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2009

Online at <https://mpra.ub.uni-muenchen.de/20978/>

MPRA Paper No. 20978, posted 26 Feb 2010 06:54 UTC

# THE IMPACT OF ECONOMIC CRISIS ON THE FISCAL REVENUES

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## *Abstract*

*This paper tries to evaluate the situation of the fiscal revenues in Romania in the context of economic and financial crisis, because the fiscal revenues are the major source of financing the public expenditure. The evolution of the level of fiscal revenue is very important because maintain the budget equilibrium. The article reveals the major trends of the fiscal revenues after EU enlargement and in the actual context of economic crisis and the impact on the budget deficit and the public debt. The state intervention in revive of the economy has to be financed through the budget, and this means a higher budget deficit. The proper solution in this condition for assuring the financial stability of the economy it was an external borrow from IMF.*

*Key words: fiscal revenues, budget deficit, public debt*

*The article's JEL code: H2, H62, H63*

## **Introduction**

The fiscal revenues are the most important source of financing the public expenditure in any economy through the public budget. The level of the fiscal revenues is determined by the fiscal policy adopted by the government, but also the evolution of the economy.

Despite a sharp drop in the last quarter of the year, GDP growth accelerated to 7.1% in 2008, from 6.2% in 2007. In the first three quarters, domestic demand for both consumption and investment boomed at double digit rates, fuelled by strong wage increases and a rapid expansion of credit. Net exports continued to record a negative contribution to GDP growth.<sup>1</sup>

In Romania, at the end of 2008 the effects of economic crisis are revealed by the evolution of the fiscal revenues: starting October, budget revenues decrease by 10% each month, according with HotNews.

The Romanian budget deficit for 2008 registered the higher value from the last years as a result of a lax fiscal policy and lower than expected revenues. The lax fiscal policy it was caused by the tax competition in which Romania it was engaged starting with 2005 with the introduction of the

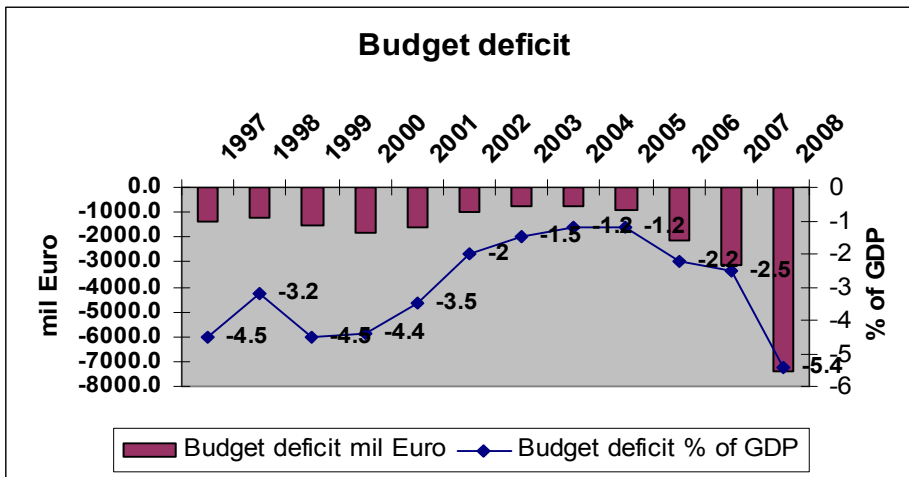
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<sup>1</sup> Economic Forecast, Spring 2009, European Commission, Directorate-General for Economic and Financial Affairs, 3/2009

flat tax. But the lower fiscal revenues are a direct consequence of the economic crisis, because many companies which in 2008 obtained profits and paid taxes, in 2009 are closed. In these conditions the budget revenues are not enough for financing the public expenditure. For reducing the budget deficit the government planned to reduce some expenditure and in the same time to increase some taxes and even introduce a new one: the minimum income tax for companies. Austere fiscal measures planned as a result for 2009 will impact on wages and social security, affecting consumer spending and economic growth.

### The long term budget revenue analysis

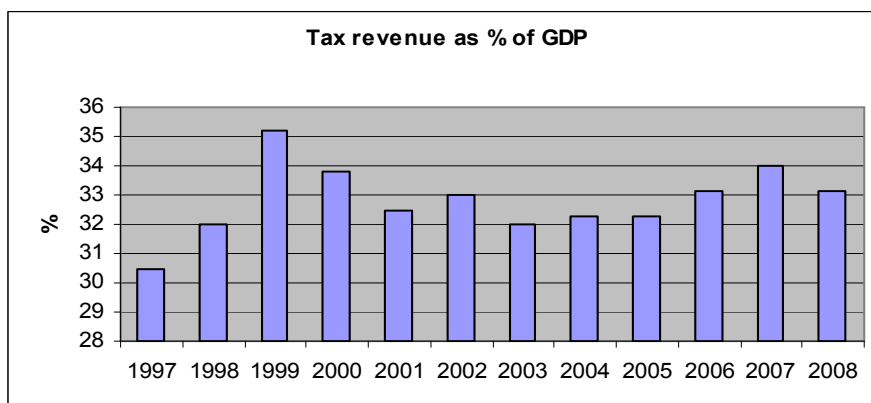
The study starts with a short analysis of the evolution of the budget revenues and budget deficit in the recent years. The budget deficit beginning with 2000 year is continuously decreasing until 2005, when start to increase, but it was below Stability and Growth Pact requirement of 3% of GDP, as can be see from the next figure.



Source: Eurostat

In 2008 the level of budget deficit is more than double comparative with the level of 2007, and this means 5.4% of GDP.

This was mainly due to substantially higher-than-planned current spending, notably in public wages and social transfers. In addition, overly optimistic revenue projections did not materialize and a sudden drop in revenue collection in the last two months of the year owing to the economic slowdown added to the worse than expected outcome.



Source: Eurostat

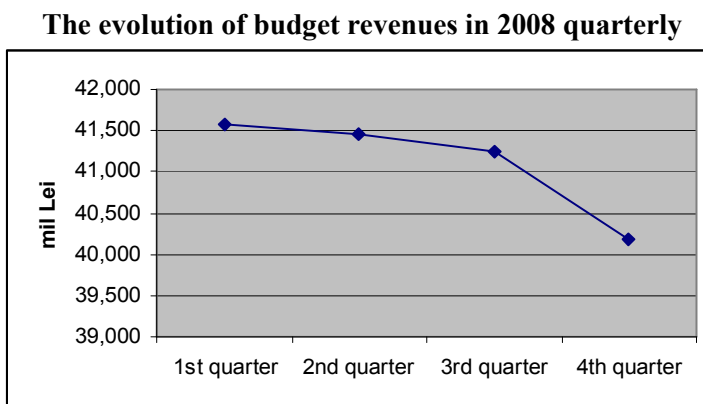
The evolution of the total tax revenue in the last ten years reveals that starting with 2005 we have an increasing of the tax receipt until in 2008. Because in this period the fiscal policy was unchanged the only cause for this decreasing remains the economic crisis, which affect not only companies but also individuals, who loss their jobs, and in this condition the income tax and consumption tax are decreasing.

### **The effects of the economic crisis on the tax revenue**

The effects of the financial and economic crisis became obviously in our country starting with the last quarter of 2008, when the economic growth it was only by 2.9% comparative with the entire year, when the economic growth it was 7.1%. In the last quarter of 2008 comparative with the same quarter of 2007, can be observed the follow trends (in the real terms)<sup>2</sup>:

- the growth of the gross value added with only 3.5%;
- decreasing of the total consumption with 2.8%;
- increasing of the gross fixed capital formation with only 2.8%;
- increasing of the exports with 1.6 %;
- decreasing the imports with 10.2%.

In 2008 the general budget revenues decreasing from one quarter to another, though these reductions were not so significant. Budget revenues decrease in the last quarter with 2.6% comparative with the 3<sup>rd</sup> quarter of the same year.<sup>3</sup>



Source: Raport privind situația macroeconomică a României pentru anul 2009 și proiecția acesteia pe anii 2010-2012

In 2008, comparative with 2007, the public budget revenues have registered an increasing in nominal terms, with almost 29%. The most important increasing have been for: corporate tax with 23.6%, income tax with 27.8%, VAT with 30.8%, excises with 8.7% and social contribution with 24.7%. These evolutions of tax receipts have been take place in the conditions in which GDP increased with 7.1% in the real terms and consumption with 8%<sup>4</sup>.

In 2009 when the economic crisis conditions becoming worse, as a consequence of decreasing the activity in many sectors of the economy, the state revenues were affected. The decreasing trend of tax revenue is obviously in the first quarter of 2009.

<sup>2</sup> National Institute of Statistics, Press statement no. 41/4 march 2009

<sup>3</sup> Raport privind situația macroeconomică a României pentru anul 2009 și proiecția acesteia pe anii 2010-2012

<sup>4</sup> National Institute of Statistics, Press statement no. 41/4 March 2009

### The major tax receipts realized in 2007 and 2008



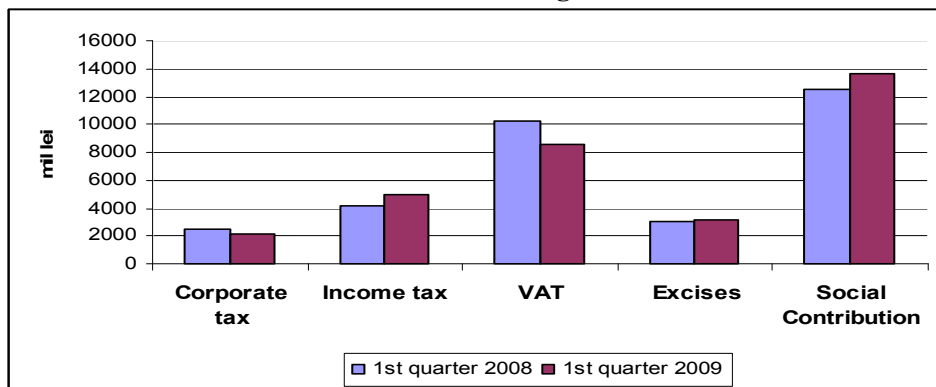
Source: Public Finance Minister

Budget revenues declined with 7.06% in the first quarter of 2009, (from 32.65 lei) compared to Q1 2008 (35.13 billion lei), according to Romania's National Fiscal Administration Agency (ANAF)<sup>5</sup>.

Concerning the major categories of taxes realized by ANAF in the 1st quarter of 2009 comparative with the same period of 2008 it can be observed the follow trends (in the nominal terms):

- decreasing of the corporate tax receipts with 13.7% (because for many companies the profits are lower);
- increasing the income tax receipts with 21.2%;
- decreasing of VAT receipts with 16.8% (this is a consequence of decreasing consumption);
- increasing excises receipts with 6.2% (because the excise rates were increased starting with 2009);
- social contribution receipts are higher with 8.8%.

### The evolution of main categories of taxes



Source: ANAF

### Conclusions

For the next period tax revenue has to be higher due to introduction of lump-sum tax and increasing the social contribution rate. These measures are not enough for assuring the budget equilibrium and the capacity of the budget to sustain all the public expenditures in the context that the effects of economic crisis are more pregnant. Much more the state intervention in revive of the economy has to be financed through the budget, and this means a higher budget deficit.

<sup>5</sup> Romania's National Fiscal Administration Agency, Press statement no. 109 0266/08.04.2009

The proper solution in this condition for assuring the financial stability of the economy it was an external borrow from IMF.

The deficit is projected to decline to 5.1% of GDP in 2009. The 2009 budget adopted in February 2009, contains several measures to lower the deficit, including a recruitment freeze and the reduction of various bonuses in the public sector, cuts in expenditure for goods and services and subsidies, limiting pension increases to inflation and a bringing forward of the schedule to increase excise taxes. On the revenue side, are taken some measures like eliminating certain tax deductions and allowances (in particular on company cars and depreciation of revalued assets). On the other hand, the government plans a substantial increase in public investment in 2009 compared with 2008. These measures are reflected in a budget rectification approved by the government in April 2009.

### References:

1. Romania's National Fiscal Administration Agency, Press statement no. 109 0266/08.04.2009; Press statement no. 943 133/09.04.2008
2. National Institute of Statistics, Press statement no. 41/4 March
3. Economic Forecast, Spring 2009, European Commission, Directorate-General for Economic and Financial Affairs, 3/2009
4. Raport privind situația macroeconomică a României pentru anul 2009 și proiecția acesteia pe anii 2010-2012

### Annex 1. Budget Revenue in 2008, quarterly (mil. lei)

	Total 2008	Q1	Q2	Q3	Q4
Revenue	164.466	41.584	41.454	41.252	40.176
Change of the previously quarter			-0,3%	-0,5%	-2,6%

Source: Raport privind situația macroeconomică a României pentru anul 2009 și proiecția acesteia pe anii 2010-2012.

### Annex 2. The major tax receipts realized in 2007 and 2008 (mil. lei)

	2007	2008
Corporate tax	10558,3	13045,9
Income tax	14374,9	18365,7
VAT	31243,2	40875,1
Excises	12511,8	13599,4
Social Contribution	38843,0	48419,8

Source: Public Finance Minister

### Annex 3 The evolution of main categories of taxes (mil. lei)

	Q1 2008	Q1 2009
Corporate tax	2.461,99	2.125,63
Income tax	4.119,11	4.993,91
VAT	10.264,16	8.535,52
Excises	3.018,21	3.206,29
Social Contribution	12.503,50	13.600,02

Source: Romania's National Fiscal Administration Agency, Press statement no. 109 0266/08.04.2009; Press statement no. 943 133/09.04.2008