

## **On the Logic of Separating the Fiscal Policy from the Fiscal Administration<sup>1</sup>**

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**Abstract:** One of the problems yet to be solved in a satisfactorily manner in Romania is the decentralisation of the public administration. In general, by decentralisation we understand the separation of the central decision from the local (or regional) decision based on the principle of subsidiarity. In our opinion, The National Agency for Fiscal Administration should function, in a decentralised manner, meaning outside of the Ministry of Public Finances. In support of this statement we will present two modules or arguments: a) we will first debate on the matter of public administration decentralisation; b) second, we will debate in favour of the institutional separation of ANAF from the Ministry of Public Finances. **Objectives:** Implementation of concrete desire for decentralization of public administration; Identification of conceptual distinctions, structural and functional development of tax policy and administration of fiscal policy. **Prior work:** Assessment of net tax burden; Phillips curve assessment for Romania; Automatic fiscal stabilizers; Sustainability of fiscal policy. **Approach:** Logical analysis of the concepts involved in the study; Highlighting the distinctions of semantic and pragmatic nature of the concepts involved in the study. **Results:** decisive arguments concerning the desirability of the structural separation of the fiscal policy from the fiscal administration. **Implications:** providing arguments for a separation of fiscal policy decision to tax administration; a collection efficiency of budgetary obligations. **Potential beneficiaries :** The Ministry of Finance; the National Agency for Fiscal Administration; the Government of Romania; the Ministry of Internal Affairs and Administration. **Value:** Contributions from conceptual nature: semantic separation of fiscal policy from tax administration; from methodological nature: demonstrating scientific research force of an application logic analysis method; from empirical nature: demonstrating the need, possibility, effectiveness and appropriateness of the structural separation of fiscal policy from tax administration. Originality from the research methodology: the use of logical method.

**Keywords:** decentralization; fiscal management; efficiency; effectiveness; monitoring

In our opinion, The National Agency for Fiscal Administration should function, in a decentralised manner, meaning outside of the Ministry of Public Finances. In support of this statement we will present two modules or arguments: a) we will first debate on the matter of public administration decentralisation; b) second, we will debate in favour of the institutional separation of ANAF from the Ministry of Public Finances.

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**Concerning the First Argument**

One of the problems yet to be solved in a satisfactory manner in Romania is the decentralisation of the public administration.<sup>1</sup> In general, by decentralisation we understand the separation of the central decision from the local (or regional) decision based on the principle of subsidiarity. As known, the principle of subsidiarity demands that the decision is made at the aggregation level of the particular system where its efficiency of the decision is maximum.

Based on these elements we will propose several subjects of interest, as follows.

We must remember that the public administration has three large functions: a) to design the public policies; b) to implement these public policies; c) to monitor (control) the efficacy and efficiency of these public policies. It is obvious that the first function pertains to designing, the second to administration and the third to feed-back (which, as we will subsequently see, has both designing and administrative characteristics).

**Concerning the First Function**

The design of the public policies requires a specific philosophy (of that particular area), hence this function should be concentrated at the central level by gathering the experts in that matter. It results therefore, that the part of actual policy (elaboration of the dedicated public policies) must remain at the central level. It is easily noticeable that this conclusion verifies the principle of subsidiarity because, being a public policy, single for the entire national territory, it must answer several general commandments which can only be decided and introduced into the norm at the central level, ensuring thus the maximal efficiency of that activity. The logic conclusion that may be inferred from here is that the central public institutions and authorities must be "populated" with social experts, analysts, designers, in a word with specialists in social engineering, who must be able to identify the best (adequate, effective and efficient) ways and modalities to shape behaviours by encoding (norming).

**Concerning the Second Function**

The actual implementation of the public policies is a matter of administration. The administration of the public policies must therefore be accomplished at the local (and/or regional) level. Therefore, it is completely inadmissible logically (and institutionally) to have effective structures for public policies administration within the central public institutions and authorities (a strong reluctance exists here to reduce the staff of these central public institutions and authorities). Therefore, one of the most efficient directions of decentralization (we are not discussing here the necessity to ensure the decentralization of the financing sources for these functions; this is a vast problem which requires separate discussion) is the separation of the function of public policy design from the function of policy administration. Another logic argument (beside that of efficacy, imposed by the principle of subsidiarity is the necessity to eliminate the possibility of a conflict of interests and, more obviously, the possibility of a moral hazard. The conflict of interests and the moral hazard may result from the fact that the same structure (or the same people) design and implement the public policy. Many of the irregularities, inconsistencies and even disfunctionalities of the project of public policy can be minimized or simply ignored by those who have designed the project of policy, due to obvious reasons. Therefore, by decentralising the function of administration a sui-generis control of the designers of public policies by the administrators of public policies is achieved.

**Concerning the Third Function**

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<sup>1</sup> Semantically, the expression "administrative decentralisation", is arguable due to several reasons: a) one may understand that this is an administrative way of decentralisation, which reduces the importance of this approach; b) it doesn't clearly result that it refers to the public administration. Within this context, with the risk of seeming pedant, we prefer the expression „decentralisation of the public administration”.

What can we say about the third function, of monitoring or control (feed-back function) in connection to the public policies? We consider that the following elements are important within this context:

1. The control of the public policy effectiveness and efficacy<sup>1</sup> must be in the hands of the one who elaborated that particular public policy. But this point of view is, obviously, inconsistent with the above statements, according to which the administration of the public policies must be decentralised. The solution is, in our opinion, as follows: at the central level (central public institutions and authorities) will remain the part of methodology and coordination (by coordination we understand, among other, the receipt of reports on the result of controls, data centralisation and syntheses serving to improve the specific public policy). As it can be seen, this component of the control activity also pertains to institutional designing, engineering, therefore it is logic to manage it at the central level; on the other hand, the administrative component of monitoring and control of the public policy must be decentralised (which is consistent with the logic exposed above).
2. Therefore, it is inadmissible to exist and function effective structures of monitoring and control at the central level (within the structures of the public institutions and authorities). These structures must be reduced to the institutional capacity to accomplish the methodological guidance and the coordination of this activity, but actual activities of monitoring and control should not be performed. This conclusion is logic because, as mentioned before, at the central level must only be maintained capacities of public policy design, not of public policy administration.

Therefore, logically, at the central level we will actually have two distinct, but not reciprocally autonomous, functions: the function of public policy design and the function of methodological and technological design of monitoring and controlling public policy implementation, while at the local (and/or regional) level we will also have two distinct, but not reciprocally autonomous, functions: the function of public policy administration and the function of monitoring and control of public policy implementation.

A logic problem appears, though. Because the monitoring and control of the public policy implementation is done by the decentralised structure, there is a potential risk that certain disfunctionalities within the process of public policy administration (administration which is done, as seen, by the decentralised structure) are deliberately ignored by the decentralised structure for monitoring and control, in its reports towards the decentralised structure. An institutional innovation must be identified here, which to eliminate this risk. In our opinion, the solution is this: the monitoring and control department of the decentralised structure of the public administration will have a double subordination: an administrative subordination towards the decentralised structure (the monitoring and control plan, etc.) and a reporting<sup>2</sup>-type subordination towards the central structure. This means that the monitoring and control department from the decentralised level will send its reports simultaneously to the management of the decentralised structure and to the management of the centralized structure. In this way the monitoring and control department from the decentralised level will not be able to withhold or distort some results of its activity that might question the effectiveness and efficacy of the activity of administrating the public policy at the local level. This institutional innovation should be completed, in our opinion, by another one with redundant function.<sup>3</sup> The

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<sup>1</sup> We also refer to the efficiency of the public policy. The efficiency of the public policy (the desirable optimum between efficacy and cost) is too complicated to be addresses in this discussion. We will only say that a public policy can be efficient even if the government loses, in monetary terms, by implementing that policy. In other words, when we speak of the "yield" of a public policy, the meaning of this term is not the usual one.

<sup>2</sup> As it is known, in the literature, the administrative subordination is referred as accountability and the obligation to report is referred as responsibility.

<sup>3</sup> The institutional redundancy is another essential problem in the functioning of the public administration, particularly within the context in which, as mentioned earlier, the yield of the public policy must not be evaluated in the classical meaning. Within this context, redundancy is an extremely important condition for the effectiveness and efficacy of the fiscal policy (as

structure of internal public audit (which, according to the law, is organised and functions at any level of aggregation of a public institution or authority) from the central structure will effectively monitor and control the decentralised structures. This exception from the rule of maintaining a structure with effective functions of public policy administration at the central level will ensure the sincerity, completeness and promptitude of the reports from the decentralised structures of monitoring and control. Furthermore, this structure of internal public audit will draw the performance report for the public budget projects of the particular public institution or authority (which again means an effective control).

### Concerning the Second Argument

The policy of macroeconomic adjustment targeting the real economy – the fiscal-budgetary policy – is the exclusive field of the government<sup>1</sup>. The government designs, implements and administers the fiscal policy through a specialised institutional structure: the Ministry of Public Finances. The fiscal policy can not be separated, either structurally, or functionally, from the budgetary policy<sup>2</sup>. Limiting ourselves to the fiscal policy, defined as that policy of macroeconomic adjustment which ensures the designing of the fiscal norm, its implementation and cashing the public revenue<sup>3</sup>, we will therefore say that it has two components, causally interconnected, yet distinct: the component of fiscal mechanisms design (fiscal norm and the institutions implementing the fiscal norm) and the component administrating these mechanisms.

The two components (we will refer to them as: „component **A**”, for the actual fiscal policy and „component **B**”, for the policy of fiscal administration, although intercorrelated they still have noticeable differences in terms of several analysis criteria:

1. in terms of *function*: a) component **A** has a institutive, normative function: it creates and introduces norms, regulations, constraints and stimulants within the functioning of the economic system according to the governance goals; b) component **B** has an administrative function: it applies the norms proposed by component **A**;
2. in terms of *finality*: a) the finality of component **A** is the ensure the institutional coherence, including the establishment of the regulatory conditions required to structure the economic behaviour (the fiscal behaviour in this case); b) the finality of component **B** is the ensure the institutional efficacy (and efficiency, as much as possible) of the application of the normative structure imposed by component **A**;
3. in terms of *modality*: a) component **A** acts theoretically: the design of the afferent norms and institutions is fundamented by the fiscal theory (philosophy) of the acting government; b) component **B** acts practically (more generally, pragmatically): it provides the institutional control of conforming

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it resulted, I hope, from the above statements, the only “ingredients” allowed for the evaluation of a fiscal policy are the effectiveness and efficacy, not efficiency).

<sup>1</sup> We do not ignore, of course, the necessity and decisive importance of a permanent harmonization of the fiscal policy with the other policy of macroeconomic adjustment – the monetary policy – the latter being the responsibility of the central bank. For the necessities of this analysis we omit the references to this harmonization, particularly since this harmonization depends on the type of dependency of the adjustment policies – we seem to go now towards a medium-term fiscal dominance.

<sup>2</sup> There are analysts who consider that conceptually, the fiscal policy also includes the budgetary policy. Other analysts, however, consider that the fiscal policy is only concerned with the “public revenue”, while the budgetary policy is concerned by the “public expenditure”.

<sup>3</sup> We will limit ourselves to include in the public revenue only the fiscal revenue and the parafiscal revenue (social contributions). Other compulsory levies to the public budgets or other cashing at these budgets are not taken into consideration to formulate these conclusions.

with the norms proposed by component **A** and applies, if and where it is the case, the sanctions (or awards<sup>1</sup>) for the fiscal behaviour related to the conformation with the mentioned norms;

4. in terms of the *temporal perspective*: a) component **A** targets the medium and long-term, structuring norms and institutions with lagging impact but with a high potential of drawing in; b) component **B** targets the short-term (often very short), structuring actions with no lag, but with a low potential of drawing in.

From the perspective of the above considerations, we may ask whether there is or there isn't an added value in the idea that the fiscal policy should function separately from the fiscal administration, not just functionally (as it somehow happens today by the distinct establishment of the National Agency of Fiscal Administration subordinated to the Ministry of Public Finances) but also structurally, meaning by the institutional separation of the fiscal administration from the fiscal policy.

We will subsequently argue that such an added value may be shown.

The **necessity** to separate the fiscal administration (component **B** of the current institution of the Ministry of Public Finances) from the fiscal policy (component **A** of the same ministry) may be argued as follows:

1. the specialisation of the officials from the two components is absolutely different (see the third criterion of differentiation of components **A** and **B**); this may lead to heterogeneities (even difficulties) of communication between the two categories of specialists who focus on different finalities of their activity and function (see criteria two and four of components **A** and **B**);
2. the different specialisation also produces heterogeneities (even difficulties) in the manner of unitary management of the professional improvement of the two categories of experts (professional career, long-life training, etc.);
3. the final goal and function assumption differentiation produces acute inconsistencies between the two components, in terms of actual strategies and measures of action;
4. there may be (or appear) different evaluation criteria of the impact of fiscal policy measures and fiscal administration measures between the two components, situation which is difficult (even impossible) to manage by a single manager (the Minister of public finances, in our case); for instance, a measure of forced execution may be evaluated as beneficial by component **B** (whose purpose is to ensure the programmed revenue to the budget, short-term objective), and as a measure with negative impact by component **A** (which has medium and long-term objectives, for instance, it may consider that the taxation basis has been reduced);
5. there may be conflicts of interests between the representatives of the two components (**A** and **B**) concerning the solution to situations in which the lack of efficacy of the activity of either component is due to the lack of efficacy of the activity of the other component;
6. we may presume, theoretically, that the Minister of the public finance will "favour" one of the components when evaluating the efficacy or viability of the two components, one of them according to his professional speciality and one according to the team that "brought him to power".

The **possibility** of the institutional/structural separation of the fiscal policies from the fiscal administration resides in the following considerations:

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<sup>1</sup> The positive side of the fiscal administration (for instance of the fiscal control) is, unfortunately, frequently omitted, the side which distributes awards for the voluntary conformation with the fiscal norm (or for efficiency in conforming with the same norm) stressing unilaterally and exaggeratedly on the negative side, penalising, of this administration.

1. the structure of the government must be, anyhow, reviewed to reconfigure the fields that fall under the incidence of the central governance because the state sector (that part of the public property that produces private goods and services and which must, therefore, be privatized, the so-called private domain of the state) shrank considerably, on the one hand, and because of the necessity to align the structure of the governmental institutions to the practice of the EU member states, on the other hand; this reconfiguration creates the opportunity (in the praxiological meaning of the term) to operate the structural separation of the fiscal administration from the fiscal policy.
2. there is, anyhow, a quasi separate experience of functioning of the structures of fiscal administration from the local level (county directorates of public finances and the financial administrations from municipalities and towns); they never played a role in the elaboration of the fiscal policy, they just enforced it. Within this context, it would only be necessary to align the structure of the central level to that of the local level;
3. the simplification of the fiscal levying (operated in Romania starting with 2005) needs no more a close collaboration (methodologically) between components **A** and **B**; component **B** becomes thus, by reason of things, much more autonomous and specialised than until now, which eases its separation from component **A** and reduces the potential transaction costs of this separation.

One of the most serious problems confronting the public sector in Romania is the fiscal administration, more precisely, two aspects of it: the efficacy of the fiscal control and the level of collecting the programmed revenue to the budget. The deficient way of solving these problems leads to structural tensions within the public budgets (and, implicitly, at the level of the consolidated general budget), introducing vulnerabilities within the general equation of the economic deficits (the deficit of the consolidated general budget, the current account deficit, the private sector deficit). Many of the vulnerabilities which the International Monetary Fund lists during the discussions with the Romanian representatives in this field are identified exactly at the level of the fiscal administration. Within this context, the structural autonomization<sup>1</sup> of this component will allow several beneficial developments:

1. accountability of the structure of fiscal administration, by taking it out from the incidence of the Ministry of Public Finances and, therefore, by transferring the specific objective directly towards the governance of this structure;
2. efficientization of the structure of fiscal administration, by focusing its activity on the specific temporal function, finality and perspective;
3. ensure the predictability of the fiscal administration in relation to the exigencies which appeared once Romania accessed the EU in terms of fulfilling the duties of Romania towards the community budget, on the one hand, and ensuring the security and efficiency of using the European structural and cohesion funds, on the other hand;
4. transmitting a signal of credibility and accountability towards the European Commission in terms of the reform of the public administration.

The presumed **impact** of this separation may be inferred from the following points of view:

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<sup>1</sup> The functional autonomization (which is, at least theoretically, currently accomplished) is not enough, because in this case, the accountability is not assumed completely. By the structural autonomization, this assumption of responsibility becomes full and effective. The closest example here is the structure of internal public audit which is functionally, but not structurally autonomized. Therefore, the efficacy of the internal public audit (particularly that of system and less that of conformity) is arguable.

1. from the *institutional* point of view: a higher level of homogeneity of the structure of fiscal administration (and, as effect, a higher level of homogeneity of the structure of fiscal policy, which will remain the only activity of the Ministry of the Public Finances); a higher homogeneity of an institutional structure already is a factor increasing the efficacy and “governance” of that structure;
2. from the *economic* point of view: the emergence of the possibility for personalized wages, within the budgetary sector; the experts of the two separated components may receive wages according to their function and role within the general institutional framework, this time existing solid arguments of differentiation (including in terms of source for the increased wages);
3. from the *technical* point of view: the higher capacity of action/intervention of the structure of fiscal administration which results from its independence from a certain minister and submission to the authority of the Prime Minister (or possibly, of the State Minister for economic problems);
4. from the *managerial* point of view: the direct accountability of the structure of fiscal administration for its actions and results will not only increase the efficacy and efficiency of its activity, but will also stimulate a process of deepen specification of the methods, techniques and ways of action and goals accomplishment;

The structural separation of component **B** (fiscal administration) from component **A** (fiscal policy) may have some inconveniencies, on the short term, which are perfectly manageable one they are identified:

1. the fiscal policy may appear exogenous to the experts of component **B** which is structurally separated, which may create a feeling of non-involvement in the design of a norm which they are asked to enforce;
2. if previous and permanent measures are not taken, which to maintain a continuous flow of information from the structure of fiscal administration towards the structure of fiscal policy and vice versa, the important advantage of the feed-back may be actually lost (by the structure of fiscal administration), namely, the evaluation/valorisation (by the structure of fiscal administration). It is established that, praxiologically, the breach of a norm (as observed by the structure of fiscal administration) is, sometimes the peremptory sign of inadequacy of that specific norm; this inadequacy should be reported as soon as possible to the structure which designed that specific norm, i.e. the structure of fiscal policy. Reciprocally, the impact studies performed (or which should be performed) by the structure of fiscal policy when it introduces a new fiscal norm (or changes an existing one) are of great use to the structure of fiscal administration which has to monitor the observance of the specific norm.

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