of Romania, Law 571/2003 with subsequent changes and additions

FISCAL HARMONISATION

"La fiscalite est maintenant une science" (Fiscality has become a science). This is how the well-known expert Maurice Laure, the father of VTA, begins his book "Au secours de la TVA"[36]. He notices that, in the 20th century, the science of Fiscality has asserted itself due to the following two factors:

a) the development of management techniques and communication facilities forces tax systems to continually improve so that no arbitrary factors occur in the economic activity that would diminish its effectiveness. In other words, the different tax treatments should not affect competitiveness of participations in the market competition.

b) the experience of countries with a command economy and that of countries with a leftist orientation confirms the lack of motivation of economic agents if they are deprived of a large part of the fruits of their efforts. Therefore, decision making should take into account the public interest, in the service of which is the state, as well as the psychological traits of human activity. The taxpayer, who is interested in his own capital and profits, perceives tax levy as a frustration, which is why he/she tries to avoid it, and generally displays a hostile attitude towards it.

For a proper operation of the economic system, the state must assume important responsibilities such as:

- Protecting the market against the freedom of initiative abuses;
- Ensuring the respect of natural and human values;
- Seeking and promoting general interest;
- Ensuring reliability of the value measuring system. Fiscality science must therefore develop reliable solutions to promote the public interest or, more accurately, to harmonise it with the individual interests of the people, because, after all, people are the utmost value.

In order to build a rational fiscal system, Fiscality must answer several questions first:

1. What is the meaning of tax, what are its reasons, its functions and defining characteristics?
2. What are the principles governing fiscal policy and what are the ways to harmonise their requirements?
3. Who are the taxpayers and who is the object of taxation?
4. How to decide and calculate taxes and how to levy them?

[36] Au secours de la TVA, Maurice Laure, 1959, p. 18

5. How big must fiscal burden be and how can tax evasion be prevented and fought?

The answer to these questions depends on multiple factors, such as the doctrine approved by the government, national traditions and pride, the need for harmonisation of fiscal systems under the impact of globalization and regional integration and so on.

Therefore, in addition to the common elements of different national fiscal systems, there are notable differences from one country to another. A comparative analysis can lead to finding solutions for harmonisation, a goal that cannot be ignored nowadays, as it is one of the foundations of fiscal reforms all around the world.

Fiscal harmonisation. Theory and practice

The growth of international trade and the increasing mobility of capital and people were the main factors that have reported the need to harmonise the tax systems of the countries involved.

The first step was to create the techniques to avoid international double taxation by establishing rational criteria for the tax treatment of revenues and assets abroad. The preferred solution was that of negotiating and signing of bilateral agreements to avoid double taxation.

The appearance of customs unions in the post-war period and the steps taken towards regional integration has raised the issue of removing barriers that prevented the free movement of goods, capital and people.

This has been an objective of the European Union since its creation in 1957. It meant first of all to have a functional European common market and to remove the existing barriers. Customs harmonisation was not difficult, with the experience of the Union between Belgium and Luxembourg and of the Benelux. The solution was to waive customs duty for mutual exchanges and to have a single customs tariff for trade with countries outside the Union. Customs harmonisation, however, was not sufficient to encourage and enhance trade between the Member States because there was still a strong fiscal impediment due to the different fiscal systems within the EU countries, which were not willing to give up their fiscal sovereignty.

There was much and profound heterogeneity in certain areas of public action and so, the adopted pragmatic and progressive approach was based on the principle of subsidiarity, which did not imply a centralization of abilities. In fiscal matters and in allocation policies, this principle means that national decisions prevail.

The idea was that the European community had no competence over fiscality. Fiscal matters were not included among the goals of the Community as set out neither in Article 2 of the Basic Treaty of Rome, nor in Article 3 on the activities of the Community. Since the Treaty of Rome was signed in 1957 until the Treaty of Nice[37] was signed in 2000, the member countries opposed the transfer of sovereignty in fiscal matters. Even today, despite attempts to create a Euro tax, there is still no such Community tax, although this idea has been brought to debate again.

Fiscal measures taken by the Member States may hinder the free movement of goods, services and capital within the Union. They can also lead to economic distortions incompatible with a single unified economic area or with the coordination of economic policies in the Euro area.

Seven of the articles of the basic Treaty (the Maastricht Treaty signed on 7 February 1992), guided by such a conception, contained explicit provisions on fiscal matters. The first four are incorporated in the chapter entitled "Fiscal provisions". Article 90 prohibits fiscal discrimination of any kind, articles 91 and 92 prohibit export subsidies and article 93 provides the legal basis for the harmonisation of indirect fiscality. The fifth article of the Treaty discussing fiscality (293) eliminates double taxation within the Community and articles 25 and 26 regulate customs matters. Numerous other items have fiscal references, namely, article 94 on the harmonisation of the laws and on direct fiscality.[38]

The whole Treaty, based on the balance between the principle of subsidiarity and community intervention confirms the sovereignty and national jurisdiction in fiscal matters, but requires the Community authorities to be concerned with the harmonisation of fiscal systems.

Moreover, fiscal harmonisation has proved indispensable for ensuring loyalty in the competition on the Community market, given that different taxation rules have a direct and powerful impact on the price and on choosing a location for production and distribution activities.

We can speak of three different levels of past fiscal harmonisation aims.

[37] The Nice Treaty of the European Union, 2001
[38] The Maastricht Treaty, signed on 7 February 1992 by the European Council

1. The first level consisted only in avoiding imbalances that could result from the complete opening of borders to trade in goods and for financial flows. This required a more or less ambitious harmonisation, depending on the extent of distortions to be avoided. To eliminate the risk of fiscal competition, such harmonisation was required to be decided collectively. The introduction and generalization of VAT in the EU countries is an example of such harmonisation.

2. The second level, more ambitious, would have meant to have a standard type of fiscal system at the EU level. This could present itself as a goal. But in truth, it has not been nor could it be a goal on a medium term. In fact, public spending has not been and it is not about to be standardized. Redistribution remains within a national framework. No one suggested that the wealthy Danish should contribute to help the poor Greeks or that the young Spaniards contribute to the good pensions of the German elderly. Certainly, integration offers poorer countries the chance of gradually reducing the disadvantage, but it does not mean that all European citizens will have the same quality of life in a foreseeable future.
3. The third level is a middle solution, favouring the rationalization of national fiscal systems so that they meet national requirements on collective consumption, but converge toward common results at EU level.

The fundamental democratic principle claims that the national character should be observed on a long term as it is difficult to have trust in a representative supranational and therefore sovereign organization. Also, national choices should not be dictated by those of the neighbouring states.

It means that the process of harmonisation is not a mere exercise of aligning the practices of each state to the Community's means of taxation so as to achieve standardisation. **Harmonisation does not mean standardisation.** Even in those cases in which serious steps towards harmonisation have been taken, no mandatory VAT flat rates have been imposed at Community level or a mandatory level for the harmonised excise tax. The solution was to observe minimum and maximum levels for standard rates and for lowered VAT rates and to observe a minimum level for excise taxes. But when a tax is found to be better than another, it is in everybody's best interest to adopt it.

Regarding the subject of harmonisation, there are at least two questions:

1. Which taxes should be harmonised?
2. What degree of harmonisation should be adopted?

It is not desirable to harmonise taxes whose impact is placed primarily on the household's income such as personal income tax, social security contributions paid by employees or inheritance tax[39].

In the case of companies, there is a different situation, as the decision regarding location is strongly influenced by a concern for minimizing costs and for maximizing the net expected return on investment. Two main categories of compulsory levies directly affect production costs: those that increase the cost of labour (social contributions paid by employers and taxes on wages) and those that affect the cost of intermediate consumption (mainly excise taxes, but not necessarily the VAT, which is recovered as it is deductible). On a long-term, the differences in the level of wages may offset fiscality differences so that countries with different systems can trade without major distortions.

However, on a short term, the change in levels of indirect taxation in one country is necessarily reflected in the activity of its partners. It is therefore necessary to harmonise certain changes in these two types of taxations.

Regarding the second issue, related to the degree of harmonisation to be adopted, the already anticipated idea should be reiterated, and namely that harmonisation does not mean standardisation. The study confirms that the existence of different VAT rates for goods, works, and services delivered favours tax evasion, both by the technical inadequacy of the state to manage these types of taxes and by significant costs of officials who must manage them.

Alternatives to harmonisation

There are two alternatives to harmonisation:

- The market;
- Negotiations.

Regarding harmonisation strategy, the different options bear the stamp of doctrines governing national fiscal policies and economic policies as a whole. These are often diametrically opposed, oscillating between the ultra-liberal trend and the most radical social democracy with tendencies of Community interventionism.

A need to harmonise the Romanian fiscal system and the EC fiscal system has occurred.

[39] Law 571/2003 on the Romanian Fiscal Code

Romania’s Association Agreement to the European Union signed in Brussels on 1 February 1993 stipulated that the harmonisation of Romanian tax legislation and the EEC legislation was one of the fundamental requirements for Romania's integration into European structures. Therefore, a major objective of the national strategy preparing Romania’s adhesion was to adapt its fiscal system to the requirements of a single market.

Romania applied for EU membership in June 1995, and was accepted as a candidate country in December 1997. Negotiations with Romania followed the decision of the European Council in Helsinki in December 1999.

One of the fundamental requirements of EU integration was to adapt the national legislation to the EU legal system - the acquis communautaire - and the candidate country's firm commitment to implement the legislation adopted after negotiations, even if it involves a period of transition.

For methodological reasons, the acquis communautaire was divided, in view of negotiations, into 31 chapters. The integration process also dealt with taxation issues and Chapter 10 "Taxation" is an important area of integration, given its impact on the normal operation of the EU single market[40].

The acquis on taxation is presented and structured in two fundamental objectives corresponding to the two types of taxes applied: indirect taxes that are best suited for harmonisation and direct taxes with limited harmonisation chances.

Harmonisation of legislation on mutual assistance in the field of direct taxation was achieved in the paragraph "Information exchange" of bilateral agreements concluded by Romania with all EU Member States, to avoid double taxation.

Through the same Position Paper from 2001, Romania committed to develop legal provisions and internal rules necessary for joining the Ministry of Finance to the Convention on Mutual Administrative Assistance in Indirect Tax Matters. It also implemented the VIES, FISCAL SCENT and SEED protocols and developed procedures to implement the Convention on Mutual Administrative Assistance in Tax Matters.

Complementary policies in harmonisation

The disappearance of tax frontiers and the fulfilment of requirements concerning the budget deficit and the public debt were not enough. A multitude of policies had to ensure that

[40] http://europa.eu

the conditions of accession and the economic and social framework able to support efforts to harmonise tax legislation were met. Economic policy with monetary policy had to jointly act on the evolution of social and economic status towards stabilizing the price level, balance of payments, the best use of labour force, to ensure a strong internal link between the economic and the social. The aim was to ensure a balanced sustainable economic growth. These policies also had to consider the effect of economic activities on the environment.

The removal of disparities between the different regions of our country was necessary to support sustainable growth and integration into the European Union[41]. Regional policy had to make use of interregional programmes to restore balance to the national level. The ultimate goal was to reduce the gaps between the Romanian economy and European economies.

Fiscal policy decisions to harmonise the structure of the fiscal system

The way in which the economic and social environment developed influenced fiscal policy decisions aimed at ensuring the structural evolution of the Romanian fiscal system and its integration into European fiscal economic dynamics.

Structural harmonisation of the European and Romanian fiscal systems was based on the principle of neutrality and moderation of fiscal burden. The former required the elimination of tax incentives that distorted competitive market relations and boosted legal tax evasion. The latter involved the decrease of fiscal burden on individual psychological decisions in the fields of labour, consumption, savings and investment. This meant reducing the government's intervention in the economy.

Since fiscal policy was an essential attribute of national sovereignty, making the right decisions to support the harmonisation process was a responsibility of Romanian government and political representatives.

Harmonisation was a lengthy process, and it was dependent on the policy mix pursued in the economy.

A systemic analysis of fiscality has allowed reflecting financially on the evolution of human societies[42], and on the theoretical efforts to seek effective solutions for solving problems in order to ensure functionality of economic and social systems.

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[41] Directive 2006/112/CE

[42] *Also see* Ricardo David - Des principes de l'economie politique de l'impot, Flammarion, Paris, 1977

General fiscal policy coordinates

One of the strongest human desires is to predict future developments. To foresee the directions of Romanian fiscal policy involved to foresee government and policymakers decisions that were difficult to predict. It was therefore preferable to determine some general coordinates arising from a pragmatic attitude emphasizing practical utility and efficiency of the fiscal system.

Although it impacts economy flows[43], the fiscal system is a tool for levying taxes and not for trend setting. Its use for interventionist purposes is aimed at amending relations between prices, may cause decreases in productivity and generate income redistribution that negatively influence individual psychological decisions.

Therefore, fiscal policy faces the difficult problem of ensuring maximum efficiency of a fiscal system capable of stimulating work effort, psychological decisions to save and invest, competitiveness and sustainable growth.

The trend to increase tax efficiency by indirect taxes, by increasing VAT rates and excise duties could become dangerous. These are passed on to the consumers, restrict consumption and fuel inflation. At the same time, they could become a barrier to an effective integration into the European single market.

Harmonisation of the Romanian and European fiscal systems

The integration of the national market into the European economic and social area has been a long process that required a comprehensive strategy and insight into the structural evolution of our economy. EU accession had both advantages and risks, to be identified and eliminated. It was necessary to harmonise supply and demand conditions in all sub-segments of the national market, with those of the European single market, as it would penalize structural units that were economically unviable or unable to adapt quickly to new competitive conditions. On the contrary, after joining the EU, Romanian businesses were able to act on a large and stable market, boosting competitiveness, growth and profitability of investments.

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43 Matei Gh. - Finanţe generale (General Finance), Mondo Publishing House, Craiova 1994

THE FISCAL POLICY – ROMANIA'S STRATEGY BEFORE EU INTEGRATION

In accordance with the Government Programme for 2004-2007, the fiscal policy strategy was structured to ensure, on the one hand, an accelerated reform in this area, with positive effects on the national economy and, on the other hand, to achieve the harmonisation of the Romanian tax legislation with the Community legislation in the field.

Indirect taxation is the field in which there were the most notable harmonisation attempts and successes registered. From the very beginning, this was a very pressing issue, given that consumption taxes sensibly affect prices paid by the end consumer, and the differences in their application could not provide the fiscal neutrality necessary for fair competition on the Community market. The main concern was directed towards the most important indirect taxes: VAT and excise taxes. The action aimed at harmonising national fiscal systems so as to make their provisions compatible among each other but also to ensure their compatibility with the objectives of the EC Treaty.

In our opinion, the EU fiscal policies should aim at: ensuring the stability of tax revenues in Member States, ensuring the smooth functioning of the single European market and contributing to the employment issue.

We believe that the European Union could develop new actions to strengthen the common VAT system in particular by a more thorough research and by a clear definition of the following main aspects:

- VAT tax base
- defining VAT payers
- exemptions
- applying nearly similar rates

We believe that the principle of taxation at origin (territoriality and place of taxation) should be defined to eliminate the cumbersome operations of triangular type.

The long-term strategy maintains the current regime focusing on four main objectives: simplification, modernization, more uniform application of existing rules and strengthening administrative cooperation.

The tendency to standardise VAT rates

Switching to taxation in the home country had the risk of increasing tax competition if the rates remained strongly differentiated between the member countries. Therefore, the following step needed was that of a gradual adjustment of their level. To this end, in 1987, the

Commission proposed to the Council a two VAT rate system, one between 4-9% for the lower rate and one between 14-24% for the standard rat. Each country could choose its right level. Border tax adjustments would be eliminated, which now would be carried out through the clearing house mechanism which presented a risk of major fraud and the proposed scheme was considered too inflexible.

In 2006, the minimum rate was observed by the Member States, including the states that joined in 2004. EU states have been concerned with the budgetary impact assessment and macroeconomic effects of VAT harmonisation.

ASPECTS CONCERNING VAT IN ROMANIA AND ITS HARMONISATION WITH THE EU MODEL

Value added tax was introduced in Romania on 1 July 1993, replacing the turnover tax which had acted for decades as a universal tax on consumption. Introducing VAT was one of the fundamental measures taken by Romania in order to reform its fiscal system. The experience of France and its attempts to harmonise its VAT with the 6th Directive of the EEC Council were beneficial for Romania and helped build the Romanian taxation model and its gradual harmonisation with the EU model.

Until the introduction on 1 January 2004 of the Fiscal Code, which is the legal basis for VAT, the measures taken over the years helped the harmonisation process. New provisions were included in the new fiscal code and in the fiscal policy strategy for the pre-accession period.

During 2004-2006, the value added tax legislation was subject to changes in order to harmonise it with the 6^{th} Directive of the Council of the European Economic Community according to the schedule annexed to Romania's Position Paper on Chapter 10 - Taxation.

The current Fiscal Code regulates in detail the VAT regime stating: its scope, the taxable people and transactions, their place, generating event and playability, tax base, legal quotas, operations exempt, deduction system, determining the tax due, payment and disbursement regulation, the special exemption regime and obligations of VAT payers.

The budget and the budget balance between 1989 and 2007

Due to the difference between the total revenue and the total expenditure of the state budget, resulting in a budget surplus or deficit, as can be seen both in the table analysis and in the graphic included in the present thesis, we can notice the following aspects (for the period 1989-2007):

- The only year with a budget surplus was 1989;
- The graphical analysis shows a steady and permanent increase both in income and expenditure of the state budget; the increase of state budget expenditures was constant and accelerated, hence the permanent deficit for each fiscal year in the study;
- For the financial years 1990-2002 there is a continuous increase in the deficit;
- The highest budget deficit was in 2002, when it reached 47.618.000 million ROL, after which there was a decrease of the deficit until 2004. In 2005, it began to slightly increase and then decrease in 2006 and 2007. The decrease of the budget deficit is based primarily on growth in absolute terms and in real terms of the total revenue collected from the state budget.

The surplus/deficit reflected by the graph shows the only year with a surplus, namely 1989. From 1990 to 2007, the budget deficit was quite high, especially in 2002. Starting with 2006, the budget deficit in absolute values registered an abrupt increase (by almost 5 times if we compare 2006 and 2007 to 2005).

The tax revenues to the state budget registered a weighted increase until 1998, which is the first year in the period 1991-2007 when there was a significant increase in tax revenues. The budget structure for the years 1989, 1990 did not contain a distinct chapter on tax revenues.

The highest weight of direct tax in total budget revenues was recorded in the fiscal year 1992 and the highest weight of VAT in total budget revenue was recorded in 2006.

The highest VAT percentage of total indirect taxes was registered in 2005. The year 2004 registered a significant decline from 2003. We can easily notice in the evolution of the weight of indirect taxes in total revenue (in the case of VAT) the tendency of fiscal burden to shift towards the end consumer.

The highest social and cultural expenditures as a share of total budget expenditures were registered in 1990 (43.56 %). Then they decreased from 1992 to 2004 (by around 25 -

29%) and then slightly increased again in 2005. In 2007, there was a decrease in the percentage of these types of expenses. It is noted that, although they are called social and cultural expenses, the emphasis was on social spending, because this was a major problem faced by people and governments of Romania after 1990.

Regarding the expenses with interest payments and other expenses related to public debt, as a share of total expenditure, the year 2000 seems significant in that their weight was very high compared to previous years, which demonstrates the Romanian state's effort to pay interest on the public debt and the public debt itself.

Regarding the external public debt, we can notice that its share in GDP was about 22 % in 1996 and 2000 and smaller in the rest of the years. The year 1990 stands out (the year following payment of foreign debts by the communist regime) as the public debt of Romania in GDP was 0.9 %, which, in addition to its positive feature also created a negative effect, namely fewer investments and less development. For the positive economic development of developing countries, foreign loans play a vital role.

Indirect taxes as percentage of the total revenue tended to decrease from 1990 to 1995; direct taxes increased during 1990-1995. In the year 1995, indirect taxes quickly surpassed direct taxes (during 1995-2007), proving the shift of the taxation system to end consumers as direct fiscal burden. After 2000, the share of the two types of taxes in total revenue remains approximately constant.

Conclusions

The fiscal policies promoted by Romanian governments influenced both the structural evolution of the fiscal system and the extent of the tax levies. The extent of tax incentives (exemptions, discounts, and deductions), the level and nature of tax rates, and the sensitivity of the taxable matter influenced the fiscal burden exerted by each tax and by the fiscal system as a whole[44].

Other key factors are found in the real economy: the level of economic development, assets structure, the structural distribution of revenue, the structural evolution of global consumption, structural changes in the labour force, etc. They are an expression of the whole economic and social policies pursued in the economy. In turn, the quality of the management of state tax claims and the population's tax education level continues to influence tax revenues and fiscal burden through tax both at individual level and at the level of socioeconomic groups.

An analysis of the overall state of the economy and of the structural evolution of the fiscal system leads to a more nuanced conclusion. The re-conversion of the property right on productive capital was relatively low[45]. Instead, tax rates showed a slight increase or compensatory changes in fiscal burden at the different tax categories. Actual decreases had almost no importance.

In turn, taxable matters tended to compress until the end of 1993[46]. Later, they began to fluctuate and rise.

Consequently, we cannot ignore the influence on the tax levy of factors specific to the transition period. Government ordinances passed year after year approved deferred payment of tax debts. These were not always generated by the payment default of debtors. Due to financial indiscipline and to its stimulation by deferring tax debts, tax arrears increased as penalties were lower than the interest rates. Tax arrears became attractive and they were used to finance economic activities. Also, tax fraud from the black or parallel economy, influenced the level of fiscal burden.

44 *Also see* Andriescu Aurel and Băghină Gh. - Legea pentru aşezarea contribuţiunilor directe asupra veniturilor,. Legea timbrului şi a impozitului pe acte şi fapte juridice - Legea impozitului pe lux şi cifra de afaceri (The Law on direct contributions to revenues, the Law of the stamp and of taxes on legal documents and activities, The law on luxury tax and turnover) Remus Cioflec Printing Press, Bucharest, 1948

45 Davin N., H.Y.Man - Public Finance: A contemporary Application of Theory to Policy - Chicago: The Dryden Press, 1990

46 *Also see* Ricardo David - Des principes de l'economie politique de l'impot, Flammarion, Paris, 1977

It is not enough to know the share of GDP used from the exchange economy to finance public economy[47], or the nature of revenues on which budgetary stability is based. As a result of the impact, repercussions and incidence of taxes, each of them influences on subjects and flows generated by their activities in the economy. At the same time, each tax has a degree of sensitivity to fluctuations in the economy. A more thorough structural analysis of statistical information reflects prevalence of funding budgetary resources at both central and local level on account of direct taxes.

The distribution system of wages promoted in the economy disrupted the correlation between the price of labour and education and training, or the importance of social labour, and economic price developments of goods or services, which have become the same or higher than those on the world market. So the price of Romanian labour is an exception. It did not register the same trend of harmonisation in the absence of coherent economic and wage-related policies. Consequently, the income distribution policy generates economic distortions between income and consumption.

Investing, stimulating capital accumulation and risk-taking needed a decrease of fiscal burden on the realized and reinvested profit[48]. The budget deficit, the lack of other fiscal resources and high fiscal burden exerted by the payroll tax, VAT and excise taxes have not allowed measures to be taken in this regard.

Thus, the contribution of VAT to finance the state budget is comparable to that of the payroll tax. Pressure from all indirect taxes on used revenue exceeds the direct pressure of the payroll tax on achieved revenues. The measures to reduce payroll tax progressivity and increase VAT tax rates[49] are:

• fostering and maintaining a process of real and sustainable income saving by people with a high income;

• increase commodity and economic services prices;

• compensatory income effects among people with low incomes. This compensatory effect is estimated to also occur with the state budget.

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47 Bălănescu Rodica, Corduneanu Carmen, Dorina Antohi, Adriana Negoiţă - Sistemul de asigurare a veniturilor la Bugetul statului prin intermediul pârghiilor financiare în contextul implementării economiei de piaţă în România (The system of ensuring revenues to the state budget through financial leverage within the context of a market economy implementation in Romania), I.F.P.P.V. Bucharest, 1991

48 *Also see* Philippe Colin, Gilles Gervaise - Fiscalite pratiques des affaires avec 15 etudes de cas, Ed. Clet, Paris 1990

49 Corduneanu Carmen, Rodica Bălănescu - Taxa pe valoarea adăugată în economia concurenţială (Value added tax in the competitive economy), CIDE – Romanian Academy, Bucharest, 1992

The problem of the Romanian economy is the lack of financial capital. Its absence leads to stagnation of reforms. A global view on the economy in terms of flow shows that the distribution of revenue flows generates distortions on the decisions to stimulate work, risk taking, education and increasing the level of professional training. The redistribution of revenue through taxation, plus the rest of compulsory levies, generates new distortions as they influence psychological decisions to work, invest and consume.

For the attraction of foreign capital to be efficient, it has to be permanently present in the economy, along with the national capital. There should be no decisions likely to distort competitive relations. Supporting the reform process requires to discourage capital immobilization in unproductive assets.

A decrease of the fiscal burden also requires reducing public spending, whose growth has become explosive. Reform of the public economy involves reviewing the efficiency of organizations, institutions, agencies, created in crisis or under pressure. Many micro-public entities created use resources without providing real public utility or they should operate in a competitive exchange economy and not in the public economy.

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