THE IMPLICATIONS OF THE ACCESSION TO THE EUROPEAN UNION UPON TAXATION IN ROMANIA

Marcel DRĂCEA, Prof.., PhD.
University of Craiova

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Abstract: European tax policy is very important for the member states, and the actions of each country may have an impact not only inside the country, but also within the adjacent countries. Therefore, together with the opening of negotiations to access to the European Union, the Romanian taxation system was submitted to some ample amendments, having as a purpose the accomplishment of the harmonization process of Romanian tax laws in force with the community one in the field. The paper aims to evaluate the implications of the access to the European Union upon the taxation system in Romania, the main target being to analyse the contribution of the taxation system to the building of budgetary revenues and pursuing the influences of the tax measures upon the evolution of public revenues during 2005-2007.

1. Introduction

The target of accomplishing the joint market and the monetary union brought on a series of amendments regarding the taxation for the member states of the European Union. Eliminating the restrictions concerning the stock mobility generated the fear that the taxable basis at national level may be reduced by means of its migration between the member states, due to the tax competition between them, which shall affect the taking degree and the capacity of ensuring the social safety (Nicodeme, G., 2001).

Regarding our country, along with the opening of negotiations to access to the European Union, the Romanian taxation system was submitted to some ample amendments, having as a purpose the accomplishment of the harmonization process of Romanian tax laws in force with the community one in the field. Thereby, the strategy of tax policy during the pre-accession period, in accordance with the provisions of the Governance Programme for 2004-2007, was drawn up so that to ensure, on one hand, *the acceleration of tax reform* and the re-launching of the economic activity, and on the other hand, *the accomplishment of the harmonization process of Romanian tax laws in force with the community one.*

In 2004, the Romanian taxation system was considered by the International Monetary Fund[1] as being a sustainable one, which didn't create macroeconomic disequilibriums on medium and long term. The Government agreed along with the IMF, since July 2004, to a programme of tax reform which would be effective starting with the 1st of January 2005. The main pillars of this programme provisioned an adjustment of the tax profit from 25% to 19%; an adjustment of the tax profit for the smallest portion of taxation from 19% to 14%, partially balanced by freezing the personal deductions at the level from 2004 and an adjustment of the rate of social insurances contributions with 1,25%. In order to balance a part of the revenue loss, the authorities wished to introduce simultaneously a land tax, to increase the dividend and exercise tax, starting with the 1st of July 2005.

Although the polls made among the businessmen in the last 5 years show that the taxation level is one of the secondary concerns for the management of the companies (less important than, for instance, the tax predictability), the tax reform from 2005 aimed to encourage the big business, the companies with an increased financial power, staking on the effects of induction of the massive investments achieved by these investors.

The taxation system which became effective in 2005 and adjusted in 2007, assignated as an objective to ensure some bigger available revenues, the potential expansion of business, to increase the direct investments, to adjust the share of underground economy, a sustainable economic increase, more places of employment, to increase the savings and investments.

Of these targets, there have been reached the increase of foreign investments (a record during the period subsequent to the Romanian Revolution of December, 9,1 billion euro in 2006), a high economic increase (7,7% in 2006, even if in a large measure based on consumption) and the business expansion developed by important companies, powerful from the financial point of view. What the reform of taxation system promoted by the Government after 2005 didn't succeed to acquire were the increase of budgetary revenue share in the GDP, the increase of savings and what made the things worse was the accentuation of the current account deficit. The higher available revenues meant a higher consumption (especially for the imported goods) and implicitly, the falling of the commercial balance deficit.

The Romania's characteristic comparing to the 27^{th} countries of the European Union consists in the structure of the revenues collected from the state budget. In Romania, the tax and budgetary revenues depend on the revenues from the indirect taxes and tax rates (VAT, exercises, customs duties, and so on), while, in the European Union, the contributions of the three big categories of taxe rates and taxes (direct tax rates, indirect tax rates and social contributions) for the development of the revenues are relatively proximate.

Therefore, through the paper we aim both a concisely evaluation of the present Romanian taxation system, comparing to the existent ones in the European Union, and an analysis of the budgetary revenues sampled at the level of the state central administration.

2. The influences of the tax measures upon the budgetary encashments

Romania's accession to the European Union brought significant amendments of the regulations regarding the profit tax, revenue tax, VAT, amendments due both to the abolition of the pikes between the member states, and the necessity of harmonizing the national legislation with the one of the member states.

Therefore, the law regarding the amendment of the Tax Code comprises legislative measures necessary for reaching the objective from the Governance Programme, for generalizing the unique rate of 16%, expanding the taxation basis, taking over the directives in the field from the legislation of the European Union and refining and simplifying the legislative framework in force.

As a general remark, the taxation in Romania is a medium one comparing to the countries in the European Union, situating at a relative proximate level comparing to Ireland or Slovakia (where it is applied a unique rate of 19% both for revenues and VAT) and much more reduced both comparing to the one in the UE15 countries, for instance, Sweden, France and Denmark and comparing to some of the new-comers countries in the EU in, as well as the Czech Republic or Hungary.

In addition, if we also take into account the unique rate relatively reduced of the revenue taxes (table 1) and profit taxes (figure 1), Romania appears as a „tax paradise" (at least from this point of view) comparing to the member states of the European Union, and this, as a member state, trespasses the objectives of tax policy at the European level and especially the one aiming the tax competition.

Table 1

The level of taxation rates on personal revenues in the member states of the European Union (January 2007)

Country	Taxation rate	Country	Taxation rate
Austria	21-50%	U.K.	0-40%
Belgium	25-50%	Cyprus	20-30%
Denmark	38-59%	Czech Republic	12-32%
Finland	9-32%	Malta	15-35%
France	10-48%	Estonia	22%
Germany	15-42%	Hungary	18-36%
Greece	0-40%	Latvia	25%
Ireland	20-41%	Lithuania	15-27%
Italy	23-43%	Poland	19-40%
Luxembourg	6-38,95%	Slovakia	19%
Netherlands	0-52%	Slovenia	16-50%
Portugal	10,5-40%	Romania	16%
Spain	15-45%	Bulgaria	10-24%
Sweden	----		

Source: http://www.worldwide-tax.com/

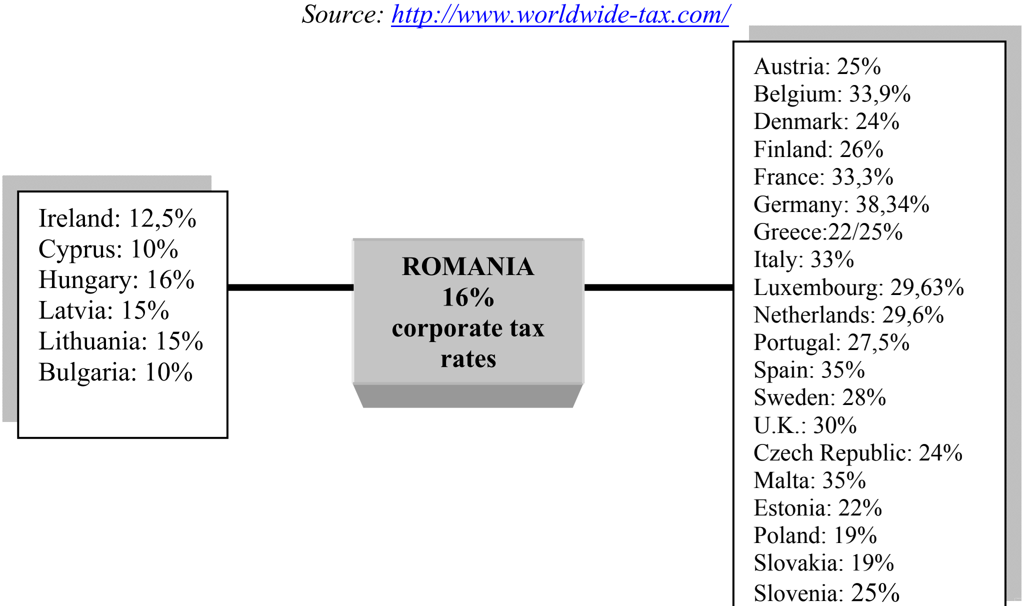

Fig. 1: The corporate tax rates in Romania comparing to the other Member States of the European Union (2007)

Source: www.worldwide-tax.com

There are four types of measures which we consider to be appropriate, on short and medium term, in order to diminish the impact of introducing the unique rate at the profit and revenue tax and sustaining the budgetary projections on medium term:

- pursuing and accelerating the reform process of tax administration;
- increasing some of the direct and indirect tax rates;
- extending the taxation basis;
- ceasing the granting of some relagging or exemptions from the payment of the tax rates and taxes.

At the same time, reducing the social contributions may lead, in our opinion, to an improvement of collecting the funds at the state budget and an increase of the probability of arising a positive Laffer effect by diminuting the tax evasion. The influence on medium term of the increment measures of the tax rates cumulated to the postponement of the reduction process of the contribution to the social insurances is synthetized in table 2.

Table 2

The influences of the tax measures upon the evolution of public revenues (billion lei)

	2005	**2006**	**2007**
Incrementing the tax on interests revenues	+1.380	+2.196	+2.295
Incrementing the tax on stock revenues from 1 to 10 %	+1.350	+1.908	+1.989
Increasing the tax on the revenues of the non-residents from 5 % to 10%	+121	+192	+201
Incrementing the profit tax rate from 10% to 16% for the sale of real estates	+423	+982	+1.174
Advancing the increment of the exercises from 01.07.2005 to 01.04.2005	+503	-	-
Savings from postponing the HIH (health insurance house) reduction	+8.331	-	-
Increasing the tax for the medium enterprises to 3 %	+5.609	-	-
Total influences comparing to the conditions of the year 2005	**+17.717**	**+5.278**	**+5.659**

Source: http://www.mfinante.ro/

Concerning the share of the consolidated budget revenues in the gross domestic product, this increased during 2005-2007 from 32,9 % (in the year 2005) to 35,3 %, especially due to the transfers which Romania received from the European Union, but also as a consequence of improving the acquisition and enlarging the tax basis. In terms of the budgetary encashments, *introducing the unique rate generated at the level of the year 2005 a diminution of the budgetary encashments,* which lead, implicitly, to an increment of other categories of taxes (duplicating the tax on dividends for the natural persons, duplicating the tax on the revenues of the medium enterprises, and so on) and to an increase of the pressure upon the consumption.

Table 3

The evolution of the budgetary revenues as a report in the gross domestic product (%)

	2003	**2004**	**2005**	**2006**	**2007**
TOTAL REVENUES *)	**33,6**	**33,6**	**32,9**	**33,4**	**35,2**
Tax revenues	28,7	28,6	27,2	28,5	28,8
Direct tax rates	**16,2**	**16,5**	**15,1**	**16,1**	**16,1**
Profit tax	2,4	2,9	2,3	2,2	2,1
Wages and revenue	2,9	3,1	2,2	2,6	2,7
Contributions to social insurances	10,0	9,6	9,7	10,5	10,5
Other direct taxes	0,9	0,9	0,9	0,8	0,8
Indirect tax rates	**12,5**	**12,1**	**12,1**	**12,3**	**12,7**
VAT|	7,5	7,0	7,1	7,3	7,3
Custom duties	0,7	0,7	0,6	0,6	0,5
Exercises	3,2	3,4	3,4	3,5	3,9
Other indirect tax rates	1,1	1,0	1,0	1,0	1,0
Non-taxable revenues	4,4	4,3	4,1	3,7	3,3
Grants	0,5	0,7	1,6	1,2	3,1

**) Comprise the external funds received from the European Union The data are calculated according to the methodology ESA 95.*

Source: http://www.mfinante.ro/

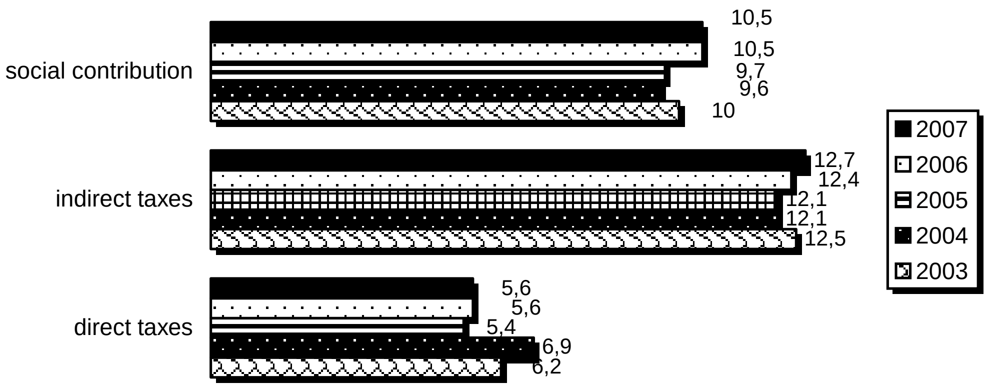

Fig. 2: The evolution of the budgetary revenues as a report in the gross domestic product (%)

As it may be noticed from the presented data, the reduction of the encashments from the revenue and profit tax was compensated by an increase of the encashments recorded at the level of consumption tax rates (VAT and exercises).

At the same time, the contributions to the social insurances continue to held the highest share within the direct tax rates, this trend being consequently increasing from 9,7 % of the GDP in the year 2005 to 10,5 % of the GDP in the year 2007 (according to the MFP estimations). The subtraction measures of their level correlated with the enlargement of the tax basis and improving the acquisition shall diminish the costs with the work force of the economic agents and shall allow a support of the forecasted social budgetary expenses.

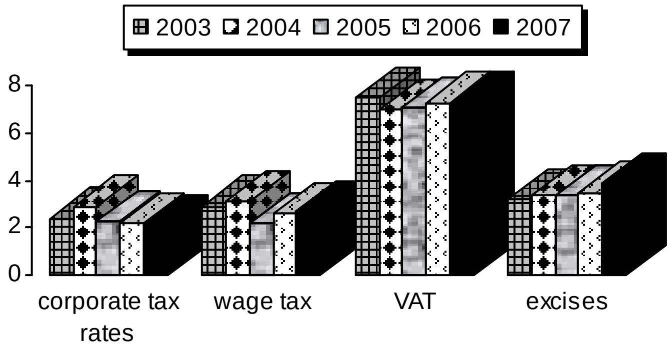

Fig. 3: The structure of the tax revenues in Romania during 2003-2007 (% of the GDP)

For a more suggestive comparative analysis, in diagram 4 it is shown the evolution of the encashments from the revenue tax, as a share of the GDP, on a larger period of time (1990-2007).

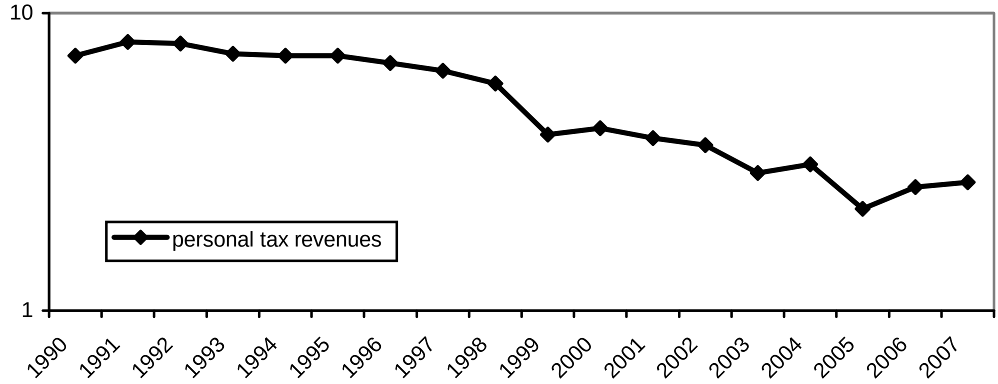

Fig. 4: The share evolution of the personal tax revenues in the GDP during 1990-2007

Source: processings based on the data sampled from the Statistical Yearbook of Romania/2005 for the period 1999-2004 and from the Monthly Statistical Bulletin no. 1/2008 for the period 2005-2007

As it may be noticed from the presented data, for the year 2005, the measure of introducing the unique rate of 16% determined the encashment of a revenue tax of 2.2% from the gross domestic product, respectively 8.3% from the consolidated general budget revenues, being, in fact, the lowest shares recorded during 1990-2007.

Regarding the evolution of the encashments from the profit tax, this is closely connected to the amendment of the regulations in the field and the evolution, in the bulk, of economy. In a first stage, the diminution of the capacity of this tax is due to the multiple facilities granted by means of tax legislation, facilities which, although, they had as a purpose to encourage the private sector, contributed in a great measure to the expansion of tax evasion phenomena. Subsequently, the evolution of the encashments from the profit tax may be attributed to the economic decline recorded at the end of the 90's and to reduction, starting with the year 2000 of the tax rate from 3%, to 25% and subsequently to 16%.

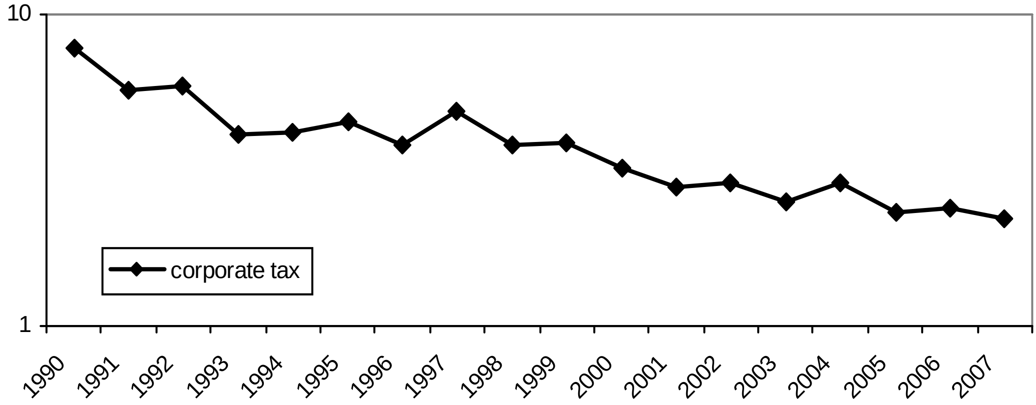

Fig. 5: The evolution of the share of the corporate tax in the GDP during 1990-2007

Source: processings based on the data sampled from the Statistical Yearbook of Romania/2005 for the period 1999-2004 and from the Monthly Statistical Bulletin no. 1/2008 for the period 2005-2007

Incontestably, the renunciation to the progressive taxation (which corresponds to the principle of tax equity) and the introduction of the unique tax rate in Romania raised a series of for and against reactions. However, regarding the taxation of the work place in **Romania**, the problem was and is *not the wage (revenue) tax, but the high rates* of social contributions.

The reduction of the real taxation on the work revenues represent, indubitably, a salutary relief from taxation, but we shouldn't expect that this would grub up revenues from the illegal employment area and neither to produce a displacement of the pay list wages from areas with small wages towards areas with superior wages.

As, regarding such grubbing up or displacements, the employers would have to pay in fact more in the account of social contributions. And taking into account that these obligations represent, depending on the wage level, between 60% and 80% of the total of the work place taxation, *the additional payments would exceed the relative revenues achieved by the reduction implied by a unique rate of the revenue tax.*

Concerning the illegal revenues in individual services, the problem is that, while the beneficiary of the respective services shall not be commonly interested, by significant deducibility, to declare them as expenses, the ones who perform the services can not be forced to declare them as revenues, in order to be taxable. The only manner to grub up these revenues to be taxable is to introduce tax deducibilities for those who make the expenses. Unfortunately, diagrams of deducibilities in this field are not taken into account. And, in their absence, there shall not exist any grubbing up of the non-taxated revenues. As, in this field, neither the diminution of social contributions nor the reduction of the tax rates of the revenues and nor the administrative and economic constraints implied by the accession to the European Union do not play any role.

3. Conclusions

In Romania, the taxation was interpreted by an entire series of taxpayers as an agression, becoming a tension factor in the economic reports. They didn't feel, either it was about the companies, or the individual taxpayers, a partnership relation. First of all, the state didn't transform a great part of the tax rates in public services, but it developed a bureaucracy which came to exceed the one from the communist time. The public administration is not by itself a public service. It is a service provider only in the measure in which proves to be efficient. This efficiency of the administration contains also non-quantificable, intangible elements. For instance, the credibility of state institutions, the confidence level which the citizens have for these are goods which facilitate the company's running. The public administration is, currently, in a certain measure an institution „in itself", used to ensure for the public clerks various rent forms, and less an institution providing public services.

In order to be a partnership relation, a selective and stimulating one, the taxation must generate obligations and rights by both parts. Very often, the state, doesn't abide its ones. From the non-payment in due time of the amounts for the compensated medicines, and up to the delay in paying the contracting obligations through the state budget or the companies which belong to it, the state is the worse payer of the Romanian economy. Under these circumstances, it's not a wonder for anyone that the taxation is considered not as an integration form of the taxpayer within an opened contracting mechanism, but as a form of its agression and isolation. Forced by the proliferation of public administration and by its own lumpishness in managing the public money, the Government tends to increase the tax rates or to introduce some new tax rates.

In addition, as the tax rates showed, especially regarding the work force taxation, there are applied to some much more reduced levels comparing to other countries, which increases a lot the difficulties of the Romanian taxpayer.

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