

# POSITION OF THE ROMANIAN TAX SYSTEM WITHIN THE TYPOLOGY OF TAX SYSTEMS

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## Abstract

In this paper we propose to achieve a theoretical classification of tax systems based on theories and literature in this field, highlighting the specific characteristics of each type of tax system. Based on the typology performed, the evaluation of the Romanian fiscal system and its positioning within the typology of tax systems will be studied, with the presentation of results relevant to the stages of economic development and the changes in the structure of the tax system that generated its typological transit. We appreciate the fact that the work developed on two classification levels, one fundamentally theoretical and one practical, will be a useful tax guide, with the presentation of the fundamental characteristics of the fiscal systems and the assessment of government options in selecting the type of tax system implemented.

**Keywords:** tax system typology, fiscal criteria, economic transition

**JEL Classification:** H, H5, E62, E63

## 1. Introduction

The fiscal policy, by the government revenue and expenditure strategies that influence the macroeconomic conditions, provide the regulatory authorities with macroeconomic adjustment mechanisms for achieving the aims of improving the unemployment rates, the inflation, of stabilizing the expansion of economic cycles and interest rates, in an ongoing effort to control and adjust a country's economic trajectory and / or to adapt to the international treaties and regulations which they complied to.

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In its action to influence the economic performance, the fiscal policy uses the tax system as the main instrument. It is a set of tax rules and norms that form, from a structural and functional point of view, a unit with its own personality and characteristics, flexible and adaptable to the goals and aims of the fiscal policy.

These features of flexibility and adaptability led in time to the shaping and conceptualization of a certain typology of tax systems, generated by a theoretical and practical necessity of achieving an organized and coordinated link, in a rational and feasible manner of implementation, between the government strategies and the real economy.

Thus, the theory of public finance provides classifications of tax systems according to several criteria. The national approaches that combine the theoretical approach with the empirical one, by which to achieve a positioning of the Romanian fiscal system following the criteria and typologies of tax systems, provide, at this time, space for maximized attention and development. In this context, we consider that the work can be, besides the issues mentioned in the summary, a wider approach on the subject that can capture the attention and concern of the scientific community. In terms of methodology, the logical analysis, the explanation of phenomena, the classification and theoretical elements interaction with the practical realities will be used in the development of the work.

## **2. Typologies of tax systems**

As noted, the tax system is the main instrument through which the fiscal policy operates based on the purpose and aims pursued, inducing structural changes on it.

The literature provides several classification criteria (Buchanan, James, and Musgrave, 1999; Dinga, coord., 2011), more or less relevant. We appreciate as relevant and sufficient to achieve the aim of the work, four criteria for the classification of the tax system, namely: the technical criterion; the economic criterion; the structural criterion and the criterion of the intensity of the fiscal pressure.

### **a) The technical criterion** refers to:

- the theme of the single tax, assumes a single tax base that would allow to increase the tax burden and to avoid tax evasion. The manifestation of such a tax system would amplify the effect on

the degree of economic inequality and prevent, from the social point of view, the tax customizing to each taxpayer's capability to pay tax;

- the theme of direct vs indirect tax predominance involves the authorities' option for one of the two types of taxation, namely prevailing taxation of income or prevailing taxation of consumption. The differences between the two types of taxation generally consists in the following:

- affordability, where the direct tax is on the person who receives the income, with immediate withholding on receiving, while in the case of the indirect tax the affordability is transferred to a third party, usually the final consumer;

- customizing of direct tax is apt at individualisation/personalization depending on the social status of the taxpayer, while indirect tax cannot be customized;

- changes in yields, both in terms of economic resilience and the statutory tax rate changes, the direct tax presents a relatively stable yield, while the indirect tax yield is fluctuating.

**b) The economic criterion** shows that the tax system, beyond the legal and technical aspects, are also dependent on the economic conditions under which they are implemented. It influences the distribution and redistribution through taxation, the development and fiscal efficiency. In economics four evolutionary stages have been outlined, in terms of economic development, which account for a certain typology of tax systems. In general, in the underdevelopment stage and in the developing (cruise) one, revenues are reduced, in which situation indirect taxation is prevailing and the tax burden is relatively low, the opposite situation being recorded in the developed and highly developed countries.

**c) The structural criterion** corresponds to the possibilities of amending the tax system through the characteristics of the statutory rate. Under this criterion four distinct types of tax system can exist, namely:

- the progressive tax system involves the application of the principle of tax rate differentiation directly proportional with the ability to pay, it has an anti-cyclical nature, being considered the only automatic fiscal stabilizer and performed by tax equity;

- the regressive tax system involves the application of the principle of differentiated tax rate inversely proportional to the ability to pay and is highly cyclical;

- the proportional tax system involves the principle of taxation with linear proportional share being characterized by the marginal tax constant value;
- the flat-rate tax system involves the establishment of fixed quanta payable by legal persons, irrespective of their balance sheet. An important feature of it is that it taxes a non-transparent base and reduces the black economy.

**d) The criterion of fiscal pressure intensity** classifies the tax systems into:

- hard tax systems, characteristic especially of economically developed countries, where the contribution of public capital in the economy is reduced, but also in former communist countries, characterized by low efficiency of the economy, administrative transition and the need for substantial public funds to achieve reforms. A tax system can be considered heavy if simultaneously the share of fiscal revenue in the total budget is more than 80-90% and the tax levies in GDP is over 25-30%;
- light tax systems, characteristic of underdeveloped countries or in transition, in which the share of fiscal absorption from the GDP is lower, about 10-15%, and the individual tax burden depends on the level of GDP and the distribution of income among the participants in its realization.

### **3. Romanian fiscal system assessment in relation to the types exposed**

The Romanian economy transition from a centralized system to a functioning market economy, the sequence of accession and European integration, the regional tax competition to attract foreign capital and permanent preoccupation of governments to ensure and increase tax revenues made the tax system a highly important anchor in achieving these goals. In order to ensure the convergence with these processes and objectives, which are sometimes overlapping, changes were made to the tax system, which were transposed, in fact, into frequent amendments to the Tax Code and the Tax Procedure.

In this economic and institutional framework, dynamic and emergent, the tax system went through several stages, which we will try to evaluate and make fit the criteria set to achieve a certain portrait of the Romanian fiscal system. We appreciate relevant to our

evaluation and results, two stages, namely: the period 1990-2004 and the period from 2005 to 2014.

***Characteristics of the tax system during 1990-2004***

The main characteristics of the tax system implemented by the government authorities during the period 1990-2004 were: the progressivity of taxation that ensures a mechanism for automatic stabilization of the tax system; redistributivity of the income through taxes and an important social component.

In terms of technical criterion, the progressive tax system applied in the period 1990-2004 was characterized by the predominance of the direct tax at the level of the statutory tax rate, which enabled its customization and adaptation according to the social status of the taxpayer. Over the period analyzed, the share of tax revenues generated by direct taxation, both in total tax revenues and in the GDP was permanently higher than the tax revenues generated by indirect taxation, estimating, in terms of the amount of revenues generated, that the indirect taxation was predominant, while, in terms of statutory tax rate, the direct taxation was dominant (progressive rates between 18 and 40%) compared to indirect taxation that ranged from 18% between 1993-1998, to 22%, in 1998 and 1999 and 19% between 2000-2004.

In terms of economic criterion, which implies the adjustment of the tax system at the stage of economic development, the progressive tax system applied in the period 1990-2004 was suitable for the development of the Romanian economy status (cruise status), ensuring the fiscal equity, the balanced distribution and redistribution through taxation and a progressive, non-accelerated, economic development.

From the point of view of structural criterion, corresponding to the possibilities of amending the tax system by the characteristics of the statutory rate, the tax system in the period 1990-2004 corresponds to the progressive tax system, which gives it a strong anti-cyclical character, being considered the only automatic fiscal stabilizer. In terms of structural effects on the income, this tax system reinforces the incomes of the categories of taxpayers with low and middle income and lays stress on high income taxation, with some social shades.

In terms of the criterion of fiscal pressure intensity, the tax system in the period 1990-2004 has the characteristics of a hard tax

system, specific to the level of development of the country at that time and the transition from a centralized economy to a market economy, when substantial public funds are required for reforms. At the start of the period, the early 90's, the tax share to the GDP was over 40%, decreasing gradually towards the end to about 30%.

***Characteristics of the fiscal system in the period 2005-2014***

The main characteristics of the tax system implemented by the government authorities during the period 2005-2014 were: to encourage large businesses ; to stimulate consumption; to stimulate foreign investment; to reduce tax evasion by tax relaxation and a sustainable overall economic growth.

In terms of the technical criterion, the tax system with a flat tax on the incomes of individuals and businesses applied during 2005-2014 was characterized by the predominance of indirect taxes, both as statutory tax rate level and tax revenues generated both in total tax revenues and GDP.

In terms of the economic criterion, which implies the adjustment of the tax system at the stage of economic development, it was considered that the progressive tax system has achieved certain goals, bringing the economy to a state that requires a large fiscal stimulus, ie a flat tax revenue. The effects of the tax reform manifested rapidly in the economy, particularly by increasing foreign investment in the economy, a high economic growth, especially in the period 2005 - 2008, an expansion of the business conducted by financially strong companies, but at budget level, the growth of tax revenue ratio to the GDP has not occurred.

From the point of view of the structural criterion, corresponding to the possibilities of amending the tax system by the characteristics of the statutory rate, the tax system in the period 2005-2014 corresponds to the proportional tax system, which confers it a pro-cyclical character. In terms of structural effects on revenue, this high income tax system reinforces and lays stress on small income taxation, with liberal shades.

In terms of the criterion of the fiscal pressure intensity, the tax system in the period 2005-2014 has the characteristics of a hard tax system with fiscal pressure relaxation trends, from around 30% in 2005 to around 28% in 2014.

**4. A "portrait" of the Romanian general tax system resulting from its assessment against the criteria set**

From the analysis of relevant characteristics of the two successive stages of the Romanian fiscal system, it can be drawn some conclusions, that are presented below, in the tabular form.

<b>No. crt.</b>	<b>Classification criteria</b>	<b>1990-2004 Stage Progressive tax system</b>	<b>2005-2014 Stage Proportional tax system</b>	<b>General characteristics</b>
1.	Technical	<i>The predominance of direct taxation from the legal share of taxation point of view and the predominance of indirect taxation in terms of generated tax revenues.</i>	<i>The predominance of indirect tax, both as tax statutory rate level and generated tax revenues.</i>	<i>Alternation of applied tax systems typologies, progressive vs proportional, ensured the specific tax equity, provided an economy's structure converging with its development needs and of compliance with some international agreements it adhered to.</i>
2.	Economic	<i>Good adaptability to the Romanian economy development stage</i>	<i>It constituted a suitable tax incentive for the real economy.</i>	<i>The high tax pressure has mitigated, inversely proportional to the Romanian economy development stages, being, in fact, the economic development impulse.</i>
3.	Structural	<i>Tax rates progressivity constituted an automatic fiscal stabilizer that has shaped economic expansion cycle and ensured equity in taxation.</i>	<i>Proportionality of tax rate changes the tax system character orientation towards pro-cyclicality and ensures equity to taxation.</i>	<i>Alternation of applied tax systems typologies, progressive vs proportional, ensured the specific tax equity, provided an economy's structure converging with its development needs and of compliance with some international agreements it adhered to.</i>

No. crt.	Classification criteria	1990-2004 Stage Progressive tax system	2005-2014 Stage Proportional tax system	General characteristics
4.	Tax burden intensity	<i>High tax pressure (40%), with a relaxation trend (30%).</i>	<i>Relatively high tax pressure (30%), with a tendency to relax (28%).</i>	<i>The high tax pressure has mitigated, inversely proportional to the Romanian economy development stages, being, in fact, the economic development impulse.</i>

Source: based on the assessment conducted by the author.

It notes that the fiscal policy was oriented towards supporting economic development, adapting sequentially by changing tax system, its stages of development by maintaining a certain tax sovereignty, but at the same time, has adapted and needs tax harmonization, in particular on indirect tax side.

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