General Issue on the Romanian fiscal system

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GENERAL ISSUES ON THE ROMANIAN FISCAL SYSTEM

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1. ANALYSIS OF THE ROMANIAN FISCAL POLICY

The arrangements of the economic and fiscal reform as well as the operating economy influenced the evolution of the fiscal revenues within 1990-2004, in Romania. *Against the background of the State's receding involvement on the economic and social level*, a fall of public costs generating a fall of the necessary budget to cover these costs occurred, amplified by the economic decline in Romania, registered in 1990. Table 1 shows the evolution of the fiscal system in Romania for a given period of time.

Table 1
Evolution of fiscal income in Romania (per inhabitant, in USD) and the tax level, during 1990-2004

YEAR/ FACTORS	Average GDP/ inhabitant (USD)	Average fiscal income/ inhabitant (USD)	General tax level* (% of GDP)	Partial tax level ** (% of GDP)	Tax level for social purposes*** (% of GDP)
1990	1648	585	35,5	27,6	7,9
1991	1244	413	33,2	23,2	10,0
1992	859	288	33,5	23,2	10,3
1993	1158	362	31,3	22,0	9,3
1994	1323	373	28,2	20,3	7,9
1995	1564	451	28,8	20,9	7,9
1996	1563	420	26,9	19,4	7,5
1997	1565	415	26,5	20,0	6,5
1998	1844	521	28,2	20,3	7,9
1999	1585	476	34,4	22,4	9,0
2000	1645	484	29,4	18,6	10,8
2001	1773	502	28,3	17,4	10,9
2002	1898	545	28,8	17,8	10,0
2003	2304	567	28,2	17,3	10,9
2004	3165	582	27,4	17,0	10,4

*General tax level. (duties + taxes + contributions) * 100/GDP
**Partial tax level. (duties + taxes) * 100/GDP
***Tax level for social purposes. (Compulsory contributions) * 100/GDP
Source : www.mfinante.ro , www.bnro.ro data

Concerning the *general tax level*, counting duties and social contributions, there is a fall during 1990-1997 from 35,5% to 26,5%, then it had a fluctuating evolution around 30% of GDP according to the economic framework, registering a growth of 31,4% in 1999, because of the economic crisis and the economic reform arrangements, decreasing to 28,3% in 2001and 27,4% in 2004, due to the economic development and reduction of tax rates. A distinct analysis of the *partial tax level*, counting only duties and taxes, reveals a different evolution confronted to the *tax level for social purposes.* It notes a 10 percentage points reduction in the case of the partial tax level (from 27,6% in 1990 to 17,0% in 2004), while the tax level for social purposes registered close values at about 10% of GDP, during the entire period. During 1991-1997, the two factors had a similar evolution, recording important reductions till 1997, then a slight increase, having distinct evolutions in 2000 and 2001, the partial tax level indicates a 5 percentage points reduction, while the tax level for social purposes indicates a 2 percentage points growth, their evolution remains constant till the end of the period.

A careful analysis of the *tax level full value*, per inhabitant, conveyed in USD suggests a relatively large variability from 362 to 582 USD, except 1992 when the value was of 288 dollars, because of the falling gross domestic product per inhabitant, representing half of the value registered in 1990. The tax level evolution per inhabitant, presented in Table no.1, notes a dramatic fall from 585 USD to 288 USD during 1990-1992, then a growth at over 500 USD in 1998 and similar values till 2004.

2.COMPARISON TO THE MEMBER STATES OF THE EUROPEAN UNION

Compared to other European countries, members of the European Union, we remark *a low general tax level registration in Romania*, the comparison is available for the partial tax level as well as for the tax level for social purposes.

Table 2

Trends in the tax burden (EU countries and Romania - % of GDP)

Country/ Year	1999	2000	2001	2002	2003	Country/ Year	1999	2000	2001	2002	2003
Austria	45,7	44,7	46,5	45,4	44,8	**Sweden**	54,6	54,7	52,9	51,0	51,4
Belgium	48,1	48,0	48,2	48,7	48,1	**United Kingdom**	38,1	38,7	38,4	37,0	37,1
Denmark	52,3	50,4	50,7	49,7	49,8	**Cyprus**	29,5	31,4	32,7	32,5	34,3
Finland	47,2	48,2	46,2	46,1	45,1	**Czech Republic**	34,8	34,5	34,6	35,5	36,2
France	47,3	46,8	46,5	45,6	45,7	**Malta**	29,5	29,7	31,9	34,3	34,2
Germany	43,9	44,0	42,2	41,7	41,7	**Estonia**	34,4	32,2	31,6	32,4	33,4
Greece	39,6	40,9	39,2	39,8	38,6	**Hungary**	39,2	39,6	39,3	38,9	39,2
Ireland	33,4	33,3	31,6	29,8	31,2	**Latvia**	32,6	30,3	29,1	28,9	29,1
Italy	43,6	43,1	42,9	42,4	43,2	**Lithuania**	32,1	30,2	28,8	28,6	28,7
Luxembourg	41,5	41,4	41,6	42,1	42,3	**Polonia**	37,2	35,2	35,4	35,5	35,8
Netherlands	41,6	41,5	40,0	39,4	39,3	**Slovakia**	34,7	33,2	32,1	32,5	30,9
Portugal	36,7	37,3	36,5	37,5	38,1	**Slovenia**	39,8	39,3	39,4	39,7	40,3
Spain	35,3	35,9	35,7	36,2	36,5	**Romania**	***34,4***	***29,4***	***28,3***	***28,8***	***28,2***

Source: EUROSTAT, Statistics in Focus, Economy and Finance, 3/2005, „Tax revenue in EU Member States: Trend, level and structure 1995-2003"; www.mfinante.ro

The conclusion arising from these comparisons is that the tax level in Romania is very reduced, thing that contradicts the Romanian citizens' attitude towards taxes considering the tax system as being suffocating. To explain this contradiction, a complex analysis beyond figures will be used in order to understand the public attitude.

In order to have a correct image of the tax system, it is important to mention that bearing 500 USD of a 1500 USD gross domestic product, per inhabitant is harder than bearing 10000 USD of a 30000 USD gross domestic product, per inhabitant, although in both cases the tax level is the same 30%. For the first situation the remaining sum does not cover a decent standard of living. Another issue is the fact that the tax level represents a ratio of tax revenues really collected within a year, indicating only a part of the total due amount owed by the tax payers according to the effective fiscal legislation and the GDP.

Considering that tax revenues really collected by the government represents only half of the total amount of fiscal obligations owed by the tax payers according to the law, then tax level indicates 50 – 60% of the GDP. There are Romanian tax payers who declare and pay the correct value of due taxes and social obligations, for them the fiscal system becomes suffocating. But there are tax payers who do not declare or pay or pay only a part of due taxes and social obligations, bearing a low tax level.

3. TAX REFORM, THE INTRODUCTION OF THE UNIQUE TAX SHARE AND SALARIES TAX

Tax reform is applied at the beginning of the year 2005 (its purpose being the introduction of the unique tax share), presented as a fiscal relaxation supporting private enterprises, foreign investments and free enterprise, leading to the consolidation and development of the market economy in Romania, an important condition for the adhesion to the European Union.

In order to fill the gaps generated by the fiscal relaxation, Ministry of Public Finance proposed unpopular fiscal arrangements, resulting from the negotiations with IMF such as doubling the sales revenue tax for micro-enterprises, blocking the social security contributions fall, postponement of the raise of budgetary salaries and pension reform, doubling the dividend taxes for individuals, raise of bank interest taxes and of profit taxes in the capital market ten times, drastic taxation of real estate business and rents.

The main issue remains the materialization of the tax reform into a fiscal relaxation policy stimulating the economic competitiveness or just a mere rearrangement of duties and tax system, fostering certain groups of interests (persons with high income) and damaging fiscal equity and social justice principles. Does the government possess a coherent fiscal strategy in order not to disturb completely the fiscal administration, collection, proceeding and tax return system? Analysts pointed out that the unique tax was a rule in all industrialized states in the first decade of the 19^{th} century, but there were demands for a “strong progressive or gradual” tax system noted for the first time in Karl Marx's communist manifest in 1848. Such a system was embraced first by capitalist states. Since then, the idea of a unique tax was brought to life several times, a considerable number of countries have adopted different variants of the unique tax regime. But still no major occidental economy has reconsidered the unique tax regime.

A modern reborn of the unique tax revenue was initiated by Estonia in 1991, followed by Latvia (1994), Lithuania (1994), Russia (2001), Serbia (2003), Ukraine (2003), Slovakia (2003), Georgia (2004) and Romania (2005). Hungary seems to consider the passage to a unique tax version for the future.

Table 3

Maximum tax revenue and corporatist tax in EU 25 and Romania

Country	**Personale income tax (%)***		**Corporate income tax (%)**		Country	**Personale income tax (%)***		**Corporate income tax (%)**	
	2004	2005	2004	2004		2004	2005	2004	2005
Austria	50	50	34	34	**Sweden**	60	60	28	28
Belgium	50	50	33	34	**United Kingdom**	40	40	30	30
Danemark	59	26,5	30	30	**Cyprus**	30	30	15	15
Finland	36	35,5	29	29	**Czech Republic**	32	32	31	28
France	49,6	49,6	34,3	34,3	**Malta**	35	35	35	35
Germany	48,5	47	27.9	26,4	**Estonia**	26	26	0	0
Greece	40	40	35	35	**Hungary**	40	38	18	16
Ireland	42	42	12,5	12,5	**Latvia**	25	25	19	15
Italy	45	45.6	34	34	**Lithuania**	33	33	15	15
Luxembourg	38,95	38,95	30,38	22,9	**Polonia**	40	40	27	19
Netherlands	52	52	34.5	34,5	**Slovakia**	38	19	25	19
Portugal	40	40	30	30	**Slovenia**	50	50	25	25
Spain	48	45	35	40	**Romania**	40	16	25	16

* maximum level

Source : www.worldwide-tax.com

This popular arrangement for the passage to a fix taxation system is justified by healthy fiscal strategies or by the desire of convincing citizens to contribute to the state budget, represents the subject of an entire debate.

Leaders of developed economies in Europe, such as the German chancellor Gerhard Schroder and the Swedish Prime Minister Goran Persson showed that transition economies in East can afford a reduction in taxes, because the income losses are compensated by subsidies coming from the European Union. This argument was rejected many times by the States in transition pointed out. Germany as well as Austria, Italy, Finland, Danemark and Greece agreed for a tax fall in order to encourage the investments and costs (consumption) and to determine an economic development.

The high tax level in Romania is generated by the salaries tax allocated under the form of social contributions, for the year 2005. This issue can be analysed according to the data in table 4.

Table 4
International comparisons of social contributions. 2005 (%)

Costs		Romania	Czech Republic	Slovenia	Poland	Hungary	Slovakia	France
Social security	**Total**	**31,5**	**34,0**	**24,35**	**19,52**	**18,5**	**18,0**	**6,65-9,80**
Compensated	*employee*	-	8,0	-	-	-	-	0,10
	employer	-	26,0	-	-	-	-	1,60
Uncompensated	*employee*	9,5	-	15,5	9,76	0,5	4,0	6,55
	employer	22,0	-	8,85	9,76	18,0	14,0	8,2
Health security		-	-	-	-	8,0	-	-
Health contribution	**Total**	**13,5**	**13,5**	**13,45**	**13,0**	**15,0**	**14,0**	**-**
	employee	6,5	4,5	6,36	6,5	4,0	4,0	-
	employer	7,0	9,0	7,09	6,5	11,0	10,0	-
Sickness preventing contrib	Total	-	-	-	2,45	-	2,8	-
	employee	-	-	-	2,45	-	1,4	-
	employer	-	-	-	-	1,4	-	-
Private health security	*employer*	-	-	-	8,5	-	-	-
Unemployment	**Total**	**4,0**	**-**	**0,2**	**-**	**3,0**	**2,0**	**6,4**
	employee	1,0	-	0,14	-	-	1,0	2,4
	employer	3,0	-	0,06	-	3,0	1,0	4,0
Risk and accidents preventing	*employer*	0,5	-	-	1,93-3,86*	-	0,8	-
TWD commission	*employer*	0,75	-	-	4,5	-	-	-
Maternity leave funds	**Total**	**-**	**-**	**0,2**	**-**	**-**	**-**	**-**
	employee	-	-	0,1	-	-	-	-
	employer	-	-	0,1	-	-	-	-
Profit participation funds	*employer*	-	-	-	0,15	-	-	-
Contrib. for work formation	*employer*	-	-	-	-	1,5	-	-
Contrib. for disabled persons	Total	-	-	0,2	-	-	6,0	-
	employee	-	-	0,1	-	-	3,0	-
	employer	-	-	0,1	-	-	3,0	-
Insurances	*employer*	-	-	-	-	-	0,25	-
Reserve fund	*employer*	-	-	-	-	-	4,75	-
Widowhood securities	*employee*	-	-	-	-	-	0,1	-
Family support	*employer*	-	-	-	-	-	5,4	-
Total amount of Employee's contributions		17,0	12,5	22,2	18,71	12,5	13,5	
Total amount of Employer's contributions		33,25	35,0	16,2	29,29-31,22	33,5	40,35	
TOTAL		**50,25**	**47,5**	**38,4**	**48-49,93**	**46,0**	**53,85**	

Source : PriceWaterhouseCoopers. 2005

At the moment, in Romania, social security contributions (SSC) represent 49,5% for employers and employees cumulatively, there is a commission of 0,75% payed by the employers, its beneficiaries are Territorial Work Departments. These costs are similar to the SSC level in Poland (48-49,33%) and higher than in Czech Republic (47,5%), Hungary (46%) and Slovenia (38,4%).

According to the Pre-adhesion Economic Program, the present government considers the fall of social contributions in the future, 10 percentage points in reduction until 2008. Thus contributions should reduce to 3% in 2006, 4% in 2007 and 3% in 2008 and aiming at the employers' ratio.

4. CONCLUSIONS

Compared to other sates, the average tax level in Romania is low around 30% of GDP, but it has an unequal distribution, while some of the tax payers allocate a tax level of 10-20%, others are forced to support a ratio of 50-60%.

Critics consider that the introduction of a unique tax share is a hasty arrangement with no substantiation or impact analysis, jeopardizing the budget balance. Other increase in tax and duties, utilities costs, appearance of new taxes and reduction in budget costs followed.

The renunciation to progressive levying of taxes (fiscal equity principle) and the introduction of unique tax share roused a series of pro and against reactions. Ignoring these controversies concerning work tax in Romania, the tax revenue and high social contributions remain an unsolved problem.

In Romania, the fall of social security contributions may provide the elasticity of the work market developing the power to encourage internal and foreign direct investments as well as the consumption of the Romanian economy.

The three important aspects of the Romanian economy are : the introduction of the unique tax share of 16%, the stimulation of work market and the blocking of qualified manoeuvre migrations abroad.

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