THE FISCAL COMPACT IN THE EU

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ABSTRACT
This paper represents an overview on the fiscal policy used in the European Union and how it develops towards a mecahnical evolution known as the Fiscal Compact or the Treaty on Stability, Coordination and Governance in the Monetary and Economic Union. The overall aspect shows that the global economy and especially EU's economy are evolving towards a positive output, but there are some issues regarding coordination and output pace and quality.

KEYWORDS
fiscal compact, fiscal policy, macroeconomic policy, efficiency

INTRODUCTION

Current macroeconomic schools were developed based on certain specific assumptions neoclassical (price flexibility) and Keynesian theory (price and wage rigidity). Expansionary fiscal policy will have a low efficiency in reviving the economy, as output reacts little to fiscal shocks. Also, fiscal policy generates effects in both the short and long term (according to Keynes) or only short-term, according to Keynesian nuance.

1. EFFECTIVENESS OF THE FISCAL POLICY (MACROECONOMIC APPROACH)

New classical economics (Lucas, Sargent) makes the following arguments on the impact of reduced fiscal shocks:

- change aggregate demand affects a very small extent of production and the income of the economy;
- expectations of economic agents are rational, they are not affected by "short-sightedness" Keynesian specific; operators optimize their consumption choices related to a forward-looking manner and have rational expectations;
- individuals do not suffer from money illusion and therefore only real changes (relative prices) influence consumer decision;
- prices and wages have a high degree of flexibility;
- as Ricardian equivalence, increased public spending, financed by borrowing or by taxes will not result in improvement of well-being because consumption and GDP remain unchanged. Reductions in public savings (due to increasing government spending) will be offset by higher private saving because consumers anticipate future tax increases. Consequently, in an economy dominated by a Ricardian view on the economy, fiscal multipliers are close to zero;
- Long-term unemployment rate depends only to a small extent of government intervention. Thus, the multiplier effect of fiscal policy will be less, as the unemployment rate is close to NAIRU: increased demand in the economy lead to higher demand for labor, but lower unemployment will be increasingly lower.

Summary neoclassical (Hicks, Samuelson) combines aspects of Keynesian short term with the neoclassical where GDP evolution is influenced by specific aspects of the offer, namely the accumulation of capital and labor, thus resulting that expansionary fiscal policy will generate growth consumption and GDP only short-term, helping to increase domestic demand.

New Keynesian economics (Taylor Blanchard, Mankiw) captures assumptions similar to those of the new economy, classical (optimization of forward-looking decisions, rational expectations), but requires the existence of real and nominal rigidities. It suggests that fiscal policy has less impact on the economy because:

- consumption does not depend on current consumption, but permanent income so that individuals will react to a fiscal expansion if it generates a long-term income growth;
- fiscal expansion generates inflation expectations; if they are rational decisions will influence the government very little economy in the short term;
- consumers act according to the principles of Ricardian equivalence;
- There are a variety of imperfections in ECOM and aggregate supply will not react immediately to changes in demand, so that fiscal policy can affect business cycle fluctuations.

Real business cycle theory (Kydland, Prescott) - These business cycles are caused by fluctuations in the growth of total factor production, and the distinction between short and long term analysis of economic fluctuations and the potential GDP is abandoned. Effectiveness of fiscal policy will only be given for the sustainable growth of potential GDP. The main tools that can generate these effects are productive public expenditure (education, research and development, public investment) and capital charges applied.

2. THE OPTIMAL TAX SYSTEM

Tax policy decisions by which the whole structural modeling of the tax system, ensuring its operation in order to achieve the desired objective by public decision-maker in the economy.

Fiscal policy is therefore a component of the financial policy of the state, which comprises both assembly regulations setting and levying taxes and embodying state options in terms of tax and fees and decisions concerning public expenditures are financed. But its components are concerted with the fiscal policy or monetary policy in question and the price of employment etc. to integrate into general policy.

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European policy on tax has two components: direct taxation -which is their responsibility and indirect taxation, which affects free movement of goods and services.

2.1. Principles used in an optimal tax system

An important problem today lies in the attention of many economists and policymakers is to optimize the tax system. Introduction or modification of a tax is an issue that must be given due importance for all consequences of this on multiple levels: economic and financial, social and not least politically. To meet certain requirements for quality and performance, modern tax systems must be organized and operate on the basis of commonly accepted principles. Among them stands out the principle of fairness and efficiency, which makes counterbalance, most often the subject of disputes related to taxation, tax each seeking to placate more or less, these two demands. More so as, while accumulating grievances population can contribute to the fall from power of political factors, which outlines its fiscal policy on grounds of fairness.

If, in terms of ensuring horizontal equity, it is generally well accepted and appreciated, appearing on vertical equity controversies about the possible ways of achieving income redistribution, considered by some arbitrary redistribution. In Romania fiscal equality is enshrined in the Constitution, so the legal system, taxation must ensure a fair distribution of the tax burden. " Shaping the tax system to achieve maximum efficiency of tax collection, involves a thorough analysis of the amount of income that can be obtained in parallel with the costs incurred for their collection. According to the principle of tax collection efficiency (or yield) taxes to be charged with minimum cost and by obtaining a large amount of revenue to the state budget.

Generally, it is considered that a tax with a wide range of coverage and low levels have a higher yield than a tax with a small area with high rates. Tax collection efficiency is conditional upon a number of factors, including very important, especially in the conditions of our country.

3.TREATY ON STABILITY, COORDINATION AND GOVERNANCE IN THE ECONOMIC AND MONETARY UNION (THE FISCAL COMPACT)

The treaty is designed to strengthen fiscal discipline in the euro area through the so-called "rule of budgetary balance" and an automatic correction mechanism. For fiscal treaty to enter into force, it had to be ratified by 12 Member States. The condition was satisfied after Finland, the 12th in the Eurozone which adopted the treaty, has deposited instruments of ratification on 21 December 2012 a press release from the EU Council website.

The treaty was designed after the Heads of State and Government of the euro area decided in December 2011 that stronger measures are needed to strengthen stability in the euro area. The fiscal pact was signed on 2 March 2012 by 25 EU member states, except Britain and the Czech Republic.

Treaty on Stability, Coordination and Governance would be built as soon as possible in existing EU treaties and the steps needed to achieve this should be made in the next five years.

According to the tax treaty, the national budgets of the states that joined must be balanced or in surplus. The annual structural deficit does not exceed 0.5% of GDP. In addition, the deficit must be in compliance with the minimum target for long-term sustainability of the country, established by the Stability and Growth Pact.

Temporary deviation from this "golden rule" budgetary balance is only allowed in exceptional economic circumstances, for example when an economic downturn. If government debt is significantly below the 60% of GDP deficit limit could be set at 1% of GDP.

If a Member State deviates from the golden rule of budgetary balance, it will trigger an automatic correction mechanism. It will need to correct deviations in a clearly defined time period.

On the other hand, automatic correction mechanism will have to respect the prerogatives of national parliaments. Member States will have to incorporate provisions on budgetary discipline and automatic correction mechanism in national legislation, preferably right in the Constitution, within one year from the entry into force of the tax treaty, in this case from 1 January 2014.

If a Member State fails to transpose into national law the rule concerning budgetary balance and regulation on automatic correction mechanism, the European Court of Justice will have jurisdiction to decide the case. Court verdict is binding and if it is not respected can apply a penalty of up to 0.1% of GDP.

The money will go directly into the coffers of the European Stability Mechanism (ESM) if the state is part of the Eurozone or go to the general budget of the EU, whether the country has passed the single currency.

In addition, a Member State subject to an excessive deficit procedure will have to complete a budgetary and economic partnership program.

The program will include a detailed description of the structural reforms that Member State will have to implement to ensure effective and durable correction of its deficit. Such programs will be submitted for approval to the EU Council and EC, and their implementation will be monitored under the rules of the Stability and Growth Pact.

Member States which have ratified the treaty will inform the EC and the EU Council on public bond issuance. In addition, they will discuss and, if necessary, will coordinate among themselves and with the EU institutions before all major economic reforms that he intends to apply.

The Treaty also provides that the Heads of State and Government of the euro area must meet at least twice a year in the euro area summits, to be attended by the EU Commission. Within them would be elected by a simple majority a chairman of the summit. Lastly, mention the fiscal pact, European Central Bank and the respective presidents of the European Parliament may be invited to these summits Eurozone.

The new architecture emerging fiscal policies in the European Union aims to create a more robust and effective framework for fiscal policy coordination and surveillance of Member States. The new structure is a direct response to the sovereign debt crisis, which showed that stricter rules be imposed, given spillovers that unsustainable public finances have had in the Eurozone. The new

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framework builds on experience gained so following the failure of the initial architecture of the European monetary union and aims to strengthen the guiding principle of sound public finances enshrined in Article 119 (3) TFEU.
The European Council meeting in March 2012, all Member States except the United Kingdom and Czech Republic, have signed the Intergovernmental Panel on Stability, Coordination and Governance in the Economic and Monetary Union, whose budgetary component is fiscal pact (Croatia has not signed no treaty before its accession to the EU of 1 July 2013 or after.) However, the Czech Republic has adopted and ratified in 2014. the fiscal pact requires dedication "golden rule" on budgetary balance, that the lower limit deficit structurally should not exceed 0.5% of GDP (if the public deficit is below 60% of GDP, the limit is 1% of GDP) into national law, preferably at constitutional level ("debt brake").Member States may bring actions before the European Court of Justice of the European Union against other Member States where this rule was not applied properly. Other provisions include, among others, triggering automatic correction mechanism and stricter rules for countries under an excessive deficit procedure. In addition, the European Stability Mechanism may provide assistance only to Member States which have signed the fiscal pact.
The impact of fiscal stimulus programs economies depends on the degree of economic openness and financial integration of the countries in which it applies. For example, in small open economies, most of the consumption growth is directed towards imports. Therefore, unless the fiscal stimulus packages are perfectly coordinated internationally, countries will prefer open relaunch by increasing public investment, which generates a greater impact on the internal market. Because fiscal stimulus packages to be successful economy should aim at targeting alcohol in order to ensure a higher multiplier effect of fiscal policy. In evaluating the success of an expansionary fiscal policy and the question arises' confidence of economic agents "- if they do not trust the long-term fiscal stability in economies promoting expansionary policies now, then they react less to the current fiscal stimuli. Short-term effects of fiscal stimulus packages are influenced by perceptions of the economy long-term costs thereof. Thus, the expansionary fiscal policy is perceived more costly in the long term (rapid growth of public debt and its associated service, increase country risk), the less it will affect the economy in the short term. Consumers without financial constraints will prefer to cover future risks, and fiscal expansion will be reflected in reduced consumption, generating a negative multiplier (Giavazzi, Pagano, 1990; Alesina, Perotti, 1997). Expansionary fiscal policy effectiveness depends on the degree of credibility of the measures announced. The more they are perceived as inconsistent, so any decision to try to stimulate the economy would introduce instability into the economic system and entail reductions in private consumption. Effectiveness of fiscal stimulus packages was estimated using macroeconomic models for determining the fiscal multipliers. For example, if the US model was used Romer and Bernstein, under which public expenditure multiplier is greater than one in both the short (1.05, after the first year) and long term (cumulative 1.55 after four years). However, there is another Smets-Wouters model developed by claiming that size budget multiplier is lower throughout the period 2009-2013 compared to the previous model. Economic growth would be lower than the size of the fiscal package to stimulate the economy, following a permanent effect contraction in consumption and private investment. Four years after the shock generated by the tax package, GDP does not increase by only 40% of the initial budget effort. The model assumes the existence of economic agents who form expectations and forward looking tools that anticipate profound changes in the years after fiscal expansionary fiscal shock. Specific model is less flexible economies, those that have certain constraints (such as an agreement with the IMF) or those characterized by a state of disbelief / pessimism private businesses. The harder the economy will react to fiscal shock initially, will also increase profitability reversal of fiscal policy promoted (to cancel the impact of deepening the budget deficit). The discretionary fiscal measures covered by programs to stimulate the economy should be interpreted in the context of rising budget deficit and rising public debt. Much of the increase in the deficit is the result of automatic stabilizers in times of economic reduction (acting mainly on the revenue side). For example, if OECD countries increased budget deficit from 1.5% of GDP in 2007 to around 9% of GDP in 2009 and public debt has reached about 100% of GDP. 75% of this increase in the deficit was the result of automatic stabilizers in the context of automatic reduction of budget revenues due to weakening economy. Thus, following the increase of public spending by 1% of GDP, will take place in a first stage increase the budget deficit by the same amount. However, since domestic production will react more to the fiscal stimulus, the budget revenues will grow automatically (eg from indirect taxes due to increasing consumption) and the budget deficit will be reduced. Thus, if a public spending multiplier of 0.7 (first year), GDP will grow by 0.7 euros after tax of one euro a boost. According to research conducted for OECD countries, the budget deficit automatically lowers GDP growth by about half, ie € 0.35. It was therefore achieved an increase in the budget deficit by only 0.65 euro (one euro and 0.35 euro initial increase due to the decrease in GDP growth). The fiscal multiplier will be higher in the short term, the medium term budget deficit will be lower.

CONCLUSION

Overall reform of EU economic governance framework and fiscal policies include, in addition to rules PSC reviewed and Treaty Intergovernmental Panel on Stability, Coordination and Governance in the Economic and Monetary Union, two regulations aimed at better strengthen economic governance in the euro area (package the two legislative proposals - "two-Pack"):

1. Regulation (EU) no. 473/2013 of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the euro area Member States
2. Regulation (EU) no. 472/2013 of May 21, 2013 on the strengthening of economic and budgetary surveillance of Member States experiencing or threatened with serious difficulties with respect to their financial stability in the euro area.

The main elements of the first Regulation provide for common budgetary timeline for all euro area Member States, and rules on monitoring and evaluation by the Commission of Member States' budgetary plans. Where serious breaches of the rules of the SGP, the Commission may seek review of those plans. In addition, it requires Member States of the euro area subject to an excessive deficit procedure to present a program of economic partnership which should be presented in detail the measures and structural reforms necessary to ensure a correction efficient and sustainable excessive deficit. The Council, acting on a proposal from the Commission, shall adopt opinions on economic partnership programs.

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The second Regulation concerns the Member States facing serious difficulties or are threatened with such difficulties with regard to their financial stability It provides rules to strengthen supervision, financial assistance and supervision of post-program (if not repaid at least 75% of the financial assistance received).

European Fiscal Compact assumed a commitment from the states participating in governance and fiscal solidity to introduce provisions for balancing the budget in the Constitution, strengthening regulations on the excessive deficit procedure by automating sanctions and European Commission draft budget submission for verification.

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