FISCAL ILLUSION – AN ACTUAL PERSPECTIVE

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Abstract: *The ongoing pro-development strategies that countries are promoting in the current era are based on the idea of finding as much public financial resources as possible to cover the growing financial needs. The more citizens understand less the financial / tax-related changes, the more they will transfer a larger part of their income or wealth to the state. This creates the phenomenon of "tax illusion" first developed by Italian economist Amilcare Puviani in 1903.*
Keywords: *fiscal illusion, fiscal sociology, fiscal policy.*

1. INTRODUCTION

After more than a century, governments behave in the spirit of this concept, making non-transparent public financial decisions that lead to an increased size of government and imprudence in the tax matters. Thus, taxpayers are in the situation of not fully understanding the tax burden related to the income earned as a result of truncated information transmitted by public decision makers and uncorrelated fiscal measures proposed and applied by governments. In this sense, a fiscal measure that wants to have a positive impact on the disposable income of individuals, such as the reduction of the income tax of individuals, becomes, in fact, a tax illusion, since it is accompanied by a transfer of social contributions from the employer to the employee, which thus cancels out the effects of a supposed measure to stimulate consumption/saving taxpayer decisions.

With these terms, Puviani wanted to point out the opacity that could be administered by public decision-makers in the imposition of taxes or in public spending management. These kinds of illusions are the product of a relationship between electors and rulers; therefore they can only be studied considering both sides (Mourao, P., 2007). Jensen and Vestergaard in 1999 define fiscal illusion as a situation where public decisionmakers (namely, the European Union, EU) only incorporate a part of the costs incurred by the constituents (the Member States).

2. STATE OF THE ART

Some studies (Wagner in 1976 and Baker in 1983) have analyzed the concept of tax illusion by linking it to the level of complexity of the tax system. Thus, the more complex a system of public revenues is, the more it is possible to experience this phenomenon of tax illusion, because it is difficult for the individual to identify the price of the economic activities and actions expressed in taxes he pays and then he underestimate the final global fiscal burden. Another form of fiscal illusion derives from the income elasticity of the revenue system. Thus, as the public revenue system is characterized by a high level of revenue elasticity, the level of public spending will increase more (Oates in 1975).

“A further form of fiscal illusion is the flypaper effect (Dougan and Kenyon, 1988), which holds that a tendency exists for categorical lump-sum grants to increase public expenditure by more than an equivalent increase in income from other sources” (Mourano, 2007). Another form of fiscal illusion refers to the fact that an increase in a jurisdiction's proportion of renters will increase the level of expenditures (Bergstrom and Goodman, 1973). In addition, we can discuss another form of fiscal illusion, recognized in the specialized literature as debt illusion, that is, financing public programs through loans can lead to an altered image of the cost of public services offered to citizens.

3. FISCAL ILLUSION AND THE ELECTORAL CYCLE

In other terms, Downs in 1957 concludes that politicians have no reason to correct the tax illusion, but rather, they want to spend as much as possible to win the election in the future. In fact, observing the level of public expenditures in Romania in previous years, it is easy to accept this principle regarding decisions that only concretize political opportunism and influence the outcome of elections through fiscal-budgetary measures whose impact is not previously determined.

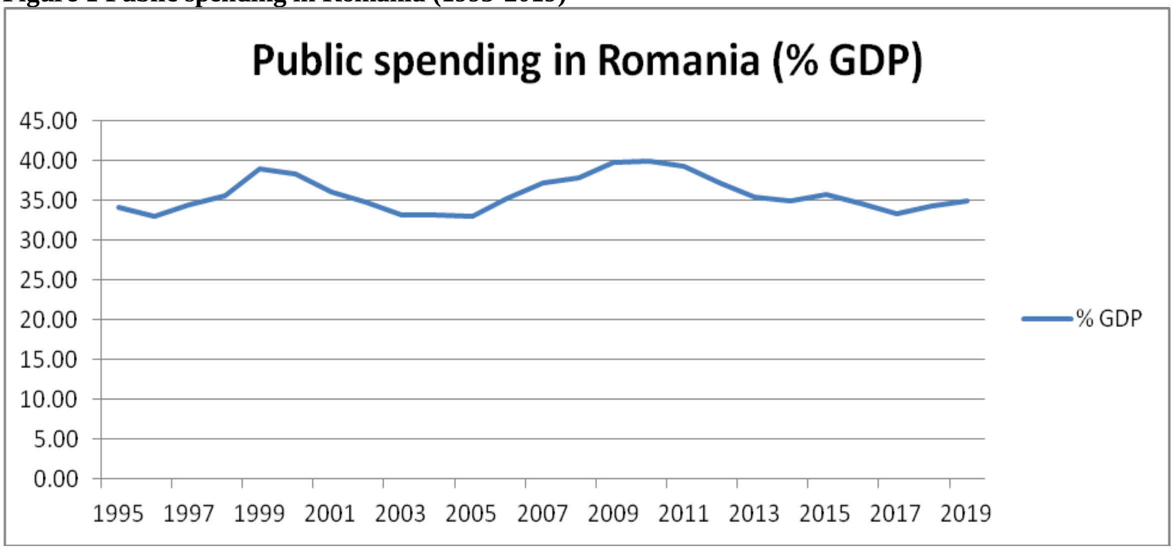
Table 1 Public spending in Romania (1997-2017)

Country	Romania	
1997	34.39	
1998	35.58	
1999	39.00	pre-election year
2000	38.34	elections
2001	36.04	
2002	34.81	
2003	33.14	pre-election year
2004	33.25	elections
2005	33.08	
2006	35.21	
2007	37.19	pre-election year
2008	37.77	elections
2009	39.70	elections
2010	39.88	
2011	39.34	pre-election year

2012	37.23	elections
2013	35.38	pre-election year
2014	34.96	elections
2015	35.76	pre-election year
2016	34.62	elections
2017	33.37	

Source: http://ec.europa.eu/economy_finance/ameco/user/serie/ResultSerie.cfm

Figure 1 Public spending in Romania (1995-2019)



Source : http://ec.europa.eu/economy_finance/ameco/user/serie/ResultSerie.cfm

In addition, Alesina and Perotti (1996) show some practices through which politicians can make public and less transparent budgets, such as incorrect forecasts and macroeconomic estimates generated by fiscal decisions, the use of multi-annual budgeting, and others actions.

4. FISCAL ILLUSION INDEX FROM MOURANO'S PERSPECTIVE

Some authors (Mourao, P.R., 2007) have built an index of the value of the fiscal illusion, using data series belonging to a number of 68 democratic countries. The purpose of creating this index was to create the necessary framework for assessing political performance and democratic quality. It is important to note that fiscal illusions can be created by handling both sides of the budget: tax revenue and public spending, with public decision-makers thus minimizing the resistance to the dominant category through various tactics used to manipulate them.

Some economists (Alesina and Perotti, 1996) highlight the fact that politicians tend to use techniques to minimize the level of transparency of public budgets; in fact, these politicians are supported by agencies responsible for producing official statistics and studies on the possible effects of fiscal-budgetary policy changes on public revenues or expenditures. The authors chose 26 variables to make the fiscal illusion index, taking into account elements related to the literature that defines the analyzed concept and elements related to the materialization of the effects and the factors that ensure the consistency of the country-wide concept. Thus, the variables envisaged belong to the following domains and ensure a clearer picture of the level of the tax illusion.

Tabel 2: The dimensions of the fiscal illusion index

	Focused Dimensions
1	Composition of Public Revenues
2	Money creation
3	Public Debt
4	Composition of Public Debt
5	Relevance ofcertain revenue sources
6	Political strategies of the ruler group
7	Public expenditure manipulation
8	Governmental discourse manipulation and electorate believes
9	Different objectives of governmental agents
10	Immaturity of the democracies
11	Composition if the public capital outlays
12	Government rent-seeking
13	Relevance of trade taxes
14	Interaction between interest groups and political behavior
15	Real public budget
16	Composition of public expenditure
17	Electorate preference on national issues

Mourão, P., 2007. Towards a Fiscal Illusion Index, MPRA Paper 9760, University Library of Munich, Germany, revised 28 Jul 2008.

As a result of his research, the author published the index of the fiscal illusion for all the analyzed country's tax, presenting the value for 1960 and 2006, the higher values of the index denoting a higher level of fiscal illusion in the respective countries. As a general observation, the published data show that the value of the index is decreasing for all the analyzed countries, which demonstrates that the maturing of democracies is an important factor in the level of the tax illusion.

Tabel 3 Fiscal illusion index -selection

Country	Fiscal Illusion Index 1960	Fiscal Illusion Index 2006
Bulgaria	0.477	0.283
Italia	0.811	0.312
Polonia	0.986	0.767
Romania	0.863	0.646
Rusia	0.999	0.830
USA	0.381	0.219

Mourão, Paulo, 2007. "Towards a Fiscal Illusion Index," MPRA Paper 9760, University Library of Munich, Germany, revised 28 Jul 2008.

From the above table (which is an extract from Maurao's research) we can see that in countries such as Romania, Poland and Russia this index is still very high (at the time of the analysis), which shows that in these countries the level of manipulation through fiscal-budgetary decisions is a higher one, and from our experience, we find that these practices persist over time, generating a series of pressures on the sustainability of public finances.

5. THE LINK BETWEEN FISCAL ILLUSION AND FISCAL SOCIOLOGY

Conceptually, fiscal illusion can be attached to the concept of fiscal sociology. Thus, fiscal sociology, which concretizes the relationship between the state and the citizens by the virtue of the socio-economic relations carried out in the double-sense, in which both parts, the citizens and the state, are in the position of receiving and paying certain amounts, definitive most of the time, may become a land of manifestation of the tax illusion. It is important, however, to observe the one-way sense of tax illusion in relation to the bidirectional sense of fiscal sociology. Thus, only the state can become the initiator of procedures that lead to tax-illusion effects, while fiscal sociology takes into account the overall fiscal relationships of the state-citizen relationship.

Identifying this link between fiscal sociology and tax illusion is a new approach to economic theory, and I think it needs to be carefully analyzed in the future. The nature of taxes set up in a certain tax system, through the traditional features of taxes, creates a situation where citizens who bear them do not know how much they will receive from their relationship with the state or how much they will pay / contribute. Even if the public financial activity is officially undergoing a process of transparency, assuming a real presentation of all revenue-generating and public spending decisions, the tax illusion takes place in certain situations.

6. CONCLUSIONS

The present paper had as its starting point the proposals for amendments to the tax legislation, some put into practice, announced by the representatives of the Romanian political power in recent years. Apart from the fact that many of these proposals did not have an applicable character, which demonstrates some awkwardness in the knowledge of the public decision-maker, many of the measures applied have had a competitive character, either canceling each other or leading to hidden effects in the economy, which led to an amplification of the state of fiscal illusion.

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