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## **The mediation of the Relationship between Organizations and Institutions. The Role of Organizational Culture**

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### **Abstract**

This article analyzes the relations between organizations and institutions and their mediation by the factors of organizational culture. After discussing the elements that distinguish organizations from institutions, we will discuss W. R. Scott’s conception regarding the constitutive and functioning structures of the institutions. The following section focuses upon D. C. North’s theory regarding the institutional stability and change, as well as the costs involved by these processes. The last section systematizes a few perspectives regarding the mediation of the relations between organizations and institutions and the role of the organizational culture in this context.

**Keywords:** organizations, institutional structures, mediation, regulations, organizational culture.

### **The distinction between organizations and institutions**

The organizations are entities made up of different groups with the purpose of regulating the relationships between them according to certain rules of social cooperation. They benefit from a certain organizing and functioning autonomy, acting not only as a stimulating factor, but also a coercive factor as opposed to the needs and aspirations of the members of society.

In the interpretation of Giddens (2010), organizations differ among themselves according to criteria such as: purposes, the nature of their activities, the mechanisms of coordination and authority, the legitimacy system, the formal or informal status of their functioning relationships, the system of interactions between their members, the

available resources, the economic, social, political and cultural (institutional) context in which they operate.

Researchers in this field (Scott, 2004; Năstase, 2004; Vlăsceanu, 2005; 2010) insist upon the fact that any formal organization has certain characteristics: it is deliberately created by a person or social group; it develops formal structural relationships and interdependent relationships between people; it has a set of objectives which guide the work of its members; it is self-perpetuating; it practices a certain division of the work to be performed by individuals; it manages material, human, financial or symbolic resources; it ensure communication between individuals and groups; it establishes a hierarchical structure and seeks to impose the presence of a leader or leaders.

The main conclusion that emerges here is that organizations have a certain normative structure (a set of rules, norms and remedies), a power structure (hierarchies, degree of centralization, the freedom of individuals, processes of cooperation or competition) and a staff structure (networks of statuses and roles, the distribution of specific tasks to each member of the group). Therefore, organizations differ among themselves both in terms of their performance and regarding their types of action, goals achieved and those persons involved in solving the goals set. What they have in common would be: their members' interaction goals, the character regulated by the principles and rules of these interactions, the continuity of a specific relationship structures as a result of these interactions, the imposition of a set of features, relationships and distinct responsibilities for their members (Scott, 2003).

In the client's language, the term institution is often overlapped to that of the organization, although there are significant differences between them. While the organization is a social group in which there network of relations based on certain norms and values, the institutions is a system of constraints that regulates life and human activity. Moreover, although both institutions and organizations provide a framework for human interaction, the difference between them is that "the institutions refer to the way in which the rules of human interaction were created and evolve, while the organizations offer the manifestation framework of the necessary strategies and skills people need to enforce the rules". The consequence arising here has a double meaning: a) to understand the operation and development method of the organizations



it is necessary "to refer to the existing institutional system, that is the formal and informal rules prevailing in a society", b) the study of the organizations should begin with the study of the institutions that have generated them and should then continue "with the analysis of the way in which institutions operate in the existing organizations to identify the potential sources of compliance, and also of institutional change" (Vlăsceanu, 2003, pp. 90-91 ).

Starting from these aspects, I will now analyze the contribution of W. R. Scott upon the process of mediation of the relations between organizations and institutions, as well as upon the factors which characterize the process of institutionalization.

### **The relationships between organizations and institutional structures**

The British researcher starts from the idea of multiple relations that characterize the relations between organizations and institutions, arguing that institutions are defined by the normative framework based on which the organizations shape their actions and interactions strategies, through the stability and resistance to change, by some symbolic elements and material resources, as well as their tendency to reproduce and transmit from generation to generation. Moreover, the institutional framework affects the appearance, operation and development of the organizations, just as the organizations, in their turn, influence the evolution of the institutional framework. From this point of view, at least three aspects should be highlighted: the first aspect refers to the fact that institutions are "the generative basis" of the organizations, which means that each system's rules or institutional constraints correspond to a particular type of organization; the second part takes into account the fact that the organization can become a factor of institutional change in the conditions under which certain rules or constraints are found to be inoperative; the third issue concerns the fact that the organizations can be considered contexts in which institutionalization and deinstitutionalization operate in the sense that the organizations reproduce the institutions, but also change them (cf. Scott, 2004, p.70).

Following the thread of this argument, the author I am referring to develop an analysis of the constituent and functioning structures of the institutions, an analysis which can be summarized around the following characteristics (Scott, 2004, p 72 and the following):

a) The regulator pillar - defines the activities of establishing the rules that constrain the behavior, but also the ones that monitor and sanction their compliance. The regulatory systems, as well as those of rewards or punishment, can operate both through diffuse and informal mechanisms (involving customs, traditions, customs etc.) as well as through certain formalized rules and mechanisms of enforcement.

The components of the regulator pillar - force, coercion, penalties and interest - are often mediated by the existence of official rules or laws. In order to ensure the compliance of individuals and groups with the rules and laws, no power structure uses only the constraint and imposition mechanisms, but also provides incentives or rewards.

b) The normative pillar – includes the value and norms systems which introduce in both the prescriptive dimension and that of assessment and establishing the need or obligation within the social life. While the values are general conceptions about what is desirable, the rules designate the legitimate means to achieve goals. The legal systems impose restrictions on human behavior and legitimate social action, they give individuals and group certain rights, but they also require responsibilities or obligations. The roles prescribed are social rules which serve at describing the behavior uniformities of the members of a group and define the social identities of individuals.

c) The cultural-cognitive pillar – reveals the central position held by the cultural and knowing elements in the production of certain events or schemes of common understanding, of a shared logic of actions, as well as certain sustained cultural significances. The idea in view relies upon the mediation action between the stimuli from the exterior, the level of cultural and cognitive acquisitions of the human subject and the repertoire of answers of the individual or group. In order to understand and explain a social action one must take into account not only the objective conditions which characterize the respective activity, but also their subjective interpretation, that is the significances associated to them within the system of institutional relations. The cultural and cognitive context is the one who ensures the setting of certain social roles which in time become models of institutional organization.

Scott's analysis brings into attention two essential aspects. The first aspect refers to the idea of organizational culture, which includes cognitive, affective and normative elements, as well as those referring to

the power structures, the social and moral climate, the behavioral regulations, or the means of understanding and interpreting events.

The second aspect concerns the extension of the framework of analysis of organizations and institutions, an extension which involves certain aspects such as: the interaction between organizations and institutions; the relation between the regulatory, normative and cultural and cognitive processes; the elements that lie at the basis of different types of organizational behaviors; the interdependency of the institutional structures and the individual action; the problem legitimizing institutions; the mechanisms of institutional stability and of the processes of institutional innovation and change; the formal-informal relation within the operation of the institutions and so on.

From this list, the legitimization of the institution, for instance, is considered an indicator of the stability of rules, regulations and routines, but also a premise of the propagation of institutions. For the study of institutions, this aspect has a triple significance: the propagation of a set of rules or structural forms in time and space reveals the force of an institutional structure; since the propagated elements are adapted and incorporated by the organizations, these studies are also called “studies of the institutional effects”; the propagation of an institutional form or practice can be considered as a possibility of institutional change.

These ideas lead us to D.C. North’s approach to institutional stability and change, a theme which I will discuss in the following pages.

### **Institutional stability and change**

After a complex analysis of the phenomena which occur within the social and economical institutions, Douglas North (2003) reaches the conclusion that the understanding of the changing process involves, before anything else, a reference to the characteristics of stability which the idea of institution is associated with. Thus, he writes: “Stability is obtained through a complex set of constraints, which include official rules arranged in a hierarchy, where each level is more expensive to be changed than the inferior one. They also include unofficial constraints, which are extensions, elaborations and categories of rules and which have the tenacity to survive, because they became a component part of the common behavior (...). The complex interaction between the official rules and the unofficial constraints, together with the way in

which they are imposed, defines our daily life and orientates us in our daily activities...” (2003, p.77).

According to North’s theory, the change of official rules implies that the parts involved should renegotiate the institutional framework, a renegotiation which could start from the simple aspects of “the social contract” all the way to the full reshaping of an institution. Talking about continuous and discontinuous changes of the institutional structures, as well as about the different political, economical and ideological conditions they determine, the author insists upon two main aspects.

The first aspect refers to the change of the official rules is expressed in the following terms: “The impossibility to reach compromise solutions may reflect not only the lack of mediation institutions, but also the limited degree of freedom of the enterprisers to negotiate and, at the same time, to keep their loyalty for the groups they belong to. Thus, the real sets of choices of the parts in conflict may not intersect, so that, although there may exist potential significant earnings from the resolution of the misunderstandings, the combination between the limited freedom of negotiation of the enterprisers and the lack of mediation institutions blocks the resolution of misunderstandings” (2003, p.82-83).

The second aspect draws attention upon the fact that, although the official rules may change in different means and forms, the unofficial constraints have the tendency to perpetuate themselves, or, in any case, to modify with greater difficulty because they solve fundamental problems of direct relationships between individuals and groups. Moreover, the variety of these unofficial constraints may have a decisive influence upon the stability, evolution and change route of the official rules which define a given institutional framework.

North offers special attention to the case where both “marginal” modifications and the discontinuities in the institutional change are influenced by ideas and ideologies, which shape the mental constructs that individuals use in their interpretation of the world and in the choices they make. The author does not forget to underline the fact that, “through the structuring of human interaction, the official institutions influence the price we pay for our actions and, to the extent to which the official institutions are structured willingly or accidentally to diminish the price of acting in the virtue of one’s own ideas, they offer the individuals the freedom to include their own ideas and ideologies in the

choices they make” (2003, p.101).The thesis that North accredits is that the existing institutions or the ones promoted by society have the capacity to generate different types of organizations, to set their functioning limits and to establish certain criteria of evaluation or means of recovering the organizational performances.

The problem posed next is the one connected to the mediations which take place between the organizations and the institutions, as well as the factors which intervene in the development of this process.

### **The mediated character of the interactions**

Not only Scott’s analysis, but also that of North reveal the fact that the organizations can react in different ways to institutional pressures, just as institutions, in their turns, influence the strategies which the organizations can use.

Among the strategies adopted by an organization which is confronted with different institutional pressures, Scott (2004, p. 210-215) identifies: the strategy of submission and conformation (the motivation being given by the fear of sanctions or by the hope of obtaining a gain of legitimacy and resources); the strategy of compromise (which manifests itself especially in the institutional environments marked by conflicts); the strategy of avoidance (where certain aspects are hidden to protect other activities of the organization); the disobedience (which manifests itself when the regulations of the organization are fundamentally different from those of the institutions); the manipulation strategy (through which the organization tries to increase its capacity of negotiation and of creation of certain relative advantages).

According to Scott’s explanation, these strategies can be found in the internal dynamics of the institutions, as well as in their relations with the environments which ensure stability, the propagation and institutional change within processes oriented in a descendent and ascendant way.

The processes oriented in a descendent way (the base activities, the social propagation, constraint and integration, the authorization or conviction) or the possibility of institutions from a higher level to model the structures and actions of the individual or collective actors from the inferior level. Simultaneously, a process of a contrary direction is emerging, where the structures from the inferior levels model the contexts where they are taking place. Among the processes that ensure

the ascendant direction of influencing the institutional structures we can include the array of interpretations which contribute to the construction of the institutional identity, as well as the strategies adopted by one organization or the other for the institutional maintenance, propagation and change.

Looking at things from a wider perspective, the process of institutional change also involves an action of the members of the organization upon the values and representations which they involve, a fundamental role being given, thus, to the organizational culture.

Understood as an ensemble of values, regulations and behavior models, the organizational culture includes the organization's visible and less visible symbols, as is the case of motivations and rewards, the rights and obligations of the members, the type of inter-human relations and the connections with the external environment, the attitude towards change and towards the forms of management.

Authors such as Năstase(2004), Vlăsceanu (2005), Tărnău (2006), Şimandan (2009), Cureteanu (2011) and others shows that for the factors which contribute to the formation of the culture of an organization we can mention: the work group, the management style, the characteristics of the organizational structure (size, the history of the organization, its objectives, complexity and economical situation), the economic, social, judicial, technological and informational environment.

From one author to the other, we witness different approaches to the organizational culture. Recently, they refer to the relation with the processes of social innovation and the management of the strategies of change, to the aspects connected to the integration, coordination and motivation of the people within the organization, to the beliefs and practices which sustain certain policies, the methods of production, technical knowledge and the objectives of the organization, to the processes of social learning and change to changes and restructuring generated by the management of knowing in the informational society in which we live.

An interesting point of view in this respect is offered by Isac and Cureteanu (2011, p. 253), who consider that an adequate analysis of the organizational culture should take into account the following aspects:

- ✓ Individual initiative (the degree of responsibility and freedom of individuals);
- ✓ Integration (the extent to which subunits of the organization are encouraged to act in a coordinated manner);

- ✓ Support to employees from the managers;
- ✓ Identity;
- ✓ Time management;
- ✓ Reward criteria;
- ✓ Attitude towards risks;
- ✓ Attitude towards conflicts (the degree to which employees are directed to an open and critical way of conflict resolution);
- ✓ Models of communication (whether or not restricted by formal hierarchy);
- ✓ Control (number of rules, the extent of direct supervision of employees).

Relating the elements of organizational culture to the structures and instructions suggested by Scott, North, Vlăsceanu and other authors, we can state that the cultural changes take the form of social learning at the level of both organizations and institutions. Looking at the situation from this perspective, learning can bring change, innovation, restructuring, the participation of groups and individuals to decisions as well as to the anticipation of certain tendencies and harmful effects of the decisions existing presently. One must not forget that cultural change also involves de-learning and social learning processes at the level of groups and individuals and of the organization.

Noticing these interdependencies, M. Vlăsceanu (2003; 2010) says that in the processes of individual and group learning, the organization itself affirms itself as an organization which learns to adapt to new situations. This process is neither linear, nor lacking in contradictions. Since the thinking and acting methods are culturally induced, the organizational culture changes in a rather difficult way if the given organization “didn’t learn to become a learning organization”, concludes the author.

### **Conclusions**

At the end of this discussion we should remember that, firstly, the idea that organizations and institutions can be analyzed from different perspectives, and according to the perspective approached, one can formulate different explanations connected to their constitution and functioning means, with the relation to the formal and informal elements of with the interaction means of their members according the objectives and targets set.

Secondly, both organizations and institutions are based on a set of common regulations, certain common practices and action systems which manifest specifically according to the social, economical and ideological conditions of the environment, to the relations and interactions from within the organization, the functions of the members of the organization and their responsibilities, as well as the conscious and less conscious relations that the individual has with the organization or the institution.

Last but not least, we have to add that the organizations and institutions, together with certain activities and resources associated to them, supply stability and meaning to the social life. As a mediating factor, the organizational culture can ensure stability and performance to the institutions, as well as the premises of certain changes in the direction of producing a new cultural, cognitive, normative and regulatory configuration, whose duration and amplitude is different from one social, economical, political, ideological, cultural, judicial etc. culture to the other.

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## **From the European Union to Euroland - Historical, Fiscal and Political Aspects**

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### **Abstract**

The processes of normalization, internationalization, since its birth - the European Union - have never had a down hill ride. The hard times have been serious and numerous enough to even threaten it. On the tenth anniversary of its birth, the Euro seems to be going through another bad phase, threatening once again the Union as in the late seventies and early eighties of the last century. In that period a Frenchman, Jack Delors, head of the commission, with a lot of courage and determination, led the then European Community into the European Union with a single currency, the Euro.

Today is the Euro to be questioned due to the sovereign debt crisis that, because of the great recession, countries have had to compensate for the drop in household and businesses spending with the increased public spending and/or load of tax reductions. In doing so they have had to widen the budget deficit and burden the public debt, which in many cases has caused difficulties in financing the deficit and refinance its debts, as investors have began to distrust the solvency of countries, especially in Eurolandia, where the lack of a single government and of a central bank that does not have the power to fund the

States, makes it much more difficult to manage the crisis..

**Keywords:** Euro, Eurolandia, European Union, Treaty of Maastricht.

### **Introduction**

The Treaty of Maastricht (signed on 7 February 1992 in Maastricht)<sup>1</sup>, highlighted the concept of social cohesion already foreseen in the Treaty of Rome, where it was stated that the Member States committed themselves to "ensure a harmonious development by reducing the differences between the various regions and the backwardness of the least favored." Indeed, with the Single European Act of 1986, the foundations for a genuine cohesion policy designed to offset the prospect of the constraints of the single market, especially in those countries of southern Europe and those regions which, because of a greater backwardness, would inevitably have suffered more than others the consequences of free competition. The advantage of the Single Act has been to go beyond statements of principle and to predict commitment by member states to implement operational measures to reduce regional disparities. With the adoption of the Maastricht Treaty, Member States have made a further step towards European integration,

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<sup>1</sup> The European Union was born with the Treaty of Maastricht: a supranational and intergovernmental political body that since 1 January 2007 comprises of 27 independent and democratic member countries and which from 1 July 2013 will have Croatia as member. (G. Di Meglio, *I fondi strutturali*, in "Diritto della finanza pubblica Europea", edited by L. Di Renzo, ESI, 2008, p. 377). Thanks to the Maastricht Treaty, greater importance has been given to the concept of cohesion to reduce the gap "between various regions," rather than "between the levels of development of the various regions" as it was sanctioned in the AUE and added that among the less favored regions of the Community were "included the rural areas". In the document the Contracting Parties confirmed the considerable role of the structural funds in pursuit of that cohesion; agreed to establish the Cohesion Fund for Community grants, in favor of projects in the fields of environment and Trans-European networks with a GNP of less than 90% of the average GDP of European countries (E.M. Piccirilli, *Il finanziamento del bilancio comunitario*", in *Diritto della finanza pubblica europea*", edited by L. Di Renzo, ESI, 2008, p. 209 footnote 50.). In perspective of the Cohesion Fund less prosperous states were considered: Greece, Spain, Ireland and Portugal, countries which have been part of the Euro zone since day one.

since the policy of economic and social cohesion has become one of the fundamental objectives of the Community, to the point that its reinforcement is placed immediately after the creation of an area without internal frontiers.

The Union is currently a free market, called the Common Market, characterized, among other things, by a single currency, the Euro, regulated by the European Central Bank and currently adopted by 17 of the 27 Member States at the time of the Treaty of Rome in 1957<sup>2</sup> but which was later completed by countries belonging to the Schengen agreements, guaranteeing their citizens freedom of movement, employment and investment within Member States.

Today there is much talk of political integration, yes - political integration, no<sup>3</sup>. The politician, who was born in 1957, has not always had a thriving season. Very often he has risked sinking and very often has found a harbor where to anchor. One of the darkest periods of the European Union was the late seventies and early eighties, when the

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<sup>2</sup> The purpose of the Treaty of Rome was to create a common market that favors a balanced development of all member countries. On one hand it was about initiating negative integration, breaking down all the barriers against free trade between one country and another. On the other hand, if the integration process had stopped here, it would not have gone beyond a mere free trade area, in which, however, imbalances between the regions risked intensifying due to the sudden fall of the protectionist barriers. For this reason, and especially with the insistence of Italy, measures of negative integration were accompanied by measures of positive integration, to actively intervene in certain areas in order to develop a real internal market ensuring a balanced development of each region (Commentario CEE, edited by Quadri R. Paintings - Monaco R. - A. Trabucchi, Milan, 1965).

<sup>3</sup> It seems that the founding fathers of the European Community have given much importance to the legal aspect of the European system. The various treaties that have accompanied the process of European integration born with the European Coal and Steel Community in 1951 and continued to the present day with the Lisbon Treaty, represent the framework of rules that govern relationships within the Union, with the institutions, Member States and EU citizens. "A decisive role in the European legal system, even more than in other jurisdictions, is attributed to the case laws of both the Community court and the national court, which has defined from onset the essential and distinctive characteristics and that, over more than half a century, has greatly contributed to its consolidation and its development. The case law is an unavoidable fact in the appreciation of the legal system of the Union. Even the doctrine of Community law, still young though rooted in strong traditions of deep scientific study in all member countries, has focused mainly on the case law of the Court of Justice" (G. Tesauro, *"Diritto dell'Unione Europea"*, Padova, 2012, pg. 2).

European Community really risked sinking. Danger avoided thanks to the work of great statesmen<sup>4</sup> who gave birth to the Maastricht Treaty,

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<sup>4</sup> With the establishment of the Single Market and the start of the Delors management, under the motto "one market one currency", it was logical to initiate a new phase of accelerated integration. On the basis of the Delors Report of 1989, this foresaw a three-step. The purpose of the Treaty of Rome was to create a common market that favors a balanced development of all member countries. On one hand it was about initiating negative integration, breaking down all the barriers against free trade between one country and another. On the other hand, if the integration process had stopped here, it would not have gone beyond a mere free trade area, in which, however, imbalances between the regions risked intensifying due to the sudden fall of the protectionist barriers. For this reason, and especially with the insistence of Italy, measures of negative integration were accompanied by measures of positive integration, to actively intervene in certain areas in order to develop a real internal market ensuring a balanced development of each region (Commentario CEE, edited by Quadri R. Paintings - Monaco R. - A. Trabucchi, Milan, 1965).

It seems that the founding fathers of the European Community have given much importance to the legal aspect of the European system. The various treaties that have accompanied the process of European integration born with the European Coal and Steel Community in 1951 and continued to the present day with the Lisbon Treaty, represent the framework of rules that govern relationships within the Union, with the institutions, Member States and EU citizens. "A decisive role in the European legal system, even more than in other jurisdictions, is attributed to the case laws of both the Community court and the national court, which has defined from onset the essential and distinctive characteristics and that, over more than half a century, has greatly contributed to its consolidation and its development. The case law is an unavoidable fact in the appreciation of the legal system of the Union. Even the doctrine of Community law, still young though rooted in strong traditions of deep scientific study in all member countries, has focused mainly on the case law of the Court of Justice" (G. Tesaro, *"Diritto dell'Unione Europea"*, Padova, 2012, pg. 2).

With the establishment of the Single Market and the start of the Delors management, under the motto "one market one currency", it was logical to initiate a new phase of the process; the negotiations began to actualize the economic and monetary union as well as a political union in an atmosphere of enthusiasm. It is without doubt that since the Single Act, Member States have shown the same feeling for economic and social cohesion with the success of very ambitious projects and far-sighted, coagulated by the Treaty of Maastricht, which promises incisive changes for the monetary policy, financial and economic integration of Europe and, in particular, lays the foundation for their co-ordination or their supranational integration: on the one hand for the transfer of monetary function from national to Community level (the renunciation of national monetary sovereignty is a fundamental political act) and for the transformation of monetary activities from restricted a discretionary activities to a bonded activity eventually identified with price stability; on the other hand, for a particularly stringent and official form between monetary union and economic union with the preparation of

which transformed the European Community into the European Union. Today, the Union is in a more or less similar condition to that of the seventies and eighties of the last century<sup>5</sup>: the Euro has repeatedly been questioned, weakening its value due to the effect of the sovereign debt crisis, caused by the Great Recession (generated by the financial crisis of the banks in the year 2007/2008 in the United States of America), countries have had to compensate for the drop in domestic and business spending with increased public spending and/or reductions in tax. In doing so, they had to widen the budget deficit and burden the public debt, which, in many cases, caused difficulties in financing the deficit and refinance its debts, as investors began to distrust the solvency of countries, especially in 'Eurozone' where, due to the lack of a single government and a central bank that does not have the power to fund the States, it is much more difficult to manage the crisis. The Eurozone countries have distinguished themselves as most reliable and least reliable. To stem the sovereign debt crisis, several measures have been taken by the Union. One of these was signed by the Heads of State or Government of the European Union, with the exception of the Czech Republic and the United Kingdom, 2 March 2012 that gave birth to the "Fiscal Compact" that is, to the Treaty on Stability, coordination and governance Economic and Monetary Union.

But it seems that all measures adopted (emergency funds, efforts to amend the Treaties, etc.) have not convinced the lenders (or investors) who continue to be skeptical because they do not see an ambitious project of the Union. Markets want to see where it's going to

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the convergence criteria , a compliance which does not allow Member States to start the third stage of the EMU. In fact, the choice of the Euro was a gradualist one (in three stages) to allow, given the economic disparities between Member States, the evaluation of the situations of the gradual reduction of the divergence (L. Letizia, *"Profili evolutivi della politica fiscale a livello europeo"*, in "Diritto della finanza pubblica europeo, edited by L. Di Renzo, ESI, 2008, p. 252 et seq.).

<sup>5</sup> "The accession of the United Kingdom, Ireland and Denmark (in 1973) coincided with a time of widespread and severe economic instability especially concerning money, which has contributed to a greater determination of European countries to pursue the achievement of Community objectives. Therefore, it is in the mid-seventies that the foundations for a stronger convergence of Economy and for a monetary union were initiated, through the creation of the European Monetary System, to strengthen the commitment to a progressive reduction of regional disharmonies through the implementation of programs to support the less developed regions and the creation of a special fund, the European regional Development "(Tesouro, op. cit., p. 8).

Europe. It is our duty to show that we believe in our political project and that we have concrete ideas and proposals to translate it into reality<sup>6</sup>.

Until now, this tool has been only a stopgap, because only by the taking bold steps towards greater financial integration it is possible to come out of the crisis (union bank, single supervisor, debt management policy, fiscal policy constrained) with a view to greater integration policy through the creation of a "Democratic Federation of Nation States" as he called José Barroso in his speech at the European Parliament, on September 12, 2012. It is about the transformation of the EU into a democratic federation with a sharing of power. In order to create this new entity it is necessary to sign a new treaty that even if it is a long and complex process, it is the only way to lead the Euro Zone into an area that shelters it from the crisis because the credibility of the currency depends on the credibility of those who support it and by its institutions<sup>7</sup>.

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According to Jerzy Buzek, former president of the European Parliament, to make the European political project credible, a new impetus must be given to our rational dream. The necessary elements are those recommended by the European Parliament: a stronger subservient Commission, a larger and more flexible Community budget, based on effective "own resources", a greater disposability to "mutualise" the debts of the Member States and a credible mechanism to allow respect for the future budgetary discipline. (Il Sole-24 Ore June 9, 2012 p. 13)

<sup>7</sup> The President of the European Commission, the former Portuguese Prime Minister José Barroso, on September 12, 2012 presented the European Parliament with the proposal of "single supervision" that is, to transfer the power of monitoring banks from Member States to the European Central Bank (ECB). The text specifies that the ECB will be competent for all key tasks of banking supervision that are necessary to identify the risks to the life of a bank, while the other supervisory tasks remain in the hands of national authorities. The ECB shall have the power to grant or withdraw a banking license in the countries using the Euro. It may, among other things, assess significant acquisitions in banks, impose additional capital on troubled banks, conduct investigations and inspections, request information, impose financial penalties (Il Sole-24 Ore source of 13/09/2012). There is no doubt that the proposed transfer of the power from national states to the European Central Bank implies a further transfer of sovereignty, which assumes that the European Parliament and national governments accept the proposal with caution. The proposal of the Commission (developed by the European Commissioner for the Internal Market, Michel Barnier) has two regulations that require two different procedures to get to the final application. The first concerns the transfer of power to the European Central Bank which in order to find application needs the consent of all 27 governments of the member states, the second regulation,

### **Material and Methods**

After the creation of the European Monetary Institute (EMI) on 1 January 1999, the European Central Bank (ECB) and the European System of Central Banks (ESCB) were born from it with the task of coordinating the single monetary policy. Two additional stages were distinguished: the first national currencies continued to circulate even if irrevocably tied to fixed exchange rates with the future Euro: in the second national currencies were replaced by the single currency. To move to the final stage each country had to meet five convergence criteria:

- ratio of public deficit and GDP must not exceed 3%;
- ratio of public debt and GDP should not exceed 60% (Belgium and Italy were exempted);
- inflation rate not exceeding 1, 5% compared to that of the three best performing countries;
- long-term interest rate not exceeding 2% of the average rate of the same three countries;
- two years permanence in the ERM, without fluctuations of the national currency.

Following the recommendations of the Delors report, in June 1989 the European Council decided that the first stage of the creation of the Economic and Monetary Union was to begin on 1 July 1990, a date when, in principle, all restrictions on the movement of capital between Member States were to be abolished. The Council, with the decision of 12 March 1990, also gave more responsibility to the Committee of Governors of the Central Banks of the Member States of the European Economic Community, which since its establishment in May 1964, had played an increasingly important role in the context of monetary cooperation; these responsibilities included holding consultations on the

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which should change the voting system in the European Banking Authority (EBA), it needs the consent of the European Parliament. As rightly said by President Barroso in his speech presenting the proposal: "We must move towards shared decision-making in terms of banking supervision in the Euro Zone" if we want the Euro continues to be credible. And it seems that now all states are taking the same path. In fact, it is no coincidence that the Barroso proposal came on the day when the German Constitutional Court gave the green light to the States rescue fund launched by the European Council on 4 December 2011, the so-called European Stability Mechanism (ESM). The ESM is a permanent fund designed to provide financial assistance, under close conditionality constraints, to the Euro member countries that request it.



monetary policies of the Member States and the promotion of co-ordination in this area aimed at achieving price stability.

In light of the limited time available and the complexity of the tasks involved, the Committee of Governors hastily began the preparatory work for the completion of the Economic and Monetary Union (EMU). In the first stage, all the introductory issues that were to be discussed in order to develop a work program by the end of 1993 were individualized, subsequently; the mandates of the sub-committees and working groups established for this purpose were defined.

For the implementation of the second and third stages, it was necessary to amend the Treaty which established the European Economic Community ("Treaty of Rome"), in order to create the necessary institutional infrastructure. Therefore, an intergovernmental conference on EMU was summoned, held in 1991 in conjunction with the Intergovernmental Conference on Policy. The negotiations ended with the Treaty on the European Union. Approved in December 1991 and signed in Maastricht on 7 February 1992. It amended the Treaty which establishes the European Economic Community - whose name was later changed to the Treaty which establishes the European Community-and it contained, among other things, the Protocol on the Statute of the European System of Central Banks and the European Central Bank and the Protocol on the Statute of the European Monetary Institute. However, due to delays in the ratification process, the Maastricht Treaty came into force only on 1 November 1993. Stage Two of EMU: the establishment of the EMI and the ECB.

The creation of the European Monetary Institute (EMI) on 1 January 1994 marked the start of the second stage of EMU and caused the dissolution of the Committee of Governors. The transitional nature of the EMI reflected the progress of monetary integration in the community. The Institute was responsible for the conduction of the monetary policy of the European Union, which remained the responsibility of national authorities, and was not competent to carry out transactions in foreign currency. The two main functions of the EMI were:

- strengthen cooperation between the central banks and monetary policy coordination;
- make the necessary preparations for the establishment of the European System of Central Banks (ESCB), for the conduction of a

single monetary policy and the creation of a single currency in the third stage.

For this purpose, the EMI represented a forum for consultations, discussions and exchange of information on monetary policy issues and defined the regulatory, organizational and logistical framework necessary for the ESCB to perform its tasks in the third stage.

In this way, the programming procedures of standardization that would lead to two convergences, one institutional and the other economic, are obtained:

- institutional convergence: with the objective of adapting their national legislation and align the management of monetary policy. Doing so, the financing of government deficit through central banks, the so-called 'channel treasure', was banned.

- economic convergence: with the objective of stabilizing prices, exchange rates and interest rates in the future euro zone.

In December 1995, the European Council agreed on the name the "Euro"<sup>8</sup> the European currency unit, which was then introduced at the

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<sup>8</sup> The Euro (EUR or €) is the official common currency of the European Union (as a whole) and the only one for seventeen Member States currently participating in the EMU (Economic and Monetary Union), namely Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Malta, Netherlands, Portugal, Slovakia, Slovenia and Spain. The last state to have adopted the Euro was Estonia in 2011. The complex of these countries, known informally as Euro Zone, with over 320 million inhabitants, taking into account also those country nationals that use the currencies linked to the Euro (the Principality of Monaco, the Republic of San Marino, etc.). The single currency directly affects over 480 million people around the world. In addition to the members of the Euro Zone, the European single currency is also used in six other European countries, following international agreements or after unilateral adoption.

Three microstates, i.e. the Vatican, Monaco and San Marino have adopted the Euro under the existing conditions of monetary union with EU member states. In addition, the Principality of Andorra has unilaterally adopted the Euro, but has ongoing negotiations with the European Union, not yet completed, similar to those of the three previous microstates. Montenegro and Kosovo have adopted the Euro unilaterally.

The Euro is the official currency also in all the overseas departments and overseas French collectivity: Mayotte (Africa), Reunion (Africa), Guadeloupe (North America), Martinique (North America), Saint-Pierre and Miquelon (North America), Saint Arthélemy (North America), Saint Martin (North America), French Guiana (South America). The Euro currency is also in Ceuta and Melilla, Spanish autonomous cities in North Africa. The debut of the Euro on financial markets dates back to 1999, while

start of the third stage of EMU, and confirmed that it would start on 1 January 1999. For the transition to the euro, a calendar of events was heralded, based largely on proposals made by the EMI. The Institute had also the task of carrying out preparatory work in view of future monetary and exchange rate relations between the Euro area and other EU countries. In December 1996 the EMI presented, a report that formed the basis of a resolution of the latter, to the European Council, which was adopted in June 1997, on the principles and core elements of the new exchange rate mechanism.

In December 1996 the EMI presented the European Council, and subsequently to the public, with a series of sketches of Euro banknotes that were put into circulation on 1 January 2002.

In order to complement and clarify the provisions of the Treaty, the European Council adopted the Stability and Growth Pact in June

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the circulation of money actually started on 1 January 2002 in the twelve EU countries that first adopted the new currency.

The name Euro comes from the initial letters of the word Europe, and was adopted by the European Council in Madrid in 1995 to replace the acronym ECU (from the English acronym European Currency Unit, or "European unit of account"), up to then used in the Treaties. The name had to be simple, unique and invariable. Many countries have decided to use the plural or the partitive plural of the name, despite the fact that the "Euro" on paper money shows clearly that the name should not know plural.

The name ECU, indicated in Article 3a of the Maastricht Treaty, was rejected for several linguistic reasons. It made sense in English, the language in which it was expressed, and in French, because the word *écu* means shield, which was an ancient French coin. The name, therefore, had no recall to the other countries. Then there was the "problem of German cow": the Germans would have had to call an ECU "ein ECU", which sounded like "eine kuh," that is, in fact, a cow.

The international three-letter code (according to ISO 4217) of the euro is EUR. A symbol was also designed (glyph) especially for the euro (€). After a public survey had narrowed it down to two, it was the European Commission to make the final choice. The winning symbol was inspired by the Greek letter epsilon (ε), as well as a stylized version of the letter "e".

The Euro is represented in the Unicode character set as well as in the updated versions of traditional Latin character set. The Western nations should pass by ISO 8859-1 (Latin 1) ISO 8859-15 (Latin 9) or, even better, utf-8 to represent this character.

The "unique name" actually has two variants: the first concerns the Greek language, the second language Bulgarian. Greece immediately got the permission to call the single currency "ευρώ" in Greek characters. Bulgaria obtained the permission during the negotiations for the Treaty of Lisbon to call the single currency "евро" in Cyrillic.

1997, which included two regulations to ensure budgetary discipline in EMU. A statement by the Council in May 1998 completed the Pact and expanded commitments.

On 3 May 1998 the Council of the European Union, comprising of Heads of State or Government in Decision 98/317/EC, verified the consensus that 11 Member States: Belgium, Germany, Spain, France, Ireland, Italy, Luxembourg, the Netherlands, Austria, Portugal and Finland met the necessary conditions for the adoption of the single currency, scheduled for 1 January 1999, and that they would therefore have participated in the third stage of EMU. Furthermore, on such occasion, the Heads of State or Government would reach an agreement on the personnel, which, on the recommendation of the Board, would be appointed as members of the Executive Committee of the European Central Bank (ECB).

At the same time, the Ministers of Finance together with the governors of the respective National Central Banks, the European Commission and the EMI, of the Member States which have adopted the single currency would agree that the bilateral central rates of the currencies of the participating Member States would have been used to determine the irrevocable conversion rates for the Euro.

On 25 May 1998 the governments of the 11 participating Member States appointed the President, the Vice-President and four other members of the ECB Executive Board. The assignment took effect on 1 June 1998, date of the establishment of the ECB. The ECB and the central banks of the Member States of the Euro Zone (Banque Nationale de Belgique, Nationale Bank van België, Belgische Nationalbank, Deutsche Bundesbank, Banco de España, Banque de France, Central Bank & Financial Services Authority of Ireland, Bank of Italy, Banque Centrale du Luxembourg, De Nederlandsche Bank, Banco de Portugal, Oesterreichische Nationalbank and Suomen Pankki - Finland's Bank) constitute the Eurosystem, which formulates and defines the single monetary policy in Stage Third stage of the EMU.

With the establishment of the ECB, the EMI concluded its mandate and was therefore placed in liquidation, in accordance with Article 123 (ex Article 109 1) of the Treaty which establishes the European Community. The preparatory work entrusted to the EMI was completed on time; the ECB spent the remaining months of 1998 on the final check-up of the procedures and systems adopted. Stage Three of EMU irrevocable fixing of exchange rates.

On 1 January 1999 the third and final stage of EMU began with the conduction of a single monetary policy under the responsibility of the ECB. On 3 May 1998 the Council of the European Union, composed of Heads of State or Government under the decision 1998/317/EC, sanctioned the Euro Zone countries fulfillment of the convergence criteria (Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, Netherlands, Portugal and Spain). On 31 December 1998 the Ecofin, with Regulation (EC) number 2866/98 fixed the irrevocable conversion rates between the Euro and the national currencies of the Euro Zone (Austrian Schilling, Belgian Franc, Finnish Mark, French Franc, German Mark, Irish Pound, Italian Lira, Luxembourg Franc, the Dutch Guilder, Portuguese Escudo and Spanish Peseta). On 1 January 2001, with the adhesion of Greece, the Member States of the EMU became 12; at the same time Greece joined the Eurosystem. On 19 June 2000 the Ecofin Council Decision 2000/427/EC sanctioned Greece with the fulfillment of the convergence criteria; together with Regulation (EC) number 1478/2000 fixed the irrevocable conversion rate between the Euro and the Greek Drachma

On 1 January 2007, with the adhesion of Slovenia, member states of the EMU became 13; at the same time Banka Slovenije joined the Eurosystem. On 11 July 2006, Ecofin Council Decision 2006/495/EC sanctioned Slovenia with the fulfillment of the convergence criteria, together with Regulation (EC) number 1086/2006 fixed the irrevocable conversion rate between the Euro and the Slovenian Tolar.

On 1 January 2008, with the adhesion of Cyprus and Malta, the Member States of the EMU became 15. On 10 July 2007 the Ecofin Council Decision 2007/503/EC and 2007/504/EC sanctioned Cyprus and Malta with the fulfillment of the convergence criteria, together with Regulations (EC) number 835/2007 and 836/2007 fixed the irrevocable conversion rates between the Euro and the Cyprus Pound and Maltese Lira

On 1 January 2009, with the adhesion of Slovakia, the Member States of the EMU became 16; at the same time Národná Banka Slovenska joined the Eurosystem. On 8 July 2008, the Ecofin Council Decision 2008/608/EC sanctioned Slovakia with the fulfillment of the convergence criteria by; together with Regulation (EC) number 693/2008 fixed the irrevocable conversion rate between the Euro and the Slovak Koruna.

On 1 January 2011, Estonia adopted the Euro, bringing the Euro Zone countries to 17.

### **Results and conclusion**

The monetary polo is from the European Central Bank, based in Frankfurt, and from the European System of Central Banks. The first body is the sole responsible for the common monetary policies, and cooperates with the second for the minting and distribution of notes and coins within the Member States.

One of the reasons for the crisis that has challenged and is challenging the same currency is due to the lack of an economic polo that Delors in 1997 proposed to put it alongside the Stability Pact. Today it can be assumed that the Euro protects but it does not stimulate growth in any way. The fact that today the permanence of Greece in the Euro Zone is under question undermines the very institution of the European Union<sup>9</sup>.

The Policy makers that decided the introduction of the single currency were aware that the system could operate properly only when integrated with the creation of a central government of the economic policy of the Euro Zone.

The European Union was created to unite peoples and solidarity must be the principle to which we Europeans must be inspired by. As stated in the pages of Il Sole-24 Ore on June 9, 2012 the former president of the European Parliament, Jerzy Burek and two thousand years ago it was said with pride: *civis romanus sum*. Today with pride we must say, I am a European citizen, before being Italian or French or German or Romanian. Because is there no contradiction in being a good European citizen and being a good Romanian citizen, being a good European citizen and a good Italian citizen. This is because there is no other place in the world like Europe where so many people can enjoy a very high standard of living. There is no other place in the world where

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<sup>9</sup> Today the spectrum of anti Europeismo seems far. The change of political rule in some European countries, Draghi's statements about the irreversible process of the Euro, the decision of the German Constitutional Court to give the green light to the ESM and the Barroso proposal to the European Parliament to give more power to the ECB, gave a twist to the European Union by allowing markets to regain trust in Eurolandia and curb the secessionist forces of the Euro.

people can rely on such a vast system of social protection, that allows people to look to the future with confidence, both in terms of health care, and in terms of programs for the most poor. There is no other place in the world where people are so strong and united in the defense of their fundamental rights.

We can and should be proud of the union and the values that underlie them

We have to prove that we have a long-term political vision. We must show that we believe in our political project and that we have concrete ideas and proposals to transform it into reality.

It seems that, the ideal charge, which inspired men like, Adenauer, Monnet, Schuman, De Gasperi, and their direct heirs Schmidt, Mitterrand, Kohl, Delors has faded out. An involution symbolically reflected in a constitution unnecessarily and harmfully plethoric to take into account the needs of the individual states.

The European ruling classes need to be convinced, and convince public opinion, that Europe is doomed to slide into insignificance if it does not find the reasons and the actions for a single project (with the risk of not becoming history, as affirmed by Romano Prodi), which requires a long view and maximum commitment<sup>10</sup>

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<sup>10</sup> A missed opportunity was certainly the Treaty that needed to adopt a Constitution for Europe (for a wider discussion: G. Maisto, *Progetto Costituzione Europea. Appunti di lavoro*, in *Rass. Trib Of Dir*, No. 7-8/2003, p. 124 et seq.). The work developed by the Presidium was ditched by the referendums in France and Holland in 2005. Of course a brake was put with those referendums but not a block to an irreversible process, leading to the creation of the United States of Europe. In fact, the journey continued with the Lisbon Treaty of 2007, ratified by all Members States, which has set itself the goal to meet the challenges ahead. From the announcement it reads, in fact, that "In 50 years Europe has changed, the world has changed. Today more than ever, in a globalized world in constant change, Europe is facing new challenges. Economic globalization, demographic change, climate change, energy supply, not to mention the new threats to security, these are the major issues with which the Europe of the twenty-first century must measure itself. Member States are no longer able to cope with all these new problems that know no borders alone. To cope with and respond to the concerns of citizens a collective effort at European level is needed. However, in order to face these challenges, Europe must modernize itself. It must have effective and consistent tools that are suitable not only for the functioning of a European Union recently switched from 15 to 27 Member States, but also to the rapid changes of today's world. The rules of common life, established by treaties, must therefore be renewed. And "This is the objective of the Treaty signed in Lisbon on 13

As Seneca said in his letters to Lucilius: continue in your progress and you will understand that, the things that are the most fearful, are those to fear the least.

We are all Europeans and soon everyone will be proud to say *civis europeus sum*.

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December 2007. Taking into account political, economic and social evolution and wanting to respond to the aspirations of the Europeans, the Heads of State and Government have agreed on new rules that discipline the flow and modalities of future EU action. The Lisbon Treaty will therefore adapt to the European institutions and their methods of work, to strengthen the democratic legitimacy of the Union and to consolidate the fundamental values that underlie them. The Lisbon Treaty is the result of negotiations by Member States within an Intergovernmental Conference, whose work was also helped by the Commission and the European Parliament. Before becoming valid, this Treaty shall be ratified by each of the 27 EU countries. It is up to them to define, in accordance with their respective constitutional requirements, how Member States are given, 1 January 2009 as deadline for the validation of the Treaty that is a few months before the election of the European Parliament “([http://europa.eu/lisbon\\_treaty/take/index\\_it.htm](http://europa.eu/lisbon_treaty/take/index_it.htm))



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## **Impact assessment of Public Relations in the Fiscal Control Management of the National Agency for Fiscal Administration**

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### **Abstract**

The present study examines the role of public relations as a socio-economic tool of persuasion and educating taxpayers of their civic responsibility to honor fair tax obligations. We propose solutions for improving and restructuring the fiscal control management by diversifying and expanding the range of the instrument constant communication/public relations and increasing their efficiency in the National Agency for Fiscal Administration, diversifying forms of public communication. The proposed work aims to fill a niche in tax audit work of taxpayers to be felt in practice equitable collection of taxes.

**Keywords:** managerial communication, fiscal control, efficiency of communication

### **Introduction**

The radical transformation of the relationship between state and individual that actually occur in Romania involves changing the manifestation circumstances of human personality and training it in achieving the social mission targeting by the entities. The complexity of these transformations drives the imperative to adapt the various

institutional structures adequately to the transition period exigencies: both people and institutions feel - as an urgent necessity for survival, adaptation and achieve the affirmation objective - the necessity to acquire the capacity and availability which contributes not only to overcome the difficulties, but also to awareness in assuming the civic responsibility, followed by involvement in managing the social-economic transformations.

Thus, in the extensive transformation and restructuring process which the Romanian economy is crossing, the managerial activity has the fundamental role in public institutions, which must be improved effectively.

Therefore, having many advantages, Public Relations (PR) - as a management tool - become a significant strategic resource for maintaining and enhancing economic performance.

### **Materials and Methods**

The conducted study is based on informal research, whose results can be used only for description and not for prediction, as well as formal, qualitative and quantitative, which allow a statistical analysis. For ANAF, external publics are represented by almost the entire Romanian society, starting with young people that will become partners in the fiscal act and continuing with all the other taxpayers, including pensioners. It is obvious that for the tax administration, the target public consists of active taxpayers. The direct relationship with them creates and influences in the highest degree the institutional image. One of the primary objectives of ANAF is to provide good quality services to taxpayers, to facilitate the revenue collection act, but also to change the taxpayer's mentality regarding voluntary compliance. In ANAF's strategic demarches to improve the taxpayer-civil relation, important and decisive steps could not have been made without a research, a diagnosis based on scientific foundations. Therefore, in the action "ANAF at your disposal," initiated by specialists from the General Directorate of Taxes and Contributions Management in the Public Finance Administrations in Bucharest, the city with the greatest number of taxpayers in the country, wanted to obtain a more suggestive image of what happens at the counters managed by IRS.

Specialists from the communication and PR structure have done this survey, in strict compliance with the requirements of such a rigorous science-based action. Moreover, such a research is a pioneering

action, being the first and only attempt of this kind that has been carried out in the Ministry of Public Finance of Romania. EU, through the European Commission in Romania, and the Romanian Government through the Ministry of Public Finance performed, in the 13-22 September, 2011, a survey on the image and quality of ANAF.

The survey was conducted with European funding, by the Center for Urban and Regional Sociology (CURS) at ANAF order under the PHARE program RO2002/586.03.04.11. *"Increasing tax collection level by improving taxpayers' voluntary compliance, by building the internal capacity of the Ministry of Public Finance to develop, with their own forces, information and communication campaigns for taxpayers, as well as a modern activity of taxpayer assistance"*, conducted with the help of MAXWELL STAMP PLC company in the UK. The survey included a sample of 2,300 people, nationally representative for taxpayers, individuals and legal entities, which are directly in contact with the fiscal administrations. The sampling error was + / - 2%.

At the end of the interview, 13% of the respondents made further comments on tax administration services. These observations are as follows: to have available brochures, statements should be submitted quarterly, staff should be supplemented during the holidays, working hours with the public to be from 7.00 to 20.00, younger officers are better trained, familiarizing population with the Internet, higher advertising regarding information, legislation and taxation; to exist different offices for individuals and legal entities, payments made by credit card, termination of the system under which certain persons are preferred, to be able to submit documents after 11.00, to submit documents also on the Internet, there should be an office for sick persons.

The indicated problems can be overcome, according to the taxpayers, by reducing the number of documents and/or simplify the forms (52%); hiring more people (32%) and open more counters (36%). The results show largely that a reorganization of the ANAF's activity is desired; at the same time being clearly expressed the option to simplify the procedures based on documents ([www.anaf.ro](http://www.anaf.ro)).

### **Literature review**

The nineties of the twentieth century have been remarked by researchers interest, given the problem of social processes correlated with taxation of individuals. It is considered that this type of tax was subject to the most reform. The papers that were focused on this issue can be classified into several categories:

- The researches regarding social causes and consequences of applying the income tax rate; papers devoted to the income taxation analysis of various social groups.

- Papers in which is conducted a public opinion analysis related to income tax. Among the most relevant research in this area we can distinguish the study of John Campbell and Michael Allen [1], which examines the causes of tax rate changes. The conclusions reached by the authors of the study show that the specific of the progressive taxation character is largely determined by the macroeconomic conditions (unemployment and inflation). Other variables - such as organizational capabilities of social classes or political conditions - have an influence on the characteristics of progressive taxation, but, in a lesser extent.

- In the research conducted by D. Jacobs and R. Helms [3] was based the idea regarding the linkage between the extent of movements in supporting human rights and the redistributive fiscal policy expansion. The income tax reform in the context of poverty was examined in a paper of researchers H.Chernick and A.Reschovsky [2], generating echoes and exhortations for "its revaluation". Broadly, it is relevant that, at that time, a great importance was given to the public opinion study, examining the perception mode regarding tax administration activities.

Thus, in one of these studies it is established that after examining the responses of taxpayers to the proposed questionnaire regarding the tax scale, the respondents' demonstrated insufficient knowledge of the problems related to the tax system and, generally, inconsistencies in responses. In a subsequent paper, also based on the study of the population's attitude towards taxation issues, this time in relation to political options, was indicated that "the support for reducing taxes has a greater affect on the voting option when the political decision is based on collective consequences of this reduction".

Marc Leroy [4] has defined a set of principles to help organizations maintain a favorable public opinion, among which we mention two of great importance:

- Economic and social stability of any organization depends on the attitudes and opinions of publics within all environments in which the organization operates.

- The communication management of an organization is essential to ensure a fair and appropriate feedback from audiences both internal and external in order to ensure the organization's adjustment and adaptation to the changes necessary for its existence.

### **Results and Discussion**

As a *result of the survey conducted in 2011*, the following elements have been identified ([www.anaf.ro](http://www.anaf.ro)): numerous and complicated forms - 44.4% of respondents; too many roads - 37.8%; waiting too much - 30.2%; frequently sent from one counter to another - 5.9%; information is not in a language that I understand - 24.1%; the staff does not recognize it makes a mistake - 23.8%; time intervals of the program – are inconvenient - 21.5%; I am required to provide unnecessary documentation - 18.6%; giving small gifts facilitates the process - 17.1%; the personnel is impolite - 15.7%; the total number of hours when AF is opened is inconvenient – 7.6%; the staff does not provide all the necessary information – 5.6%; the survey proved that almost 50% of the respondents had to appeal to more than one officer to solve a problem.

In Table no. 1 are presented the comparative results of the surveys performed in 2005 and 2011.

"Officers are not polite" is not a significant problem. If the survey of year 2005 showed the presence of only 5% of the respondents who reported this fact, the survey performed in year 2011 showed that the share of unsatisfied respondents increased up to 15.7%. "Do not explain" is a matter of "low intensity" according to the survey of year 2005, while in the 2011 survey, the share of respondents who consider the presence of this problem important is 24.1%.

**Table no. 1.** Comparing the results of public surveys from 2005 and 2011, regarding the assessment of ANAF's services

Elements of reproach	2005	2011
	Share %	Share %
1. Waiting too long to the counter	25	30,20
2. Too many complicated documents	40	44,40
3. Inappropriate work program for the public	17	7,6
4. The information is not in a language that can be understood	14	24,10
5. "Walking" from one counter to another	20	27,90
6. Too many roads	27	37,80
7. I am required to provide unnecessary documents	-	18,60
8. Without a bribe, how small, nothing is solved	4	17,10
9. Officials do not admit their guilt	11	23,80
10. Officials' lack of politeness	5	15,70
11. I do not have objections	26	4,9
12. I cannot pronounce	3	-

"Officials do not admit when they make mistakes", in the 2005 survey, the share of respondents that affirmed this was 11%, while in the survey of year 2011, the share of "unsatisfied" reached 23.8%.

"Without a gift you do not solve anything", this response does not represent a significant problem; only 4% of the total respondents from 2005 identified it as a difficulty in relation with AFP, while in the survey from 2011, the share of people who identified this was 17.1%, which allows us to conclude an increase of the corruption among civil servants in the fiscal control field.

"Too many roads", is a significant problem, being accused by 27% of respondents and indicated as the only problem in the relation with AFP (2005), while in the survey from year 2011, this difficulty was indicated by 34% of the respondents. "Too many roads" correlates with "too many documents", which confirms that AFP activities continue to be bureaucratic.

"From one counter to another" seems to be a problem of moderate intensity, but only in relation to other issues. "From one counter to another" is associated with "Too many documents".

"Working hours with the public" is a significant problem, being indicated by 17% of the respondents in 2005. At the same time, it was considered the only problem encountered by 10% of those who indicated this single difficulty in 2005. In the survey for the year 2011, only 7.6% of the respondents consider ANAF's working hours a problem, which confirms that in recent years, an effort was made to create a working regime of AFP more comfortable for taxpayers.

In the survey of 2011, about half of the respondents with secondary or primary education and half of those with higher education want the documents simplification. The weak differentiation according to education, but also according to other variables, shows that this is a general problem that all taxpayers confront with. The "Too many documents" option is equally associated with "too many roads", "waiting too much" and "going from one counter to another" by two thirds of the respondents. It can be deduced from this that the "too many documents" option has the highest probability to constitute the fact that too many roads are made, that people have to wait too long at the counter and that they are often sent from a counter to another when they come to the AFP headquarters. The fact that the response "too many documents" is closely associated with "too many roads" shows that in a given extent, the problem of documents is also related to the unawareness of taxpayers regarding the necessary documents that need to be submitted to ANAF.

In general, if we compare the results of public surveys in 2005 and 2011, evaluated on AFP's activities, we observe that the share of reproaches to most of the researched questions increased. We believe that this situation has occurred because of the economic crisis of 2009-2011, which required ANAF to reduce a considerable part of the staff, including spokespersons and PR, but broadening their skills and level of responsibility of those left in office.



**Table no. 2.** Increasing the performance degree of ANAF's tax inspections, 2008-2010

Indicators	2008	2009	2010	Percentage variation	
				2010/2008	2010/2009
Number of fiscal controls	127.934	112.170	109.286	-14,60%	-2,60%
Supplementary obligations determined, (mil lei)	4.705,40	6.082	8.728	+85,5%	+43,50%
Precautionary measures (mil lei)	628,80	1.948,10	2.642,30	+320,20 %	+35,60%
Confiscations (mil. lei)	36	96,90	122,30	+239,70 %	+26,20%
Expenses with ANAF Personnel at one million lei collected (mil lei)	12,63	10,85	9,26	-14,60%	-26,60%

ANAF collaboration with tax administrations and European bodies in order to return and fight cross-border fraud, to improve and perfect techniques, control methods and skills, has allowed ANAF to perform multilateral controls of the Romanian entities that were involved in fraud chains. This fact is confirmed by reducing the number of tax inspections, increasing their quality and reducing the maintenance costs of ANAF personnel, hired to collect taxes.

According to the mathematical model developed by the author on processes of using advertising resources in competitive conditions as a component part of PR proved that exceeding the optimal level of advertising expenses awakens repulsion from consumers, rejects potential customers and also they are not economically justified.

### Conclusion

The effective communication component of the public institution management is possible only in the conditions of human society democratization, when the public interest information acquire a

public status. The PR system can provide organizational opening against the social environment in which it operates. PR does not solve all the problems related to the interaction between public authorities and the public, but being recognized as an instrument of public management, they contribute to public image, taking into account the public opinion and the needs of the human society.

It is demonstrated that the process of change in society is associated with certain social technologies designed to change the social status of public institution. In the context of these changes, PR relies more on the public relations component. In this paper we study the public opinion on the quality of ANAF services based on the public survey, which showed that reducing the number of tax inspectors, including those who are concerned with PR, lead to the reducing of the quality of tax services. Advertising tax audit activities should be diversified, it should alternate, time limited, as to take account of the potential customers specific, and the advertising frequency should be optimal. Overcoming the optimal level of advertising forms awakens repulsion from consumers, rejecting potential customers, being economically unjustified.

The research has shown that during the economic crisis, the number of staff hired as spokesman for ANAF was reduced, which is detrimental to the fiscal control activities. If we consider the fact that the purpose of PR within tax authorities is to strengthen fiscal discipline and increase public confidence in tax administration, the implementation of PR becomes extremely important. As a result of personnel reduction of tax authorities, first, the effects of management and educational activities are reduced, which was confirmed by the comparison of the public survey results on ANAF services.

Based on the investigations carried out and the formulated conclusions, some recommendations are proposed which will help increase the efficiency of the PR services in tax structures:

- It is appropriate that PR specialists acknowledge the need to develop innovative vision of personal communication, determining its role in the efficient execution of professional duties, to improve their ability to be good communicators and tax professionals: the ability to combine knowledge of tax legislation with the PR principles and methods, in order to understand taxpayers, to meet their expectations, to carefully guide their aspirations and behavior.

- It is appropriate that the management, managers and PR specialists in Tax Service have to discuss the issue of the taxpayer's communication process, to initiate and to make decisions, instructions, regulations, instructions for perfecting taxpayer's communication management. The normative acts issued by ANAF in this direction, such as external communication Charter of ANAF, Management Charter of ANAF, are very general and do not contribute enough as to train these skills.

- We cannot assess the economic impact of PR profession and those who work in this field without setting their performance criteria, in accordance with institutional strategic objectives, but also with socio-economic environment. The author comes up with a proposal for the implementation of performance evaluation indicators of fiscal control management at different stages, including the PR. This will help create an open and honest organizational culture, to breaking rigid and inertial patterns of the inter-human relations that currently exist in ANAF, improving the attitude towards taxpayers and, ultimately, the social awareness of the need of every taxpayer, to contribute to the achievement of social programs by transferring the taxes on time.

- Solving as soon as possible and constructive the problems of defective PR relates to the use of manipulative conviction by educating persuasive communication. We welcome the proposal to fit the civil society in the process of solving potential conflicts between PR professional and taxpayers, the civil society would act as an impartial "referee" in the objective resolution of conflicts.

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**Is Self-reliance possible?  
An Investigation into the Romanian Sugar Industry's  
Ability to cover domestic Consumption**

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**Abstract**

This study investigates the degree to which Romania is able to produce the quantity of sugar necessary for domestic consumption. The results of our research can be used to improve the situation of the sugar industry of Romania, which is difficult at the moment: Romania has become the largest sugar importer of South-Eastern Europe, while it used to be an exporter. We have shown that Romania is fully able to meet its domestic consumption requirements, provided that sugar beet cultivators are encouraged to produce this plant, that the modernization of Romanian factories is completed and that there are no negative effects of EU policies on beet producers and on the Romanian sugar industry. The study was carried out by using a variety of sources, like specialized publications, EU and Romanian regulations, research studies and internet sources, as well as our own calculations.

**Keywords:** sugar industry, domestic consumption, scenarios, costs

**Introduction**

The aim of this study is to evaluate the degree to which Romania is able to meet the needs of its domestic consumption by its domestic production, with a view to producing recommendations that could be

used to improve the present situation. Currently, Romania is the largest sugar importer in its region, although it used to export sugar. The overall sugar beet-cultivated area, the sugar production and the number of sugar factories have decreased.

Our claim is that Romania is fully able to cover its domestic consumption needs, provided that certain conditions are fulfilled, which are outlined in our article.

The reference value for the necessary quantity of sugar was estimated at an annual 20 kilogram's per capita, which means an overall 450,000 tone per year. The former value, 20 kilogram's, is the average sugar quantity consumed by the Romanians in the last years (cf. *Statistic Year Book of Romania*), which was multiplied by the average number of Romanians in the same period.

### **Material and Methods**

The study is based on evidence provided by other research studies, EU and Romanian regulations, specialized publications, as well as by internet sites. In order to answer the research question, we have consulted and analyzed published sources and we also did our own calculations. In doing so, we have encountered difficulties related to differences in data published by various sources.

### **Literature review**

One of the raw materials for sugar production, sugar beet, is cultivated in Romania. Sugar is obtained from three sources: date palms, sugar cane and sugar beet ([www.food-info.net](http://www.food-info.net)<sup>1</sup>). The latter is cultivated in some Romanian regions; therefore we can assert that our country does have the raw material for sugar production.

However, one could wonder whether Romania does possess the natural conditions necessary for sugar beet cultivation. This is important because, if it does not, beet would be cultivated only in small quantities, probably just for individual farmers' use, and crops would not be of the highest quality, as they would not benefit from the best pedo-climatic conditions.

The latter regard two aspects: soil and climate. According to the information published on the Romanian agricultural portal, [www.agra.ro](http://www.agra.ro), soils should be fertile, rich in humus, deep and well-

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<sup>1</sup> [www.food-info.net](http://www.food-info.net) is managed by the Wageningen University in the Netherlands.

structured; also, they should have high water retainment capability. As for the climate, the temperate continental one is the best for sugar beet cultivation<sup>2</sup>.

Romania has four regions where beet is cultivated: the center and Eastern parts, the Western one and the Southern one. The former three meet the beet cultivation requirements, while the latter does so only under certain conditions. Thus, the center and Eastern areas have a temperate continental climate, as well as chernozem and brown-red soils, which have the above-mentioned characteristics. The Western region has a warmer climate, but still within satisfactory limits, and its soils belong to the chernozem and clay-sand groups. On the other hand, as mentioned above, the Southern part needs to be subjected to certain conditions, because it does not fulfill the above-mentioned requirements to a satisfying degree. Firstly, temperatures can vary highly from year to year and from day to night. Secondly, they are higher than in the other regions, which can be detrimental, as sugar is no longer accumulated in beet roots if the temperature exceeds 26°C. Finally, rainfall can sometimes be very low; there have been years with 180-230 days without rain. Lack of moisture can lead to biological and biochemical transformations of the plant, which has negative consequences on sugar beet quality. Therefore, the Southern region is considered a beet cultivation area only with the following reservations: there should not be high temperature variations, the land should be thoroughly irrigated and only areas with chernozem soils should be used.

The second problem that needs to be discussed is Romania's ability to process the sugar beet crops and produce the sugar needed for domestic consumption.

At first sight, the situation does not appear very promising. In 1991, there were 33 sugar factories in Romania, but in 2011 only 8 still functioned. They were: S.C. AGRANA România, S.C. Zahărul Liești (Lemarco), S.C. Zahărul Corabia, S.C. Zahăr Oradea, S.C. Zahăr Luduș, S.C. Zahăr Bod, S.C. Zahărul Călărași, S.C. Marr Sugar Urziceni. However, taking into account their production capacities, which you will find in Table 1 below, it is clear that they could cover and even exceed the quantity Romania needs, i.e. 450,000 tonnes. Thus, their total daily capacity is 27,000 tonnes a day, which would mean almost 10m tonnes a year (360 working days).

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<sup>2</sup> [www.agra.ro](http://www.agra.ro) is a project of IBD/GTZ and the "Haralamb Vasiliu" Agricultural High School in Podu Iloae, Iasi County. IBD/GTZ is a programme of the German Ministry for Economic Cooperation and Development, meant to support Romania's economic conformity with the EU. It is carried out together with the Romanian Chamber of Commerce and Industry and the German Society for Technical Cooperation (GTZ).

**Table 1:** Romanian sugar factories functioning in 2011

No.	Name	Production capacity (tones/24 hs)
1	ZAHĂRUL BOD	2,000
2	ZAHĂR CORABIA SA	3,000
3	ZAHĂRUL LIEȘTI SA	1,000
4	ZAHĂRUL ORADEA SA	3,000
5	MARR SUGAR URZICENI	4,000
6	ZAHĂRUL LUDUȘ	3,000
7	AGRANA ROMÂNIA - ROMAN	8,000
8	S.C. ZAHĂRUL CĂLĂRAȘI	3,000

*Source:* Romanian Ministry for Agriculture and Rural Development

There is yet another problem related to Romanian factories: the quality of the production equipment they use. The factories that were set up after 1970 had been provided with equipment produced in Romania, which in our days has become outworn and technologically outdated. Moreover, the average extraction capacity of the equipment used by Romanian factories is four times lower than the European average.

This situation has changed, to a certain degree. Thus, the eight factories mentioned above have been privatized and new equipment has been installed. As an example, we can cite a statement by Petru Gavriș, a counselor with the Romanian Ministry for Agriculture. The statement was made in March 2005 to *Rompres* and cited by *Jurnalul de Botoșani și Dorohi* ([www.jurnalulbtd.ro](http://www.jurnalulbtd.ro)). Gavriș declared that the beet-processing factories at Oradea, Luduș, Bod and Roman had made significant investment in the modernization of the technology they used. Moreover, between 2004 and 2006 more than 10m euros were available for investment in the sugar producing industry; this funding was provided by the European Union, by means of the SAPARD Program, according to information published on [www.finantare.ro](http://www.finantare.ro). A further possible encouragement for the replacing of old technology is represented by the changes brought about by the previously mentioned state subvention for beet cultivators and pre-contracting system. If cultivators are more interested in producing and factories increase their production, then there is a high probability that these businesses become more interested in and able to modernize their equipment.

To conclude on this point, Romania does have the production capacities necessary to process sugar beet, although further

improvements need to be made in the modernization of the technology used, especially to increase sugar extraction efficiency. Steps have already been taken in that direction, but the process needs to be completed.

The sugar production necessary for domestic consumption benefits from EU subsidies, in the production quota system. Robu et al. (2006) explain that, according to this system, the EU grants subsidies for a certain quantity of sugar, which is calculated function of the sugar production in the last five years before EU accession. Although, in Romania's case, those five years were very weak, the quota was higher than expected, i.e. almost 440,000 tones. The authors mentioned above also state that this is explained by the choice of the reference period, which was 1998-2002, when the sugar industry performed better. If we remember that the necessary quantity for Romanian consumption is estimated at 450,000 tones, it can be seen that a very large part of this quantity will be produced with EU subsidies, which may be beneficial for our concern.

Further research needs to be made, however, into two directions. First of all, the 440,000 tones which are subsidized are not all for beet sugar. Instead, according to data published on the Ministry of Agriculture site, the quota for white sugar obtained from beet is only 109,164 tones, whereas 329,636 tones will come from raw cane sugar, imported in a preferential system (the rest is for a sweetener made out of corn). Consequently, research is needed into how this will affect local beet producers and ultimately, the entire industry.

The second direction or problem is that the EU has initiated, in 2006, a reform of the sugar industry which is meant to ensure it long-term prospects. Among its consequences, though, there is the decrease of the price beet cultivators receive for their crops. This information is provided by Robu et al., who state that the decrease was from 34 euros to 32.9 euros in 2006-2007, while starting with 2009/2010, the price is 26.3 euros.

The problem of local beet producers is important because, as it will be shown in the next section, Romania is able to ensure the necessary quantity for domestic consumption out of its own beet crops, provided that certain conditions are met.

Common practices (Crețu R.F. and Crețu R.C., 2011) of the ecologic agriculture comprise the following: crops rotation as a requirement for the efficient use of the farm's resources; extremely



strict limits regarding the use of chemical synthesis pesticides and chemical fertilizers, antibiotics for animals, food additives and other auxiliary substances used for processing agricultural products; forbidding the use of genetically modified bodies; capitalizing the existing resources, such as using the muck from animals and the roughage produced on the farm as fertilizer.

### **Results and Discussion**

We have constructed several scenarios to examine what ways there may be to ensure the quantity of sugar necessary for consumption in Romania, by processing the sugar beet produced here. In this section we have included a brief description of the methods used in developing them, the hypotheses upon which we have based them, the scenarios themselves, together with an evaluation of the costs involved in domestic consumption coverage, as well as a prediction on what consequences there will be for various stakeholders.

These scenarios have been based on an analysis of the dynamics of the beet-cultivated areas, of overall production, of per-hectare and regional production, as well as of the 2010-2011 sugar production. We have also taken into account the investment and equipment modernization done in the sugar industry in the last years after 2000, as well the specialists in this field.

Our claim, that the necessary quantity can be domestically produced, is based on the following hypotheses:

1. All the commercial agreements signed by Romania will be reconsidered;
2. The beet and sugar price will be guaranteed, so as to encourage farmers and beet processors to cultivate and process it;
3. Average sugar production per hectare is the average of the last 10 years;
4. The extraction efficiency of sugar from beet is the maximum value of the average annual efficiency;
5. Consumer price of sugar will not increase.
6. Annual consumption for all scenarios is 450,000 tones, which ensures 20 kilogram's per capita.

Here are the scenarios, which describe three possible situations: domestic consumption requirements are met in a percentage of 50%, 75% and 100 %. As can be seen from Table 2, for each of them, the

cultivated area and overall production increase according to the degree of domestic consumption coverage.

**Table 2:** Suggested scenarios

	<b>Scenario I (50%)</b>	<b>Scenario II (75%)</b>	<b>Scenario III (100%)</b>
Cultivated area (thousands of hectares)	102	186	248
Average production (kg/ha)	20	20	20
Overall production (thousands of tones)	2045	3713	4950
Extraction efficiency (%)	11	11	11
Sugar processed in Romania (thousands of tones)	373	411.5	450
- beet sugar (thousands of tones)	225	337.5	450
- raw sugar processed in Romania (thousands of tones)	148	74	0
Imported refined sugar (thousands of tones)	77	38.5	0
Domestic consumption (thousands of tones)	450	450	450
Coverage of domestic consumption need (%)	50	75	100

*Source:* Own calculations

We have also estimated the costs involved in meeting the requirements of domestic consumption. In doing this, we have taken into account, on the one hand, the prices offered by the factories for the sugar beet and the costs of producing the beet; on the other, the prices of imported refined sugar and the prices of beet, domestically-produced, sugar.

From Table 3 it can be seen that the costs of subsidizing the sugar beet and the sugar production increase with the growth of the coverage of the domestic consumption need. In addition, the subsidizing costs for beet cultivation have the largest portion of the costs for this

coverage. Finally, overall costs go up from 95m euros in the first scenario to 215m euros in the third one.

**Table 3:** Costs of domestic consumption coverage

		<b>Scenario I</b>	<b>Scenario II</b>	<b>Scenario III</b>
Sugar beet production cost	euro/tonne	49	49	49
Ex-works sugar beet price	euro/tonne	21	21	21
Sugar beet cultivation subsidizing costs	euros (thousands)	57,273	103,950	138,600
Sugar price (domestic)	euro/tonne	423	423	423
Imported sugar price (CIF)	euro/tonne	252	252	252
Sugar subsidizing costs	euros (thousands)	38,475	57,713	76,950
Total costs of domestic consumption coverage	euros (thousands)	95,748	161,663	215,550

*Source:* Own calculations

The three scenarios may have consequences on the following categories of stakeholders: farmers, sugar factories, traders, consumers and tax payers. Thus, we predict that farmers' revenues will increase in all the three cases, because the sugar beet price will rise practically by 100%; thus, they will be interested in investing in its cultivation. As for sugar factories, the sugar price will be guaranteed for them, too, but, at the same time, they will lose the revenues resulting from processing imported raw sugar. Traders' profit from dealing in sugar will decrease

in all three cases. Consumers, on the other hand, will not be affected, because the consumer price of sugar will not change.

### **Conclusions**

In this study, we have shown that Romania is fully able to produce the quantity of sugar needed for domestic consumption, provided that certain conditions are fulfilled. Thus, our country has the raw material, sugar beet, as well as the pedo-climatic conditions necessary for the cultivation of the latter.

In addition, Romania has enough sugar producing units, able to produce the necessary quantity. Although production equipment used to be too old, modernization has begun. It is necessary, however, that this process be completed. Romania also benefits from EU subsidies for the production of a quantity of sugar covering the one we need to a large degree.

The findings of this study can be used to improve the current situation of the sugar industry in Romania. They may also serve as an argument against the EU decision to grant a higher subsidized quota for preferentially imported raw sugar.

To facilitate this, further research is necessary in the following directions: (a) assessing the effect of EU policies (quota distribution and sugar industry reform) on beet producers and on the entire industry; (b) evaluating the degree to which it is preferable to rely mainly on either domestic beet production or on imported raw sugar for the production of white sugar.

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## **Customer Satisfaction Measurement: an empirical Study of the Need – Gap Analysis in the Service Industry**

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### **Abstract**

The Need-Gap analysis determines deviations between actual and expected quality, taking corrective action. The analysis indicates the presence of multi-dimensional aspects regarding a complaining behavior. Critical analysis of results helps to evolve service strategies in response to customer needs.

**Keywords:** Customer's complaints, service strategies, service delivery, enhancing customer satisfaction

### **Introduction**

Customer complaint is a very important factor for any airline. In the services, human behavior plays a very important role to minimize the customer complaint. There are two types of complaints: viz controlled and uncontrolled. There are many factors that affect passengers such as: flight delays, misbehavior by staff etc. Whereas, there are so many situations which can't be controlled such as, weather problems, technical fault, etc. Although these situations are not in control but can reduce the complaining behavior which depends on "how situation is handled by airline staff". If a staff is not trained to handle a situation, then it is not acceptable because it is the airline's fault. If the staff misbehaves with the passenger or due to lack of staff knowledge, wrong information has passed to the passenger. Such are the complaints which can be minimized and controlled. However, genuine customers' complaint can enhance the service quality of airlines. Some airlines have customer feedback form for rating of the services rendered

by them and feedback helps the airline industry in identifying its strengths and weaknesses.

### **Customer complaint behavior**

It is the tendency of every human that whatever is promised, it must be given to them; if there is any deviation, will attract complaint. Whenever a passenger book ticket for any airline, at the time of booking he/she is informed about the services which will be rendered to him/her, thereon. If they will not receive the promise services, at the promised quality, this will lead to complaint. There can be two categories of customer complaint: controlled and uncontrolled.

**Controlled customer complaints** - are attracted by staff error or staff behavior. These things are in the hands of the airline people. We are explaining some common customer complaints.

- **Flight related problems:** Such problems lead to customer complaint when there is planned delay or cancellation of flights and passengers are not informed in advance. It is dissatisfying if change is planned or unplanned and the passengers are not informed. Even if passengers are informed about schedule change, it is complaining for customers having onward flights for different destinations while alternative arrangements were not done.
- **Fare related problems** means a discrepancy in fare related issues, such as incorrect fare information, extra charges, wrong availability status etc.
- **Boarding discrepancies:** At the time of boarding, there may be discrepancy such as duplicate seat numbers, wrong boarding pass to passengers, other flight passenger etc.
- **DNB/DNG\* due to over sale:** Over sale in the flights is a common practice of airlines. Due to this, passengers who are having confirmed ticket for the flight are denied to board the flight. Likewise, if passenger is having higher class ticket but due to over sale in higher class, passenger is permitted in lower class.
- **Reservation/Ticketing:** Any mistake at the time of ticketing by travel agents or airline staff in terms of date of travel, name mismatch etc. leads to waiting in queue for a long time for obtaining tickets.
- **Baggage mishandling** comes because the baggage's missing or damaged on arrival. Claim settlement is not done properly for missing or damaged baggage.

- **Refunds of tickets:** If ticket is unused partially or fully and refund is not processed. That means there are problems in airline procedure for obtaining refund for unused tickets.
- **Excess Baggage charge:** If excess baggage charged wrongly due to non updating of current procedure, staff error whereas passenger was allowed to carry that much weight.
- **Staff attitude:** Staff attitude plays a very important role in complaint as well as a compliment. If staff attitude is positive, that can convert a complaint into compliment and vice versa.
- **Advertising:** If any airline do wrong advertising for their services, will directly lead to complaint.
- **In flight services:** If services are rendered in flight not up to the standard and behavior of cabin crew is also rude and unhelpful, will lead to complaint.
- **Cargo:** If a person books urgent cargo with the airline and it is misplaced and not delivered on time due to staff error.
- **Tour operation:** Nowadays, airlines operates tours (Air tickets, hotel reservations, sight seen, taxi etc.) even if there is no problem with air travel, attracts complain if there is any problem in full tour package, because it was sold by the airline.
- **Airline Security:** Generally, airline security people are not trained in customer handling, therefore they behave in ordinary way with the passengers or unnecessarily tease passengers which attract complaint.

**Uncontrolled customer complaints:** There are so many problems which can't be controlled by the airline:

- **Flight related problems:** When there is unplanned delay or cancellation of flights and passengers are not informed in advance due to weather problems, such as fog, rain, thunderstorm etc. and if there is any schedule change due to technical grounding of the aircraft.
- **Fare related problems:** When there is any discrepancy in fare related issues due to misconception of passenger, such as heard wrong information from unauthorized persons.
- **Excess Baggage charge:** Passenger is allowed to carry check-in baggage, as per free baggage allowance mentioned in his ticket; if he carries more, the excess will be charged thereafter, if passenger makes a complain regarding excess baggage.
- **Airline Security**



- **Cargo:** If a person books urgent cargo with the airline and it is misplaced due to wrong address of consignee which is given by the consignor.

### **Research Methodology**

The Need – Gap Analysis shows the gap between the current performance and the expected performance (Rummler, 1987). There are different ways to determine the need gap. There are various methods like interviews, documents, surveys, observations or focus groups (Wexley and Latham, 1981). Analyzing and identifying the gap that may exist between what the airlines is supposed to be doing and what it is doing, points toward areas for complaint and scope of improvement. In this regard, Quality function deployment (QFD), one of the structured methodologies that translate customer needs into specific quality development, displays and achieves effectiveness (Chan and Wu, 2005). QFD bridges the gap between what the customer wants and how the airline can render high quality services to reduce customer complaint. It is a powerful analytical framework called the ‘House of Quality’ (HOQ) matrix, because of its shape, with various ‘rooms’ containing the results of research and analysis on customer groups and competitors (Walker, 2002). It has also been applied to service industries recently (Ermer and Kniper, 1998) and the application in airline industry can largely reduce the customer complaint behavior. Understanding customer needs means to organize the strategy to develop service quality in achieving customer satisfaction.

The exploratory research consisted in a survey that was applied to 100 customers. The questionnaire method has been used for primary data collection. Responses from 100 customers were taken to study the complaining behavior of customers at the airport. Concerning sampling as it is intended to get data related to complaint issues, it was key to have responses from people who have had a bad experience, this means, they have been dissatisfied with the services. For the preparation of 5 point Likert scale, the studies of Cadotte and Turgeon (1988), Sue and Bowen (2001), Wildes and Seo (2001), Heung and Lam (2003), Lam and Tang (2003), De Franco et al. (2005), Sujithamrak and Lam (2005), Yang (2005), Yüksel et al. (2006), Kim and Lynn (2007), have been useful. Pilot test stage of the questionnaire, which was the data gathering instrument, was tested on 20 airline customers. Cronbach alpha coefficient of the data analysis after the pilot test stage was calculated as 0.617. In the light of the results of the pilot test stage, the questionnaire was implemented. It was observed that 80 percent from

the customers were complainers and 20 percent were non complainers. The data gathered have been analyzed with SPSS 17.0 for Windows program.

### Data Analysis

The data from questionnaire and analysis clearly indicate the factors responsible for customer complaint. The pilot study and the Cronbach Alpha value also validate the same.

**Table no. 1:** Percentages of respondents for complaints

Column1	Column2	Strongly Agreed	Agreed	Average	Disagreed	Strongly disagreed
S.No.	Parameters					
1	On Time Performance	80	10	5	5	0
2	Cost Reduction	73	17	8	1	1
3	Security System	76	10	13	0	1
4	Booking/Ticketing	90	6	3	1	0
5	In-Flight Services	85	10	1	2	2
6	Air Traffic Control	81	12	2	4	1
7	Navigation	75	20	0	5	0
8	Check-In	96	3	1	0	0
9	Delay/Cancellation	94	5	1	0	0
10	Take-Off/Landing of Flight	79	8	8	5	0
11	Baggage Services	91	6	1	1	1
12	Meteorological system	70	20	8	1	1
13	Passenger facilities	97	3	0	0	0

For data analysis, to check validity and reliability Factor Analysis was used the Varimax Rotation. To check reliability of each factor, Cronbach Alpha was calculated.

**Table no. 2:** KMO and Bartlett's Test

Kaiser-Meyer-Olkin Measure of Sampling Adequacy.		.465
Bartlett's Test of Sphericity	Approx. Chi-Square	57.212
	Df	78
	Sig.	.963

**Table no. 3: Communalities**

	Initial	Extraction
OnTimePerformance	1.000	.481
CostReduction	1.000	.703
Securitysystem	1.000	.500
Booking	1.000	.546
InflightServices	1.000	.608
AirtrafficControl	1.000	.669
Navigation	1.000	.487
Checkin	1.000	.478
Delay	1.000	.578
TakeoffLanding	1.000	.714
Baggage	1.000	.526
Meterological	1.000	.707
Services	1.000	.622

*Extraction Method: Principal Component Analysis.*

Six Four factors resulted from the factor analysis. The loading values of the scales items in their respective factor went from 0.48 to 0.70. Regarding reliability, Alfa Cronbachs were not very high, ranging from 0.52 to 0.66. In relation to the total explained variance, this was only 57 percent. The analyze show that although complaints and complaint behaviors are studied in the same study, the investigations of the relation between them are very limited. Complaint behaviors increase with an increase in customer complaint. The relation between complaint and complaint behaviors have been defined with the Pearson correlation analysis. Hence the hypothesis of the study can be stated as:

**H1:** There is a positive correlation between customer complaints and complaint behaviors.

The values gathered from Kaiser-Meyer-Olkin and Bartlett's Test (KMO = 0.47;  $p = 0.000$ ) show the adequacy of sampling and applicability of factor analysis. Cronbach's alpha coefficients relating to customer complaint and complaint behavior scale factors have been calculated as over 0.60. Pearson correlation coefficients relating to factors between complaint and complaint behaviors have been given in Table no. 3. According to this, all the correlation coefficients between the factors of customer complaints and complaint behaviors have been found significant ( $p < 0.001$ ). The inspection of correlation coefficients

shows that there is a positive correlation between all the variables. It is seen that these findings support H1, the hypothesis of the study.

### **Recommendations and Conclusion**

When there are flight related problems, true information must be given to passengers, as well as alternative arrangements should be made at least for onward connecting passengers. If there are planned cancellations or delay, then passengers must be informed well in time, so that they can report accordingly. Although, DNB and DNG are very common practices in the airline industry to maximize revenue, notwithstanding these practices should be minimized and utmost care must be given to the privilege members of the airline. Airline must have their own employees instead of outsourcing, to facilitate their passengers in a better way. Staff must be provided with soft skill trainings, to handle controlled, as well as uncontrolled problems. Generally, baggage handling is done by the loaders and they are not educated properly; therefore, it must be monitored by the airline staff. Passengers must be educated for their free baggage allowance and security procedure to avoid unnecessary discussions. These corrective measures can be accepted to minimize the customer complaints.

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## **Considerations on the Structure and Particularities of Tax Revenues in the 2000s Romania**

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### **Abstract**

The fiscal policy has the purpose to delimit broadly the volume and the structure of optimum tax revenues, in order to maintain a financial equilibrium. Likewise, the fiscal policy should fit within the national economic and macro-financial objectives. From this perspective, fiscal policy inhibits certain activities through the increase of tax burden, while stimulating others through tax incentives. Likewise, the type and number of channels that contribute to the consolidated budget are highly relevant for the definition of the state fiscal policy.

**Keywords:** tax revenues, fiscal policy, public resources

### **Introduction**

The Romanian fiscal policy over the last decade (the analysis period proposed in the present paper) is characterised by the completion of two main stages: the first stage (between 2000 and 2007), characterised by a stabilization tendency of the main economic and financial macro-indicators, and a second stage (between 2008 and 2010), characterised by an economic and financial crisis. The international economic and financial crisis affected Romania as well, causing its economic recession. Likewise, the fact that Romania became a member state of the EU in 2007, influenced the Romanian fiscal policies before and after this date. All these aspects will be approached in the present study.

### Material and Methods

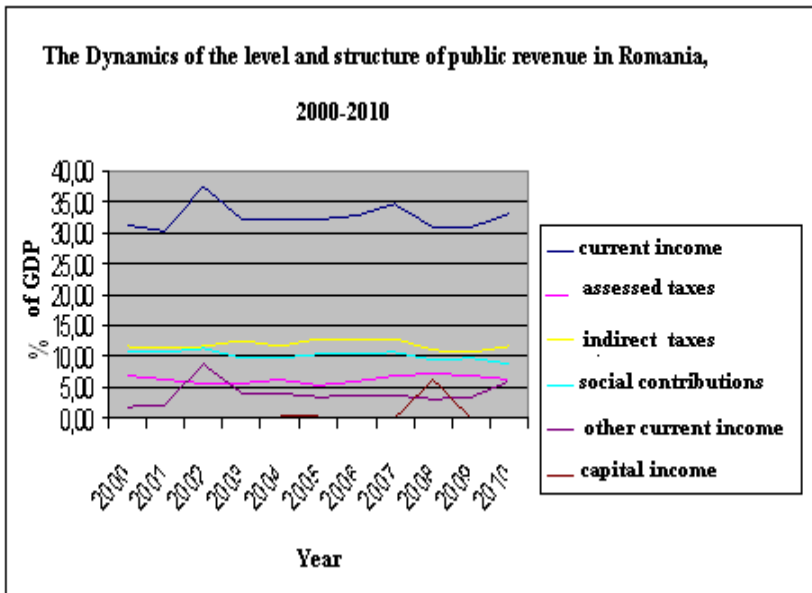
The present paper uses the information regarding the 2000-2010 Romanian fiscal aggregates, whose analysis will be carried out by means of empirical studies, which are based on the statistical processing carried out by INSSE, The Ministry of Public Finances and the NBR reports.

We initiate our research by presenting a landmark concerning the evolution in nominal figures of the Romanian fiscality during the analysed period. This landmark can be viewed and studied in the following table:

**Table no. 1.** The dynamics of the level and structure of public revenues in Romania, 2000-2010

Specification/ Year (% in GDP)	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Total revenue	<b>31,3</b>	<b>30,3</b>	<b>37,6</b>	<b>32,2</b>	<b>32,4</b>	<b>32,3</b>	<b>33,1</b>	<b>34,7</b>	<b>32,0</b>	<b>32,0</b>	<b>33,0</b>
Current income	31,2	30,3	37,4	32,0	32,0	32,1	32,9	34,6	31,0	30,9	33,0
Direct taxes	6,9	6,2	5,7	5,7	6,4	5,3	6,1	6,9	7,3	7,0	6,4
Indirect taxes	11,6	11,2	11,7	12,5	11,8	12,9	12,7	13,0	11,0	10,7	11,7
Social contributions	10,8	10,8	11,3	9,8	9,7	10,3	10,3	10,8	9,4	9,7	8,9
Other current revenue	1,9	2,1	8,8	4,0	4,1	3,5	3,8	3,9	3,1	3,4	5,9
Capital revenue	0,1	0,0	0,1	0,1	0,4	0,3	0,1	0,1	6,2	0,1	0,1
<b>% Total</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>
Current revenue	99,7	100	99,7	99,7	98,7	99,2	99,6	99,6	96,9	96,6	100
Direct taxes	22,0	20,5	15,8	17,7	19,7	16,5	18,4	19,8	22,8	21,8	19,5
Indirect taxes	37,1	37,0	31,1	38,9	36,4	40,0	38,5	34,5	34,4	33,4	35,5
Social contributions	34,5	35,6	30,0	30,6	29,9	31,8	31,2	31,6	29,4	30,3	27,1
Other current revenue	6,1	6,9	23,5	12,4	12,8	10,9	11,5	11,2	9,7	10,6	17,5
Capital revenue	0,3	0,0	0,3	0,3	1,3	0,8	0,4	0,4	0,6	0,5	0,4

Source: www.mfinante.ro.



**Figure nr. 1.** The dynamics of the level and structure of public revenue in Romania, 2000-2010

Regarding the evolution of the budgetary aggregates per capita, it can be stated that these offer an image concerning the tax burden on citizens, thus providing a landmark necessary in the comparison of tax and budgetary burden during various periods of time or between citizens belonging to different states.

In Romania, the evolution of the budgetary aggregates per capita, during the analysed period, can be viewed and studied in the table below:

**Table no. 2.** The dynamics and evolution of the share of the per capita budgetary components in Romania between 2000 and 2010

Specifi- cation/ Year	BGC income/ per capita	income in direct tax/per capita	indirect tax revenue/per capita	expenditure BGC/per capita	Lei
					gross budget deficit/per capita
1	2	3	4	5	6=5-2
2000	1.194	264	444	1.355	161
2001	1.685	345	623	1.879	194
2002	2.698	411	844	2.856	158
2003	2.901	517	1.133	3.046	145
2004	3.639	728	1.342	3.821	182



2005	4.390	725	1.764	4.581	191
2006	5.144	954	1.986	5.520	376
2007	7.209	1.438	2.709	7.772	563
2008	8.048	1.895	2.856	9.917	1.869
2009	7.211	1.633	2.497	9.568	2.357
2010	7.945	1.541	2.817	9.510	1.565

*Source:* Annual Reports of BCR, 2000-2010; www.mfinante.ro-arhivă, general consolidated budget 2006-2010

The dynamic of public revenues resulted from direct and indirect taxes and public social insurances, at an EU level, registered the following evolution:

**Table no. 3.** Dynamics of EU27 government revenue from direct taxes (% of GDP)

Specification	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
<b>EU maximum</b>	30,3	29,3	29,1	29,3	30,2	31,7	30,2	29,4	29,7	30,1	x
<b>EU average</b>	12,5	12,2	11,9	11,8	11,7	11,9	12,1	12,5	13,1	11,9	x
<b>EU minimum</b>	7,2	6,6	6,3	6,5	5,8	5,5	5,5	6,1	6,4	6,0	x

*Source:* Eurostat, <http://epp.eurostat.ec.europa.eu>

**Table no. 4.** Dynamics of EU27 public revenues resulted from indirect taxes (% in GDP)

Specification	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
<b>EU Maximum</b>	17,0	17,2	17,4	17,2	17,5	18,7	19,4	18,5	18,2	18,9	X
<b>EU average</b>	13,4	13,2	13,3	13,4	13,5	13,8	13,8	13,7	13,5	13,7	X
<b>EU minimum</b>	11,3	11,0	10,8	11,1	11,1	11,0	10,9	10,9	9,9	8,7	x

*Source:* Eurostat, <http://epp.eurostat.ec.europa.eu>

**Table no. 5.** Dynamics of EU27 public revenues, public social contributions (% of GDP)

Specification	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
<b>EU Maximum</b>	18,3	18,2	18,2	18,3	18,0	18,1	18,2	18,0	17,2	18,3	22,7
<b>EU average</b>	12,2	12,2	12,1	12,2	12,1	12,0	11,9	11,9	12,3	12,1	13,4
<b>EU minimum</b>	2,6	2,6	2,1	2,1	2,1	2,0	1,9	1,9	1,2	2,0	3,6

*Source:* Eurostat, <http://epp.eurostat.ec.europa.eu>

### **Literature review**

The *theoretical aspect* of the study is highlighted by numerous works belonging to Romanian and foreign authors out of which we mention selectively a few names such as: I. Văcărel, T. Moșteanu, I. Stancu, I. Talpoș, D. Dascălu, T. Stolojan, M. Duverger, P. Samuelson, M. Friedman, R. P. Musgrave and last but not least J. M. Keynes, the first to advocate the model of public funding through budgetary deficit.

The *procedural aspect* of the paper is highlighted by the national and community legislation, out of which we mention the following: The Law of Fiscal-Budgetary Responsibility, no. 69/2010, Government Emergency Ordinance no. 64/2007 regarding public debt, The Stability and Growth Pact, as well as the considerable volume of statistical information on the budget executions, respectively the ones on the evolution of budgetary deficit in Romania and in the EU member states, as well as those on the structure and dynamics of the Romanian sovereign debt stock, during the analysed period.

The information database was provided by the monthly, quarterly and annual reports of the National Bank of Romania, the reports of the Ministry of Public Finances, the Eurostat data bank, the data basis of the International Monetary Fund, of the European Commission and of the Organization for Economic Co-operation and Development.

### **Results and Discussion**

Regarding the volume of public resources, it has been observed that not all channels of budget formation, which form the consolidated budget, function with the same efficiency. This situation leads to disequilibria which will be financed through the resources of another budget and ultimately through public loans. In this respect, one cannot overlook the importance and relevance of transfers between the state budget and local budgets through sums and VAT share splits and income taxes or the covering of temporary cash gaps of local budget from the resources of the general current account of the State Treasury.

Likewise, during the analysed period (2000-2010), it was noticed a lack of resources in the budget of social insurances. This was the effect of electoral delays of the reformation of the social public

insurance system. A study<sup>1</sup> in this area carried out in 13 EU member states revealed fiscal stationary and long structural pauses in time, which denote the authorities' caution before taking decisions that are not usually very popular.

However, in a state in which the ensuring of public salary and pension funds represents a problem, the reduction of expenditures is no longer a suitable solution. Thus, the public credit is used in order to maintain the financial equilibrium. However, it is preferable to use the credit extant on the internal market and not the one extant on the external market, with the condition that the former is not too expensive or a generator of economic eviction. Excessive dependency on external resources leads to the increase in vulnerability of the national economy and of its macro-economic equilibrium in case of fluctuations on international markets or as it is nowadays in case of the worldwide economic crisis. This aspect was highlighted through a study<sup>2</sup> that points out the relationship between the primary surplus and the level of the public debt, as an indicator of fiscal sustainability. For both - industrial countries and emerging economies - there are proofs of a long term relationship between the primary surplus and debts, as long as we take into consideration a common stochastic tendency.

Moreover, it has been observed the existence of a stochastic trend for liquidities at a national level. While the fiscal sustainability of emerging<sup>3</sup> market economies is widely dependent on the worldwide liquidity, the industrial countries seem to be less affected by this common stochastic tendency. As a result, the fiscal policy on the emerging markets seems to be led by the pursuit of the unique purpose of fiscal viability, while the industrial countries combine a preoccupation for public debt sustainability with a consolidated welfare of the business cycle. Unlike emerging market economies, the industrial countries are capable of running deficits when they are confronted with periods of economic regression or in order to compensate the temporary increase of governmental expenses.

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<sup>1</sup> Holmes, M.J., Otero, J., Panagiotidis, Th. Are EU budget deficits stationary?, *Empirical Economics*, Volume 38, Number 3, 2010, pg. 767-778

<sup>2</sup> Byrne, J.P., Fiess, N., MacDonald, R. The global dimension to fiscal sustainability, *Journal of Macroeconomics*, Volume 33, Issue 2, June 2011, pg. 137-150

<sup>3</sup> Miyazaki, T. The effects of fiscal policy in the 1990s in Japan: A VAR analysis with event studies, *Japan and the World Economy*, Volume 22, Issue 2, March 2010, pg. 80-87

The above mentioned affirmation is consistent with the difficulties encountered by emerging market economies when issuing government securities.

During the analysed period, the management of fiscal policies despite the political background was characterised by the perpetuation of the structural budgetary deficits combined with a restricted space for manoeuvring regarding the fiscal corrections due to the high level of twin deficits; for example, in 2008, the nominal budgetary deficit represented 5.4% of GDP, while the current account deficit represented 13% of the GDP, both being considered excessive.

Likewise, maintenance of fiscality at the same level in 2007 and 2008, which were years of economic growth characterised by an economic overheating, is another mistake of the Romanian authorities according to the theoretical predictions.

The studies<sup>4</sup> carried on after 2007 - the beginning of the financial and economic crisis - highlighted a reduction in the governmental reaction revenues, reported to the economic cycle for the majority of countries, compared to the capacity to react of the governmental expenses. Thus, these results notify a deterioration of the capacity of fiscal authorities to use the automatic stabilizers to counteract the negative effects of the economic crisis.

### **Conclusion**

Drawing a conclusion on the aspects observed previously but also considering the huge fiscal stimulus packages used on the background of the financial crisis, the budget consolidation is going to be one of the most important tasks of the governments around the Globe. Recent studies<sup>5</sup> bring forward the fact that corrupt countries register less success in the consolidation of their budgets during times of serious crisis. Researchers managed to identify two negative effects: a direct and indirect one deriving from the choice of the wrong fiscal policy tools. From a political and economic point of view, this might be explained through the fact that corrupt governments have higher

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<sup>4</sup> Afonso, A., Agnello, L., Furceri, D., Sousa, R.M. Assessing long-term fiscal developments: A new approach, *Journal of International Money and Finance*, Volume 30, Issue 1, February 2011, pg. 130-146

<sup>5</sup> Arin, K.P., Chmelarova, V., Feess, E., Wohlschlegel, A. Why are corrupt countries less successful in consolidating their budgets?, *Journal of Public Economics*, In Press, Corrected Proof, Available online 31 January 2011;

stimulant's that allow them to maintain their huge expenses even during consolidation periods, so as to take into consideration the lobby interests- the so-called parasitism among lobby groups<sup>6</sup>.

The fiscal behaviour of corrupt countries during harsh periods has to be monitored carefully by international organizations such as The European Union and the International Monetary Fund. As corrupt countries, they cannot consolidate in a durable way their budget, even during harsh periods, because they chose the wrong tool which induces the idea of the projection of certain control mechanisms which refer not only to short term deficit, but are also guided directly towards the reduction of expenses. This might also be an intelligent device to alleviate the disproportions caused by the corrupt governments, towards high expenses without interfering in a justifiable manner with the real needs of the public services.

Regarding the impact of decentralization and regionalization on the tax component and finally over the budgetary balance, there were identified and brought forward through B. Neyapti's<sup>7</sup> study, a series of proofs that point out a serious negative effect of fiscal decentralisation. Neyapti's findings recommend caution regarding a fiscal decentralisation since the country characteristics and the institutional characteristics influence greatly the efficiency of fiscal decentralisation in deficit reductions. The study shows that the efficiency of fiscal decentralisation in the deficit reduction is increased by population growth, even though deficits are usually associated in a positive manner with the population growth. The results also warn on the fact that decentralisation affects public expenses, which are more efficient in case of low levels of ethno-linguistic and government division, while these characteristics do not seem to influence the effectiveness of decentralisation over revenues.

However, in our country, over the past two decades, the general equilibrium of the society, of the economic and social system has been distorted if we take into consideration the contradiction between the two systems. On one hand, the social system inclines towards a Ludwig Erhart type of social model, characterised by increased social protection

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<sup>6</sup> Dharmapala. D. The Congressional budget process, aggregate spending, and statutory budget rules, *Journal of Public Economics*, Volume 90, Issues 1-2, January 2006, pg. 119-141

<sup>7</sup> Neyapti, B. Fiscal decentralization and deficits: International evidence, *European Journal of Political Economy*, Volume 26, Issue 2, June 2010, pg. 155-166

measures which imply the levy of an important quota (40% of the gross domestic product); a model applied in the North European States and having Germany as its main pioneer. On the other hand, the Romanian fiscal model of the past two decades has rather been a minimalist one, according to the analysed figures and if we take into consideration the fact that tax levies represent approximately 31% of the gross domestic product. Likewise, it is questionable how much of the Romanian social model has an explanation in the need of collecting votes and if the actions anticipated through the public budget represent a true reflection of the necessities that are needed for the present development of our country; respectively if it can be justified from the point of view of the rigors of the efficiency criteria regarding the spending of the public money.

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## **The Comprehension Process of Audit and Accounting Culture through the Academic Environment**

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### **Abstract**

While the organizational culture and the professional culture are centered on serving the customer, the accounting and audit culture are focused on helping all accounting users. Mainly, culture operates with information that is prepared, disclosed and, in the same time, interpreted by its receivers and senders. The way each of us interprets the information or offers judgments and opinions, depends on our referential framework, that is a combination of our educational, developmental intellectual culture and work related experiences. The present study tries to point out how these concepts are understood by students from the academic environment and how knowledge gathered during their educational cycle can be transferred into practice.

**Keywords:** accounting and audit culture, academic environment, accounting profession, audit profession, practice

### **Introduction**

Accounting history's lesson shows us how two different accounting cultures formed and developed during time – the Anglo – Saxon accounting system and the European continental accounting system. The two of them are considered by some authors as being rivals. The study of the circumstances they appeared in can provide answers to a series of questions regarding the current problems of accounting and audit harmonization and internationalization. The appearance and the

development of the accounting and audit culture, in various forms of organization, followed the way designed by the accounting systems, in the attempt to answer at the requests of these systems regarding the information requirements of the financial information users. Therefore, it is essential to understand the way information from the academic environment is revealed and put into practices, and how this kind of element can influence both - the accounting profession and the audit one. Actually, practices gained during the educational cycle can definitely influence the attitude of each practitioner that acts in the economic environment.

### **Materials and Methods**

In order to establish a connection between the concepts and practitioner elements gained from the University, a complex questionnaire was well-established for the field research. The research methodology is based on the fact that concepts understood from the bachelor's and master's cycle can heavily influence the attitude of student at the working place. Moreover, the behavior of them is defined by the concepts established by the company where they work.

The questionnaire was formed from 9 questions, 3 of them being opened questions, while the others were close questions. The close questions were used as they offer a facile way of summarizing the results, while the opened questions were used as the respondent is not restricted by the given answers, and consequently, there is the possibility of free manifestation of their own opinions and developments. The questionnaire was completed by 50 students from the Faculty of Accounting and Management Information Systems, both from the under graduated environment and the graduated one (students that already had a bachelor degree).

The respondents were divided in two groups, each with 25 students. The respondents were both from the rural and urban locations as no discrepancy between them should be provided. It is considered that the academia's environment mitigates the differences between social provenience and that both students should achieve the same amount of information. As a fact, from the first group of interviewers, 16% have their home destination in rural area, while the percentage was lowered for the second group, as only 3 students came from the rural environment, or in other words, 12% of the sample were considered as having a different home destination than a Romanian city.



Another important element of our research is that the students were all Romanians, as we wanted to establish how their attitude in the working area would be as regarding the audit and the accounting profession.

The objectives set for this research area were based on the fact that we wanted to establish a connection between the practices and the concepts obtained during the educational environment and to show how these elements could be pointed out at the working place.

The data was collected at the beginning of the 2012 academic year, by selecting random students from both educational cycles.

### **Literature review**

The connection between accounting and audit profession can not be denied, as both of them have their main activity related to the financial statements of the analyzed company. Furthermore, these professions influence the institutions and the accounting systems. The factors that influenced the emergence of the various accounting systems, as well as the accounting systems themselves, have decisively influenced the forms of organization of the accounting and audit profession (Mihalciuc, 2006).

In 1965, Mautz underpinned the rapid and even dramatically change of the business environment in which accounting exists. The scientific management with its emphasis on the operations research and the application of various quantitative methods in decision making, the expansion of organization, the interest in economic analysis and the innovations in the methods of accumulating and processing business data had significant implications for accounting and audit at that time and they still do nowadays.

As Bayou and al. (2011) observed, the accounting and audit profession continues to struggle with the problem of the veracity of accounting reports, in light of the different needs of various financial statement readers for truthful reports.

As emphasized by Saltera and Lewis (2011), research has shown that differences in financial reporting practices between countries have costs associated with those differences. For example, Choi and Levich (1991) provide evidence that accounting diversity can affect the actions of individual investors; while Saudagaran and Biddle (1995) show that accounting diversity can adversely affect the number and volume of listings on stock exchanges, elements that have a crucial impact upon

the audit elements. Most recently, as shown by Saltera and Lewis (2011), Karamanou and Raedy (2004), Ashbaugh and Pincus (2001) demonstrate that differences in financial reporting practices and resultant accounting and audit outcomes between countries can adversely affect the performance of securities analysts. Recent studies have continued to conclude that these financial reporting differences are not going away. Chatham et al. (2010), Lewis and Salter (2006), Jones and Wolnizer, (2003), d'Arcy, (2001), Larson & Kenny, (1999), all cited by Saltera and Lewis (2011), show that there are still significant differences in the financial reporting practices between the countries. Moreover, Popescu L., Oancea- Negrescu M. D, Anica-Popa, A. (2010) revealed the importance of proper evaluation of the company as the values provided by the accounting practitioners and the information revealed by the audit team. Similar idea was developed by Stanila, G, A, Popa, A. F, Ispas, S. (2012) as they emphasize that a proper financial reporting offers relevant information for sustainable developments of large Romanian companies.

While it can be argued that as IFRS based financial statements become more common, Douppnik and Tsakumis (2004) point out that the flexibility of interpretation contained within IFRS and the ability of any country to carve out unacceptable portions of particular IFRS standards will continue to lead to different accounting and audit practices outcomes among countries.

As shown by Finch (2007), Gray proposed that the national accounting and audit culture could be characterized by their position in relation to four accounting values, which are the principal values for the accounting and audit subculture: Professionalism versus statutory control; Uniformity versus flexibility; Conservatism versus optimism; Secrecy versus transparency.

The first two relate to the authority and enforcement of the accounting and audit practice, while the second two relate to the measurement and disclosure of accounting information at country level.

In one of his studies "The role of accounting education in reproducing the accounting profession", Duncan (2002) examines the interaction of two institutions: one academic and one professional, trying to show how and why the first one is dominated by the other one. His opinion is that the profession is able to impose its vision of accounting education in the field because the field is heteronymous and highly demand-driven. The two sets of players occupy a field where

they “attempt to usurp, exclude and establish monopoly over the field’s reproduction and type of power effective in it” (Everett, 2002).

The educational system and its modern nobility only contribute to disguise, and thus legitimize, in a more subtle way the arbitrariness of the distribution of powers and privileges which perpetuates itself through the socially uneven allocation of school titles and degrees (Bourdieu and Passeron, 1990). Bourdieu’s work (cited by Duncan, 2002) contributes to our understanding of the relation of an education system to our society. Many of his concepts help us understand how an education system “contributes to reproducing the structure of the distribution of cultural capital and, through it, the social structure” (Bourdieu and Passeron, 1990).

Tucker (1995) considers that students are seen as „meaning makers” not only through their reading and writing, but also through their interpretations of the facts, while Wang (2007) points out that the teaching skills might not be readily transferable across populations of students and types of schools or programs.

Taking these elements, we wanted to establish if there is a connection between the concepts gained in the university, the audit and accounting profession and, in case of positive response, how these elements influence both professions.

### **Results and discussion**

After the data has been collected, the answers were analyzed and important conclusion was developed. Moreover, a score according to the degree of relevance was established in order to have a better understanding of the students’ attitude.

The answers provided to our questions are revealed in the following section. As a consequence, the first question was “How many years have you been studying accounting and audit subjects?” The answers were divided in the following parts: less than a year, 1-2 years, 3 years, 4 years, more than 4 years, and the scores attributed to them were rated between 1 and 5.

**Table no. 1.** Results obtained for the first question

<b>Question 1</b>	<b>less than 1 year</b>	<b>2 years</b>	<b>3 years</b>	<b>4 years</b>	<b>more than 4 years</b>
<b>Answers</b>	5	10	15	15	10
<b>Percentage</b>	10%	20%	30%	30%	20%

*Source:* Own compilation

As it can be seen, in the third and fourth year of study there are 60% of the interviewers and they considered that the information regarding the audit and accounting courses is relevant. The scoring is 180, and it covers 72% of the largest value.

The second question was: “How do you consider that knowledge gained from participating to the accounting and audit courses is?” The possible answers were over the expectations; as expected; normal; below expectations; I don’t know.

**Table no. 2.** The results obtained for the second question

<b>Question 2</b>	<b>I don't know</b>	<b>Below the expectations</b>	<b>Normal</b>	<b>As expected</b>	<b>Over the expectations</b>
<b>Answers</b>	3	5	17	9	16
<b>Percentage</b>	6%	10%	34%	18%	32%

*Source:* Own compilation

The results point out that more than 84% of the respondents are content with the information obtained during their educational environment. The score is 151, and it covers 60.4% of the highest value.

The third question was: “How would you appreciate/rate the relation between accounting and audit profession, accounting and audit education?”

**Table no. 3.** The results obtained for the 3rd question

<b>Question 3</b>	<b>I don't know</b>	<b>Below the expectations</b>	<b>Normal</b>	<b>As expected</b>	<b>Over the expectations</b>
<b>Answers</b>	5	4	17	5	20
<b>Percentage</b>	10%	8%	34%	10%	40%

*Source:* own compilation

As it can be seen, 84% considered that there is a high relationship between the concepts gain in the university and the similar profession. The result are somehow connected with the second answer and point out that there is a high expectation that university will covered the information need at a working place. The score is 135 and it covers 67.5 of the highest value.

The fourth question was: “Which of the following values did you find in the information received during the accounting lectures?” The answers were: professionalism, uniformity, conservatism, secrecy. Multiple answers were permitted, and as a consequence no score was calculated.

**Table no. 4.** Results obtained for the 4th question

<b>Question 4</b>	<b>Professionalism</b>	<b>Uniformity</b>	<b>Conservatism</b>	<b>Secrecy</b>
<b>Answers</b>	50	45	40	38
<b>Percentage</b>	100%	90%	80%	76%

*Source:* own compilation

As it can be seen, almost every concept is detailed in their educational environment, as these are considered to be the accounting values and they are presented in the education system.

The fifth question was: “Do you consider the accounting information received in the faculty is useful in your career?” The answers were definitely no, no, I don’t know, yes, certainly. The results are presented in table 5.

**Table no. 5.** Results obtained for the 5th question

<b>Question 5</b>	<b>Definitely no</b>	<b>No</b>	<b>I don't know</b>	<b>Yes</b>	<b>Certainly</b>
<b>Answers</b>	0	0	3	20	27
<b>Percentage</b>	0%	0%	6%	40%	54%

*Source:* own compilation

The results proved that more than 90% of the students interviewed considered that the information received among their years' of studies is useful for their future career. The score covers 54% of the highest value.

The sixth Question was: "Can we talk about an accounting culture in the accounting profession"? with yes and no as answers.

**Table no. 6.** Results obtained for the 6th question

<b>Question 6</b>	<b>Yes</b>	<b>No</b>
<b>Answers</b>	50	0
<b>Percentage</b>	100%	0%

*Source:* own compilation

The answers established that there is a high connection between the audit profession and the accounting one, while the audit and accounting culture are correspondently.

The following questions were opened: "Why is important for accountants to be aware of the values, beliefs and assumptions that underline the accounting culture? Which are the elements that determine the accounting and audit culture? Describe a real situation where you would use information gathered from your lessons?" For the 7<sup>th</sup> question, the answers were around the importance of a proper and reliable evaluation of the company's performance, while the 8<sup>th</sup> one, revealed that accounting and audit principles and practice are the main elements of the accounting and audit culture. In the last situation, students would apply their knowledge in order to evaluate correct the accounting information offered by the company where the audit is realized or where the accounting is kept.

### **Conclusions**

The present research tries to point out the importance of accounting and audit culture related to the accounting and audit professions, as the knowledge is observed and understood from the educational cycle. The study was realized considering the answers of 50 students from the Faculty of Accounting and Information Management Systems, who provide proper information by answering to a questionnaire. The results point out that there is a high degree of connection between the concepts gained in the educational process and the practice of the audit and accounting profession. Moreover, the results emphasize that the influence of education systems upon the audit culture and accounting one could not be denied, and nonetheless, there is a high preparation level in the university when these two professions are considered very important in the Romanian environment.

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## **Knowledge-Management in the Hungarian Economy**

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### **Abstract**

The key to a successful crisis management is prevention. In crisis management, not only the strategy and scenario development play an important role. One way to deal with the financial crisis is to cut costs by downsizing and reducing production, but, as some businesses have chosen, it is also possible to invest in innovation and quality improvement. Value creation for customers is essential, even if consumption may temporarily decline during this period. As soon as the recession ends, new products may be in competitive advantage against the competitors who have been trying to adapt with reduced prices. This study examines the strategies and management tools of businesses that have experienced only a small decline or even a business-growth during the global financial crisis. It highlights the importance of investing in innovation, quality management and human resources, since these are critical factors also in prevention and crisis management, not only in income maximization.

**Keywords:** financial crisis, SMEs, innovation, knowledge-management, competitiveness

### **Introduction**

We have been feeling, even deeper, that we are members of a global society, where not only our dependence on each other, but also our interdependence is getting intensive – underlined Leslie Newbigin, the undisputedly relevant theologian of the end of the 20th Century. These changes in globalization have an effect on our lives, although these effects and the reactions to them can be considerably different. The most important problem of our epoch is to combat with the anti-balances, which appear in every aspect of our lives. The evolved anti-balance situation has been intensifying in the last 30-40 years, by expanding the globalization processes, because not all the economic participants and national economies were able to defer to the changeable global circumstances.

The fact of the change sees the story of the humankind and the development of the company through it. Changes which appear in an economy can be generated by two important facts. One is the maintenance of competitiveness, the aspiration to satisfy the consumer demands at a higher level, otherwise any kind of unwanted situation and firstly a negative economic event, stagnancy or crisis.

The role of know-how and intelligence are more and more revalued. Contrary to the traditional resources, the number and the efficiency of investments in know-how, education, research-development, is getting dominant. In the knowledge-based economic systems are only those organizations viable which have an up-to-date knowledge. It means also that organizations should become knowledge-based, in order to preserve its competitiveness.

Peter Ducker underlined that the added value need resources, but not natural resources, not even capital, he need knowledge. The continuously change, the technological innovations and the increase in the number of competitors are characteristic for the success of the companies. These activities define the knowledge-based company, whose only and most important task is the continuously renewing. Many people think that the organic learning in long-term will not be a competitive fact, but its lack will mean a drawback in competitiveness. The only sustainable advantage up to your competitors is that, when you are ready to study faster than they use to do.

The Hymer-theory for the market economy means that the company which wants to exist for a long-term in the market, need to have some kind of special competitive edge. This competitive-edge can

derive from many resources, but developing the knowledge-based economies any of the companies can become competitive.

Peter F. Drucker who claims, today the only really valuable resource for the individual and the society is the knowledge, defines similar thoughts. To overstep this statement we can also say that knowledge is not only a production factor. It is not only the condition for the maintenance of the competitiveness, but it is also the successful mean of the crisis management and for its prevention. All these have been proved by many world economic crises, which made many companies and the national economic to go bankrupt.

Many enterprises have tried to defend against it by investing into knowledge and all their efforts became successful. The investment in knowledge is a very good solution for the management, not only in order to keep competitiveness, but also in coordinating the crisis management.

### **The relation between the principles of economic rationalism and competitiveness**

Lester Thurow pointed out in a prediction for the 21<sup>st</sup> century that, the main resource of competitiveness is human capital. In the knowledge-orientated society, success is defined as a value. Although we can not accept from everyone to be successful, but for the individual and its family it is a vital thing to have at least one field where they can show up results – argues Peter F. Drucker. At the same, it must be accentuated that only the existence of knowledge does not mean a guarantee for the permanent market success.

According to Edward E. Free, the statement that knowledge is power is not entirely true. The used knowledge is power, money and charge. Knowledge itself when it is not used has no power. Knowledge must be maintained continuously and the employers must be motivated to improve their skills and abilities. In this process, management has a prominent role. Management is a conscious influence upon the organizational members, in order to let them be active to achieve the defined goals of the company. In such a way, management focuses on the people through their motivation and its maintenance.

According to Thomas H. Davenport and Laurence Prusak, lack of motivation and without any motivation means the improvement of knowledge. In their opinion, many initiations related to knowledge were

based on a utopian assumption that knowledge moves steadily without interference of the motivation powers.

The definition of the knowledge-share motivation was summarized by Tomka: it means a competence which makes the managers able to reveal the reasons and the power to get the employers with appropriate arguments to share their knowledge with each other. Effective management with knowledge does not only mean that management looks after the employee's continuous training. It also means that we can also benefit from their abilities at the most appropriate place and time. Moreover, management creates such circumstances for the employees, where they can work together with pleasure and also share their ideas and knowledge with each other. This is only possible by a company, which has a strong social capital, where the employees work in teams, and they can entirely identify themselves with the company's and team's interests.

According to Ten Have: "Control can collide with creativity, initiative abilities and taking risks." For management must be created a balance between the employees' demands and the company goals. If we want to define knowledge, most of the experts agree that it means a kind of ability for solving an issue. According to Mihály Polányi: to understand something is not a free-will activity; it is even not a passive experience, but an activity with big responsibility. Saint-Onge and Wallace defined knowledge as an ability to be able to act with result. They mean that knowledge laid in context and by authentic people validated information.

According to Th. Levitt, our most important goods – our colleagues, good reputation and brands - are not listened in our accountancy. Tomka said: it is known that many companies market value is a manifold of its accounting value. The reason for that is that most of the intangible assets are not displayed in the company's booking. The part of these assets is formed as the human capital as well, which means the individual competence, the colleagues' knowledge and proficiency.

The essential term of the contribution is knowledge division. To the successful working of the knowledge-organizations, the barriers must be overstepped and these difficulties go over the facts impeded the contribution inside the group. On the other hand we can say that, the management of organizational knowledge is the biggest dilemma.

### **Crisis management and the competitiveness with knowledge management**

In the developed economies, the sharing of knowledge, the knowledge-transfer and the opened innovation is a well-tried practice and it is also the basic factor in increasing competitiveness. In Hungary, this process is not usual. Our country wants to achieve more profit by employing cheaper work force, thus it will not have any chance for the real and for the general welfare. Nowadays, the economists speak about a new revolution: the knowledge and information revolution. The importance of the traditional resources like capital, for example, is being decreased. In the knowledge – epoch, the most important resources are knowledge and intelligence. According to John Weinstein – who is the member of the Pharmaceutical Executive – the crisis does not only mean a danger, but it is a possibility as well.

According to this meaning, the crisis is not else than a new chance for the re-organization of our company focused on the problematical issues and continuing our activity in a very new dimension. If we do not only focuses on the problematic issue, than it is possible that in spite of the crisis, the company gets improving itself. The crisis can also be very useful, forcing the company participants to think over and re-organize its whole activity. The re-thinking and re-organization of the company's activity is called revitalization.

The crisis also means an important change. The crisis is the compulsion of change. Each of these definitions agrees that crisis is the consequence of the temporary disorder of the balance, because the company is forced to go ahead towards innovation and renew itself. The company's successful or unsuccessful crisis management depends on the promptitude and quality of the reaction. Because of the crisis, the company will not break off. With an appropriate strategy and innovation, it can be pulled through and its activity can be pursued. One of the key of change is the aspiration for reformation, research and innovation. The role of knowledge competitiveness appears here. Among the Hungarian enterprises just only a few recognized that the quick change and adaptability became one of the most important structural potential.

According to Jonas Ridderstale: we have to put aside our fears and we need to recognize that only two kinds of companies will exist in the future. The first, which can react quickly to the changes, the second, which will die. In the first category will be those companies that deal

with their people knowledge as a key factor. Helen J. Alford and Michael J. Naughton draw our attention to this and they underline: the re-organization of work is anxiously complicated. In Hungary, it is still a popular error that everything is for money. Obviously, knowledge cannot be reached without money, but it is not the money, which is the most important for the company. According to Janos Reith: we overestimate the importance of money and the companies do not first money, but work, because there is not money where no performance exists. The biggest fault of the Hungarian economy is that it is not focused on production.

In Hungary are needed such enterprises which would invest mostly into the development of knowledge, which compete with knowledge and higher benefit. To make the country more competitive would be one of the key-momentum to create knowledge-based enterprises. In the knowledge-companies, the workers are high-qualified, well educated, whose job mostly consist in converting information into knowledge, using their own competence, just sometimes the information and help of the special knowledge providers. These companies have a little real capital; their intangible assets are more valuable than their property means. These companies are on a leading edge in innovation, in asset procreation; they create high quality products/services and belong to the most competitive enterprises. In the interest of preserving competitiveness, the leading managers have to be aware in the fact that the long-term success of their companies can only be guaranteed when they absolve the theory of lifelong-learning concerning to themselves and also for the human resources.

The role of knowledge by the aspiration of the competitiveness and crisis managements is beyond doubt. The crises are accompanied by changes, but there are also such changes which are needed to precede them. Such changes can be a new strategy and its realization, the reorganization of any kind of position or a work, the launch of a new product or the development of knowledge. There are little changes involving only a few people, but there are also deep, radical and expanded ones. The alteration is one of the most difficult and riskiest manager's assignments. It doesn't matter what methods are used in changing the management, knowledge can be a very useful resource of a successful work.

Change-management and its methodology are in modernization. Under change-management we mean the coordination of changes,

which are operative, needs daily interference, economic planning, but it is not a short-term lasting process. For this period draws the attention Galileo Galilei who said: not knowledge, but learning, not the tenure, but the getting, not the attendance, but the way which leads to there mean the greatest pleasure.

It is generally known the fact that the companies which do not invest in knowledge do not compete with quality and creativity. Graffiti emphasizes this fact and raises an adequate question: "For those people who mean that knowledge is expensive, do they really count with the costs of the ignorance?"

### **Results - INNOTARS (questionnaires)**

The Hungarian ventures do not compete with knowledge and a nationwide research program proves high benefit. First have a look at the results of the INNOTRANS program, whose research leader is Csath Magdolna. The National Research and Technological Office financed the Program. The most important goal of the program was to introduce the most authentically national small and middle enterprises innovation performance. I feature from the research those questions which are related to the knowledge economy, in any kind of aspects. Altogether 814 questionnaires and 85 deep interviews were at our disposal. In the first point, I was looking for an answer about how the economic policy could help to improve the innovation's performance of the companies.

Innovation is such an activity which cannot be successful without appropriate expertise and high-qualified human resources. Innovation is based on knowledge and it also needs it, requires creative and high-qualified experts. On the other hand, the enterprises drew the attention to the fact that for innovation, successful economical activities are needed: a favorable taxation system, the bureaucracy and corruption should be brought down. On the other hand, only a few 26.04% of the companies are on the opinion that the economic-policy should support the education and the training of experts. The Hungarian ventures have not recognized the potential possibilities lie in knowledge management.

**Table no. 1.** How could the economic-policy help the enterprises?

The economy-policy would promote the innovation with the following issues		
More prosperous taxation	693	85, 14%
Less bureaucracy	549	67, 44%
Less Corruption	430	52, 83%
More favourable support system	415	50, 98%
More favourable credit intake possibilities	311	38, 21%
Less self-power by each applications	259	31, 82%
Interests supports by innovation investments	256	31, 45%
<b>Education, experts training</b>	<b>212</b>	<b>26, 04%</b>
Others	20	2, 46%
All enterprises	814	all firms 814=100%

The next chart uncovers much about in what measure the Hungarian enterprises prospects on knowledge. Among the activities which are highly based on knowledge, significant is the research-development activity. The expertise and the existence of creative experts are essential for this. The measure of how important the role of knowledge in the company's activity is and in what measure they use the obtained or obtainable knowledge is appropriate shown by the rate of workers from the R&D sector. From the interviewed 814 ventures, in 540 do not work employed experts in R&D field. What is the main reason for that? The answer can be defined in two aspects: on the one hand, for the Hungarian companies only in a little measure are characteristic the innovation, on the other hand, the majority of the enterprises doesn't want to compete with quality, but cheapness and price-reductions. On innovation and knowledge – development, only a few enterprises spend a considerable amount.

**Table no. 2.** What is the rate of workers in R&D by the interviewed companies?

Rate work in R&D	Number of firms	Rate (%)
<b>0%</b>	<b>242</b>	<b>29, 73%</b>
1-10%	177	21, 74%
11-20%	35	4, 30%
Over 21%	62	7, 62%
<b>No dates</b>	<b>298</b>	<b>36, 61%</b>
All enterprises	814	100%



For the management, it is not the only issue to motivate their employees to achieve a higher work performance, but also to help and motivate them to feel some kind of commitment to improve their own individual skills as well. The success of the company can depend on – beside some other facts – the employees' positive attitude, qualification and creativity. In a well-managed business, the stakeholders share, their own ideas contribute together to the team and company's successes.

The prompt ideas and creative thoughts should be appreciated and possibly recompensed. The stakeholders should be inspired of sharing their ideas, knowledge and thoughts, because it can be the secret of success. If someone has a good idea, if he or she uses her or his knowledge and creativity to make her/him useful for the business, it is even not sure that he or she gets an honorable mention (in the Hungarian entities).

It is well mirrored in the next table that in a huge number of the Hungarian companies there are managers who do not even expect from their employees to help with their own ideas the decision-making process.

**Table no. 3.** The appreciation of knowledge, creativity and brainstorming, in management

<b>Colleagues who are interested in knowledge-share</b>	<b>Number of answers</b>	<b>Rate (%)</b>
Ideas without remuneration	448	55, 04%
Ideas, praise	217	26, 66%
Ideas, promotion	187	22, 97%
Ideas with remuneration	170	20, 88%
<b>It is not expected from the colleagues, the management decides</b>	<b>132</b>	<b>16, 22%</b>
Ideas, ideal	74	9, 09%
Other	30	3, 69%
All enterprises	814	all firms: 814=100%

### Results - INNOTARS (deep interviews)

In the next point we are looking for the answer to the question: “Do the companies employ knowledge managers, innovations-manager and change-managers?” All the three positions have an important role if we deal with the knowledge-economy. From the 85 interviewed companies, only 12 firms indicated that they employ those people in the above-mentioned working position or in similar. It means only 14% of the companies involved in this research.

The question arises again in the reader: all the other companies are not managed the knowledge-processes or there is not enough financial coverage to employ such a kind of professionals. For the 14% rate, the question itself gives the answer.

**Table no. 4.** Do the companies employ knowledge managers, innovations-manager and change-managers?

<b>No data</b>	<b>4</b>	<b>4, 71%</b>
<b>No of them exist</b>	<b>69</b>	<b>81, 18%</b>
There is one of them	12	14, 12%
Altogether	85	100, 00%

In 12 enterprises we only found 7 change managers, that means 23% of all the companies. Innovation manager’s work for 6 companies, their rate is 7.05% compared to all the interviewed companies.

The next table also draws the attention that Hungarian enterprises do not count on knowledge, but only on human resources. The question is: “What kind of outstanding participants/shake holders are important for the effective innovation by the companies?”

Here it is shown again that for the Hungarian companies not the participants are the most important from whom they can get knowledge, new ideas, or with whom they could improve together the existed knowledge-level, but they rely on customers, partners and representation organizations, in a most widely range. The importance of customers is prominent according to the Hungarian firms. It is essential the continuous contact with the customers. The story is not about how to establish with creative thinking, knowledge, new, innovative things.

**Table no. 5.** From who can derive knowledge to realize a reform?

No dates	11	12, 94%
Brain stormers	1	1,18%
From whom you can get knowledge	1	1,18%
State, authorities	6	7, 06%
Suppliers	7	8, 24%
Universities	9	10, 59%
Competitors	7	8, 24%
<b>Customers</b>	<b>21</b>	<b>24, 71%</b>
Insurance companies	1	1, 18%
<b>Partners</b>	<b>16</b>	<b>18, 82%</b>
Endowments	1	1,18%
Industrial chambers, trade corporations	11	12, 94%
Research Institutes	5	5, 88%
Experts, consultants	9	10, 59%
Appropriate market circumstances, tenders	2	2, 35%
And its participants	2	2, 35%
All enterprises (85)=100%		

The INNOTRANS program had been always looking for an answer to the question, what kind of abilities the firms possess if we talk about reform. The next table summarizes, what would be needed for the companies for a more innovative operation? These dates also confirm my statement, which was defined earlier in my essay, namely the Hungarian firms do not base their operation on knowledge and it's not knowledge the primary factor in competitiveness.

Most businesses would need money and as we could understand from Reith Janos's former defined words, it is not always the money which is the most important benchmark and key factor of performance.

**Table no. 6.** What would be needed for the companies for a more innovative operation?

Information	29	34, 12%
Knowledge	36	42, 35%
<b>Money</b>	<b>62</b>	<b>72, 94%</b>
Technology	29	34, 12%
Relationships	37	43, 53%
Creative workers inside the company?	35	41, 18%
The innovation inspired by the	37	43, 53%
Others	4	4, 71%
All enterprises (85) =100%		

### **Results - MMV research program**

I have received similar results from another national - wide research program, which was organized by a Foundation named Local Enterprise Agency. The research leader of this research was Csath Magdolna, chairman of the department.

The aim of the research was to study how the situation of the inland small and middle enterprises has changed since 2002. From the research I could raise two issues, which could refer to the quality of the knowledge economy. The next table gives the answer for the question, which are the means of a successful long-term operation of the company?

We can see that from 71 enterprises, less than 20% would need better professionals. Among the listed factors it cannot be found that the ventures would need for knowledge-development a more efficient management. In the highest rate was out raised the new markets, but in high proportion are referrals to the products and services. In this survey, none of the Hungarian enterprises refers to the importance of knowledge.

The results of the MMV survey agree with the observations obtained from the INNOTARS research. Therefore, the general consequence - the Hungarian enterprises do not see knowledge as a chance for growing its competitiveness or as a mean of handling with crisis management - seems to be proved as a penitence.

**Table no. 7.** The means of a firm for a long-term operation

With a new product or service on the market	33	46, 48%
New technologies are needed to be practiced	21	29, 58%
New markets are needed to look for	37	52, 11%
Costs should be reduced	20	28, 17%
Quality should be improved	11	15, 49%
The managing and organizational methods should be developed	20	28, 17%
<b>More qualified professionals are need to employed</b>	<b>14</b>	<b>19, 72%</b>
Credit is needed	21	29, 58%
Other	14	19, 72%
All the enterprises		All firms: (71) =100%

Table no. 8 further support this conclusion. We can get the answer to the question: “What kind of contribution could help the firms to improve their chances on the market?” Similar to the INNOTARS research, we can also deduce the fact from the MMV survey, that the enterprises are not based on the participants during their operation, who make good use of their knowledge. A key role use to play the customers and the partner organizations..

These economic parties/participants do not form the company’s operation with their obtained knowledge and also their products and strategies, but with their existed demands and needs, which the firms want to satisfy at a higher level.

The most important motivation factor for the Hungarian enterprises in their operation and inspiration for innovation or change-management is not knowledge-development itself, but the continuous adaptation to the customers’ demands and needs.

**Table no. 8.** What kind of contribution could help to grow the market chances of the companies?

<b>Chambers</b>	<b>24</b>	<b>33, 80%</b>
Educational institutions	9	12, 68%
Competitors	12	16, 90%
<b>Buyers</b>	<b>42</b>	<b>59, 15%</b>
Suppliers	15	21, 13%
Bureaus	13	18, 31%
Others	3	4, 23%
All enterprises		71 = 100%

### **Results - KPMG research program**

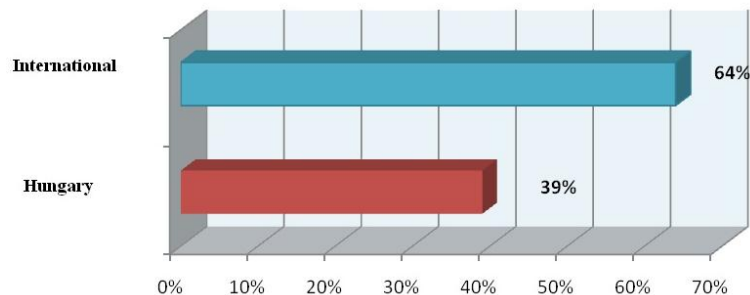
The KPMG has made a survey in 1998 and in 2000 about the issue of knowledge management and its situation, about the knowledge management practice in the huge companies. According to the research partners, in spite of the fact that it has just recently got into the business language, even more people share the opinion that in this approach hides such a power what can be a source of the sustainable competitive advantage.

The colleagues of KPMG have seen 18 more remarkable Hungarian enterprises, with a questionnaire which had already been used by a former international survey. The report has given us a relevant general idea about the Hungarian enterprises in the issue of knowledge management-development and in its adaptation, and about how they consciously deal with knowledge. By the chosen companies, firstly the top managers, the human and IT managers have been interviewed, who are closer to knowledge-management as an issue. Among the interviewed companies we can find public enterprises, companies in private sector in Hungarian ownership, international and national joint ventures, as well as firms participated in stock exchange and Hungarian subsidiaries of global international companies.

The most important question was in the survey, whether the Hungarian companies dispose of a strategy related to knowledge-management or not. In Hungary, only 38% from the interviewed companies dispose of it, contrary to 64% laid down in the international survey. From this result we can see the factors that backlog the

Hungarian economy competitiveness, compared with the developed countries. The table below made by KPMG also supports this statement.

**Chart no. 1.** Does the company dispose of a knowledge management strategy – comparison between the companies given a YES answer to the question?

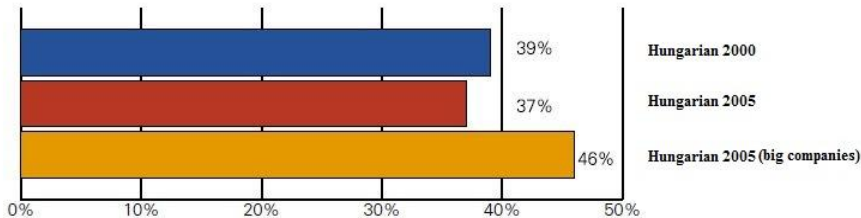


Why knowledge management is not effective for the Hungarian companies? One of the main factors is the lack of the cognition of the advantages related to knowledge-management, the lack of time and the fact that the colleagues do not want to share their knowledge with each other and with the management. It comes from the un-appropriate managing methods and from the lack of existence of the supportive corporate culture. By the half of the companies it has been proved that management is not committed enough to operate more effective.

Though these shortcomings were clearly shown by KPMG research that it does not mean knowledge for the companies, they could create competitive resources and successful crisis-management. The reason is behind the attitude, which is occurred by the competition with cheapness and it is very characteristic to the economy-philosophy of the Hungarian enterprises.

The KPMG has made a survey about the judgment of the inland situation of knowledge-management. It was made a survey in 2005, with the participation of 130 business organization. The comparative results are shown in the second chart recorded in 2000 and 2005. From the survey result it can be seen that compared to the 2000 results, the number of Hungarian enterprises has been decreasing.

**Chart no. 2.** Does the company own a knowledge-management strategy? – In rate of yes answers



### Conclusions

In this or that measure, any kind of knowledge – particularly the common knowledge about the same issues, determines the society's details in many ways. Finally, all kind of knowledge is determined by the society and its structure. Knowledge is such a power resource and such a competitive element, which can basically determine the performance of a company, moreover the performance of the completely national economy.

In our globalized world, knowledge, research-development and innovation are proved as such unique means, which can mean the outstanding possibility to be able to be competitive. Knowledge is a competitive advantage, a possibility for change and the most essential source of power in adaptation. We could be able to be ready for the continuously renewal with knowledge, expertise, creativity and to produce such products and services which can always create newer and newer values for our customers.

There are some countries and enterprises where it has already been recognized knowledge as an investment. Knowledge is today one of the most returnable form of investment, because we can improve our competitiveness with appropriate knowledge or at time of recession we can reduce the impacts of crisis at a certain level. Those countries, where more money is invested into this, have not suffered such big losses than those, which have tried to reduce the damages derived from the recession with cheapness. Knowledge is not only an effective and more competitive economy resource, but it's the possible mean of creating social capital.

According to Dalai Lama: Share your knowledge with others: this is the only way to be immortal. In the interest of success they are



equally needed resources as power for the economy, financing, the employees' satisfaction, the corporate culture, innovation, social capital and at the same time focuses on knowledge. Everything is connected to everything and we could perceive it in connection with knowledge-management.

The effective knowledge economy assumes the massive social capital, the excellent corporate culture and the employees' satisfaction. If knowledge is at a high level, it is easier to create new products and services, the employees are more creative and the problem solving is simpler and quicker. These abilities are more strongly needed when the company has to face with recession.

The competitive corporation is an agile company, whose real competitive advantage derives from its flexibility. In our fast moving world, the conformation became a fundamental assumption in order to be in competition. To be competitive means to have such factors as innovation, research – development, education training, quality etc., which are also the means for the reduction of the impacts derived from crisis.

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## **Corporate Governance - Key element in the Growth of Audit Quality**

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### **Abstract**

In the recent years, because of the many financial scandals, we have witnessed numerous debates concerning topics, such as government enterprises or aspects of participants reporting process. It is obviously that it is necessary to examine the corporate governance issues and those relating to the audit committee; that's why, even if the financial statements are the responsibility of the management, it's important to ensure the provision of information taking into account the principles of true and fair play, in the audit committees and through the external auditors.

**Keywords:** financial audit, corporate governance, audit committees

### **Introduction**

The concept of governance has versatile significance and it comes from many sciences. It is necessary to understand knowledge concerning the history of the national economies, to understand company law, organizational management, business finance, accounting, etc.

Practice confirms the need and role of corporate governance as a result of recent studies, because it was observed that those organizations that have adopted a governance model effectively perform much better against organizations that fail to do so.

### **Material and Methods**

This article aims to investigate a topical issue that is discussed more and more often in the economic literature. As a research method it was used the descriptive analysis, which attempted to study the role of corporate governance and audit committees in improving the quality of financial audit.

### **Literature review**

The paper is based on the analysis of the results coming from a relevant international research concerning corporate governance and audit committees, conclusions that in fact inspired the Romanian laws and regulations in that field, including here: Company Law no. 31/1990 as amended and supplemented, Governance Code (2009) issued by the Bucharest Stock Exchange and the Institute of Corporate Governance (IGC), Deployment Guide to Corporate Governance Code issued by BSE and IGC in March 2010.

### **Results and Discussion**

Currently, no modern society can be imagined without the existence of highly diversified organizations in which different individuals are associated with a variety of interests. These interests can generate potential conflicts between them. In terms of the business internationalization of the markets and the absence of strict rules, it may appear difficulties in the organizations, which requires the adoption of some measures, accordingly.

In Romanian, the term "governance" is synonymous with "management" and "leadership"; corporate governance or enterprise governance comes from the Anglo-Saxon translation of the term "corporate governance", designating the entire system by which economic entities are directed and controlled.

The literature abounds with various definitions. There is still some confusion about the concept of corporate governance. Nowadays, the definitions of governance have certain common characteristics regarding exercise levels, supervision and structures, ethical and social responsibility, mechanisms and instruments, all the rules and procedures of governance having the purpose of increasing the value of the organization.

Internationally, we note that there are several approaches in defining corporate governance, coming from different institutions or

organizations. Among them we believe that the full definition is that given by the Organization for Economic Cooperation and Development<sup>1</sup>. This definition summarizes in the best way the relationship of an organization with the internal and external environment, emphasizing the interaction between these environments and the entity's management structure. According to OECD, corporate governance means:<sup>2</sup>

- a set of relationships between the management of the company, the Board of Directors, its shareholders and other interest groups;
- a structure through which the companies objectives are set to achieve the monitoring performance;
- a system of incentives for the objectives of the Board and of the management, needed to increase the interest of the society and of the shareholders and to facilitate the monitoring; it encourages - at the same time - the entities to use resources in an efficient manner.

The subject - corporate governance has come under the spotlight following a series of failures in the private sector. That have created around the investors a sense of uneasiness, seriously shaking their confidence in how are managed both: large organizations and public institutions. The question arises whether these failures were due only to a lack of integrity in management or were consequences of the gaps in the legislation.

In response, the government's bodies made important changes concerning the legal sanctions, introducing ethical and transparent policies to be adopted by the companies.

The government's role is to provide a framework for the activities of the companies and institutions, identifying and achieving common interests for all the involved parts. From here emerges the idea that governance especially has some socio-economic structure in which an important role occurs the following entities:<sup>3</sup>

- joint stock companies, in which the Government ensure that shareholders are not only simple investors;

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<sup>1</sup> The abbreviation used in the literature for this organization are: in English - OECD (Organisation for Economic Cooperation and Development) or in French OCDE (Organisation for Cooperation et de Développement économiques);

<sup>2</sup> OECD Principles of Corporate Governance, 1999

<sup>3</sup> Aslău, T., Almasi, R., Internal Audit, 2009, Arad, Aurel Vlaicu University Press, pg. 82

- public institutions, such as state and local authorities, which must ensure the rights of the citizens;
- social organizations, ensuring both: respect for the contributors and for the beneficiaries of social action;
- various other legal associations, which aims, through the act of governance, to ensure the respect for all the members.

In any of these structures, the corporate governance is aimed primarily towards performance increase, in harmonization with the interests of various groups. Thus, corporate governance has many socio-economic benefits.

There is no single model of corporate governance. Each structure is unique and consequently.

A corporate governance model that have to be implemented is influenced particularly by the company's characteristics<sup>4</sup>. In other words, corporate governance model differs from one country to another, depending on the nature of the society and its development. However, each governance model should consider at least four principles:

- shareholders' rights and an equitable treatment;
- the role of interest groups (stakeholders);
- board and management oversight;
- transparency and disclosure of information.

In our country, the concept of corporate governance has emerged recently and it is only visible for about 9 to 10 years. There are serious efforts to generalize corporate governance in Romania.

The Romanian corporate governance can't be analyzed only in terms of the evolution of political, legal, economic and social context of the transition from the centralized economy to a market economy; the Romanian companies' management is strongly influenced by the ownership reform.

Therefore, the national legal framework allows both: tier management systems specific to the Anglo – Saxon model and the German model specific tier. However, in our opinion, the Romanian model of corporate governance is a combination of the two models established at EU level.

We believe that legislation may provide a potential basis for solving many problems that Romania still has in terms of corporate

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<sup>4</sup> Bowman, B. Principles and recommendations proposed in the new Code of Corporate Governance, Journal "Financial Audit", no. 10/2010, pg. 52

governance. We also note the progress relating to the management of the Romanian companies reform, leading at least to a substantial improvement of the legal framework. The governance models must be developed to include those additional levels regarding liability, as a result of financial audit.

We also consider that different systems of governance can have a significant influence on the role and financial audit quality, as evidenced in countries where the predominant entities with diversified ownership structure have a favorable perception of the role and usefulness of the audit services. In other words, understanding different systems of governance can have a significant impact on the understanding of the financial audit.

Effective corporate governance models assign important roles to the auditors, particularly in matters relating to the financial reporting transparency and the monitoring of internal controls. In these circumstances, the role of communication between auditors and those with governance is obvious.

Communication is extremely important because it supports the understanding of the audit issues, developing constructive working relationships between the independent auditors and those charged with the governance. Good communication between the two parties may assist the auditor in obtaining relevant audit information and also assist those charged with governance in carrying out their responsibilities in overseeing the financial reporting process.

The standard that sits in the foreground relationship communication between the auditor and those charged with governance is ISA 260, "Communication with those charged with governance". For this, the auditor must first identify those persons that are charged with governance. According to the legislation, in Romania they may be the administrators of the entities, the directorate and supervisory board. In both cases, these entities are required by the law to audit the annual financial statements and should establish an audit committee.

Also, the auditor should use professional judgment in identifying those charged with governance taking into account the specificities of the governance, of the entity, the circumstances of the engagement and any relevant legislation.

A good governance of an entity requires also a good cooperation between the supervisory boards, the management, the managers and the audit committees. Regarding the financial reporting process, they are

primarily responsible the supervisory board, the managers and the external auditors. The role of the audit committee is to inform the Board about the accurately of the financial reports and not to make decisions. Eventually, the audit committee can guarantee the accurate and complete financial information.

In our opinion, the role of oversight committees and audit committees in the corporate governance process should be a key one.

Given the composition and responsibilities of the audit committees, they can be a useful ally for the shareholders, not only in matters of financial reporting, risk monitoring of the internal control and audit. However, to achieve this important role within an entity, the audit committee members must be independent, having also an excellent training.

### **Conclusions**

We consider absolutely necessary to continue the efforts concerning the alignment of the Romanian corporate governance practices with the established internationally standards, deleting the ambiguous and contradictory provisions.

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## **Analysis and risk Management. Risk Management implementation in the Romanian Public Sector**

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### **Abstract**

The complexity of a public service corresponding to the demands of the nowadays society and limiting the necessary resources for the functioning of the institutional environment determined the changes of the vision for the management in public system regarding the risk and implications of it in realizing the objectives on an entity inside the public system, in Romania.

**Keywords:** risk, risk management, probability, impact, risk exposure, tolerance to risk, internal control

### **Introduction**

Daily experience shows that the economy and the hazard are statements strictly tightened and the try to motivate in detail this statement would be useless because the evidence is overwhelming.

Each economic activity assumes successive choices which affects even the decider person as many other people, and from this reason the formal theories in this direction becomes more and more scientific fundamented.

Existing since 1921 (Frank H. Knight) concerns regarding uncertainty and risk in the organizations activity, is surprising that until the occurrence of probabilistic economy (T. Haavelmo 1942), economic theory assigns for the economic phenomena and behaviors a determined

route. After that, economic model started to be built on uncertain type elements, and today the widely opinion among specialists is that the managerial decisions, most of them, are more or less affected by uncertainty and/or risk.

### **Material and Methods**

Analysis and management of risks at institutional level in Romania impose a matrix construct for risk evaluation for realizing the risk profile and internal control measures that need to be done. In this case, the inherent initially identified risks should be further classified under the tolerance limit agreed in the organization.

### **Literature review**

Documental research for defining the term for risk and risk management in Romanian public system is realized with the support of The Ministry of Public Finance – Central Unit for Harmonizing of Financial and Control Management Systems. It was studied also the Romanian legislation concerning risk management as an integrating part of internal control standards implemented by OMFP 946/04.07.2005 in the public institutions in Romania.

Also it was taken into account the international literature concerning the risks management developed in public system. In this field, it was taken as reference the Orange Book – Management of Risks Principles and Concepts (HM Treasury 2004).

### **Concept of risk**

The humanity realized from ancient times that risks exists.

In a first (classic) approach of the concept, it is identified a negative dimension of risk seen as a loss, a fatality, risk notion being exclusively limited to mathematical wait of losses which can appear in the case of one possible variant. Now, this exposure is useful only in the condition of identifying of pure risk, when there are low chances that the decider, following the application of one decision, to record a loss, without the chance of a gain.

In the last years, it is observed the evolution of tendencies for defining the concept from negative sense (risk=danger), to positive valence, based on experience, professionalism and anticipation capacity, which treats the risk as an event which can be generated by the

environment or organization, with rapid influences (negative or positive) on the activity.

In the present, the concept of risk takes a bigger importance, so the human factor sensibility to risk becomes higher, defining the risk as representing the assumptions of actions which will be made in the future. Therefore, top managers do not agree with a passive acceptance of risks and considers that they ought to seek the best methods to control so that goal achieving to be realized in optimal conditions.

As a conclusion, the risk is a multidimensional concept whose level cannot be reduced to a single element, to a number. It is important for each organization to establish an acceptable level of risk to be able to assume. The acceptable level of risk referees to the maximum level which can be accepted without harming by failing the proposed objectives.

### **Management of risks**

Over the years, the existence of a wide range of risks generated continuously concerns in efficient managing of risks. Such, there were created procedures and modern instruments for exposal control of entities to different risk factors in order to minimize the risks and turn to account the opportunities.

Therefore, in the literature appeared the notion of 'risk management'. If the concept appeared first in '50 in some enterprises in Australia and New Zealand (as integrant part of insurance mechanism), the end of 20-th Century and the beginning of 21-th Century were marked by appearing of numerous publications and standards regarding the risks, these referring especially to the activity in private sector.

The first standards recommended to the organizations from the public sector and which regarded the negative and/or positive consequences of risks on short and long term was elaborated in 2002 by specialists from United Kingdom (The Institute of Risk Management; The Association of Insurance and Risk Managers; The National Forum for Risk Management in the Public Sector).

According to this standard, management of risk in an organization should be realized in a continuous process related to its strategy. The process will be implemented by the manager with the help of all the employees. The main lines of the standard are: the overview of the organization, the improvement of decisional process through planning and prioritize objectives and activities, optimizing the

operational efficiency, contributing to efficient split of capital and resources, reducing the volatile unimportant zones of business, protecting and improving values and company image.

Due to internal and external diverse factors which act on the environment in which the organization behaves, the specialists implemented The Management Standards ISO 31000:2009.

In our days, the platform of this kind of risk management integrated in the entire organization structure can be structured as follows: 1. Identifying the risk profile of the organization; 2. Operational risks management to each level of the organization; 3. To put into practice risks management to each level of the organization; 4. The developing of risks management.

As presented, the modern concept of risks management implemented in all organization processes, is in fact an answer (based on experience) to the uncertainties of environmental factors and to the necessity of strictly controlling the risks to which an organization is exposed to.

### **Implementing a risk management methodology for the Romanian public sector**

Starting from scientific researches regarding risk management, the author of this paper proposes a critic analysis of the risk management implementation in the Romanian public system.

Due to Romania acceding to the EU and due to the fact that it is necessary to have reasonable risk management, in the last years, public institutions realized the necessity of a risk management system with all the integrated processes which are realized.

Actually, it starts from the premise that, the main objective in the public sector is a public service that must answer to the contributors needs. This objective is influenced by the accuracy of data and by a lot of internal or external factors that generate uncertainty in reaching the objectives. Sometimes these cause negative consequences over the public service environment.

In the Romanian public sector, risk management is based on the experience of other countries such as England, well known as the promoter of modern principles in risk management; France, a country based on an efficient principle of public management, promoted by EU and Holland.

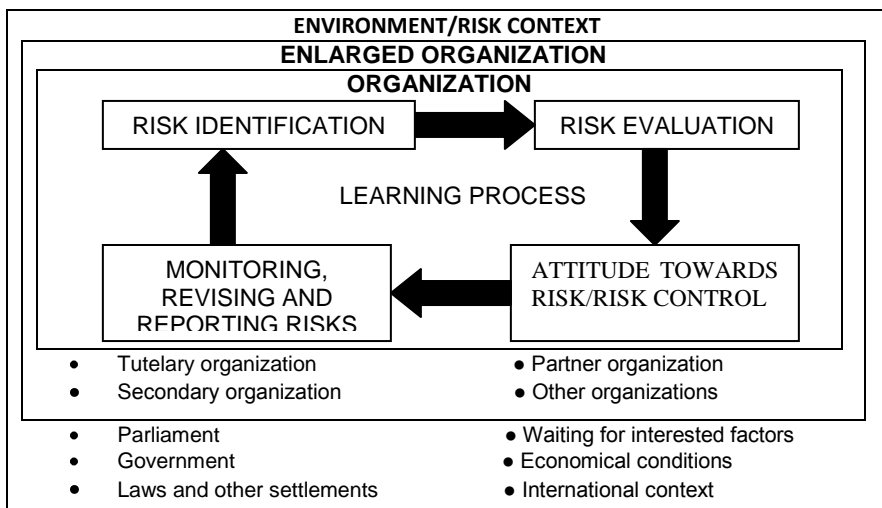
Starting from the experience of English specialists in defining risk management for public sector and its standardization at international level, The Romanian Ministry of Public Finance – Central Unit for Harmonizing the Financial and Control Management Systems, created the legal frame for the development of an efficient risk management.

Through OMFP no. 946/04.07.2005, Romania created the legal frame for implementing the risk management as a standard of internal control, as a uniform and coherent model of internal control with which are evaluated the internal control systems (implemented by public institutions managers).

Risk management is seen under a traditional form based on identification and evaluation of risks, controlling the risks and monitoring, revising and reporting risk state.

The managers will implement a system of internal control based on identified and evaluated risks and risk tolerance.

In fact, it is about implementing the English model of improving a public sector to manage risks and uncertainty. The management it's not realized in isolated organizations, but at country level.



In the following, they are studied the main lines of the process for risk management necessary to be integrated in institutional culture in Romania. This process suppose the following steps: risks identification,

evaluating the risks, identifying the tolerance to risk, the answer to risk-controlling the risks, revising and reporting the risks

a) Risks identification

In any organization, the process of risk management starts with risk identification at every level referring to the organization's objectives. In fact, it's the first step to establish the kind of risks may occur.

The identification activity can be an initial one typical for a new organization or for a new process in an existing organization and it can be a permanent one for an organization which has an active process of risk management.

There are a few important rules in risk identification and definition: risks are an uncertainty, or more exact are probabilities for an event to happen; responsibility in solving identified difficult problems (crisis); the events with no impact to the organization's process are not risks; not to identify certain events; not to define risks by denying the objectives; use the cause and effect principle upon objectives in risk identification; treat differently inherent and residual risks; broach the risks with suitable instruments (internal or external listener for risk analysis); group the risks.

With regard to the above mentioned principles, in this stage, the risk management must be realized objectively.

b) Risk evaluation

The second step, after the risk identification is the evaluation of them. In fact, it is the evaluation of risk importance referring to the activity where it was identified. Usually, we do that on a numeral scale (especially for financial risks), but there are risks that we evaluate from a more subjective perspective (image risk, credibility risk) and because of that, the evaluation is more an art and less a science.

We do this evaluation of risk importance to can prioritize the next steps for a proper control of risks. The aim is that risks must be between reasonable limits.

In the end, risk evaluation is done by two essential indicators. We are talking about the probability of risk attaining and its level estimation, and the impact of risk attaining over the objective of the organization. Those two indicators combined, represent the organization's risk exposure to its environment.

In this stage appears the organization's risk awareness. The limits of the evaluation system enable framing the risk as insignificant,

minor, moderate, major and sever. In other words, a matrix model based on the two indicators, probability and impact to evaluate risk is, in fact, the key factor, to quantify the risk exposure of an organization and to situate a risk potential due to the maturity of organization management.

It is recommended to use a 3 level risk evaluation classification scale, in the implementation stage. Applied to all organization levels, it is necessary to build a 5 level risk evaluation classification scale, in order to have a strong internal control.

<b>IMPACT</b> Very high High Medium Low Very low	VH - VL	VH - L	VH - M	VH - H	VH - VH
	H - VL	H - L	H - M	H - H	H - VH
	M - VL	M - L	M - M	M - H	M - VH
	L - VL	L - L	L - M	L - H	L - VH
	VL - VL	VL - L	VL - M	VL - H	VL - VH
<b>PROBABILITY</b>					
	Very low	Low	Medium	High	Very high

The limits in between a risk is framed from probability and impact points of view, is quantified by every organization, due to risk nature, risk “documentation”, organization usual risk and management interest in risk analysis.

c) Risk tolerance

Risk tolerance is a level of risk that an organization is willing to take without damaging its objectives. Risk tolerance can be seen either an opportunity or a threat. As an opportunity, risk tolerance concept is the limit till an organization is willing to expose itself in order to obtain benefits. As a threat, risk tolerance concept is the limit that an organization must reach for the identified risk, not to represent a threat for the organization’s objectives.

Because risks are generally regarded as threats, and if they materialize the objectives might be harmed, risk tolerance, as the main responsibility of risk management, is in fact, a cost problem (if we talk limited financial resources). Therefore, risk tolerance for any

organization is the level where it is possible to realize a balance between risk cost control and risk cost exposure to a materialized risk.

In practice, tolerability level is realized from top to bottom, from top management to operational level, regarding the major objectives of the organization. Based on top management references, the reasonable tolerance is sent to the second level of management. This second level of management establishes organization limits to risk exposure for every other organization level. So, all the risks with a bigger risk exposure than established limits are identified. It is possible then, to perform internal control actions to situate risks inside tolerability limits. If risks aren't between the established limits, they are sent to the next superior hierarchical level, for them to either take the decision of direct managing of risks or ask for supplementary measures of internal control.

After the assessment of these limits, next step is to proceed to a thorough analysis of costs and benefits, settling new adjustment if necessary. These new adjustments (more costs) of risk tolerance and insufficient resources ask for a hierarchy of risks based on priorities and aim for readjustment of tolerance limits for other, less important risks.

All the things mentioned above are useful in the registry of risks of an organization, as follows: describing risk/inherent risk (probability, impact, display); internal control measures/residual risk (probability, impact, display).

d) Risk response – Risk control

After the organization identifies and evaluates the risks, after the organization settles the tolerance limits, it is necessary to settle the response time for every risk.

The risk response depends of the nature of risks from the possibility of control perspectives. In fact, we talk about the answer to the next questions: Are the organization able to control the risks? If yes, is the organization able to control the risks until a satisfactory level? If not, can the organization externalize the risks or the activities generating the risks?

In risk theory we identify a few alternative strategies that public institution managers can adopt: risk acceptance (tolerance), risk avoidance, risk transfer, risk attenuate, difficult situation treat.

e) Revising and reporting the risks

Revising and reporting the risks is done for two reasons:



- Monitoring the changes of risk profile due to the implementation of internal control instruments and changes of circumstances who favor risks;
- To obtain assurances regarding risk management efficacy and to identify the need for future measures

Revising processes must be applied if the risks persist, if there are new risks, if impact and probability of risk are modified, if internal control instruments used are efficient, if some risks must escalate to superior levels of management

The results of the revises must be reported to ensure a sequel monitoring of risks situation and to see the major changes that call for a priority change.

### **Conclusion**

Through this debate, the author wants to highlight the necessity of implementing an appropriate mechanism of risk management in the Romanian public system. The high level of objectives set by the quality of public services that must answer to contributors needs and the limited level of resources from public system, bring to a major exposure of the organization to a series of risk factors. Therefore, a mechanism of risk management able to minimize public system exposure under the tolerance level must be one of the major concerns of public system management.

Therefore, starting from the idea that now, the Romanian public system does not have an appropriate risk management concordant with the trend dictated by the complex activities and diverse factors, this paper wants to loom a minimal elementary construct which every Romanian public institution should develop and adapt to realize an optimum risk control.

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## **The Quality Performances of the Products – A permanent Preoccupation of the Companies**

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### **Abstract**

A very important element is for one to understand the fact that products satisfy certain consumer needs. Thus, the offering company, knowing consumer exigencies, will orient its activity according to them, the role of *the primordial character of the request* being essential in the strategic orientation of the company.

Under the conditions of globalisation and the increase of the importance of information for the modern consumer, the people's exigencies regarding the household appliances will be more and more focused upon the unrestricted access to information, one of the premises of the international society.

**Keywords:** product, intelligent house, efficient refrigerators

### **Introduction**

Companies are obligated nowadays to cope with the present economic and social environment, the integration of marketing in their activity being, thus, the most appropriate way for a modern and profitable management. Moreover, they must take into account the fact that, at this moment, there are problems related to:

- the accentuation of competition at a global level;
- the existence of an economic stagnation or recession in some countries;

- complex changes at the level of consumption markets (the increase of the number of employed women, smaller families, the diversification of lifestyles, late marriages) and of business markets (the superior quality of goods, their faster delivery, the reduction of the product lifecycles), that accelerate the dynamism of modern market;
- the increase of the exigencies regarding the level of training of the work force;
- accomplishing an integrated system of quality and environment, correlated with the norms for security and occupational health;
- the increase of the differences between the population with large incomes and the one with small incomes;
- the reduction of the work force in many sectors, as a consequence of automation, robotics;
- the transition to the market economy of the Eastern Europe countries, a process that is complex, difficult and long;
- creating a favourable company image.

Marketing will give managers the specific techniques and instruments to be able to get a market study that is as complete as possible, so they can afterwards establish a certain strategy that offers the company a favourable position on the market and has a certain competition advantage. The specific marketing activities (market research, the analysis of consumer behaviour, the policy regarding the product, price, distribution, promotion etc.) will be correlated with all the other business activities (research-development, production, commercial etc.), all being applied by the management functions (planning, coordination, execution, control, regulation).

The offered products and services, the improvement of their quality, are a permanent preoccupation of the companies in order to establish the marketing strategies. An element of great actuality, harmoniously integrated in the future society and that must keep in mind is the development of home automation.

### **Results and Discussion**

Home automation represents a stage in full ascension, which leads to the increase of the quality of life and the rational use of the existing resources. One prefigures the gradual transition to automated electronic devices that can be controlled and commanded from distance,

due to the artificial intelligence they will possess and the ability to communicate through a network.

Modern man has rapid access to information from all over the world, as a consequence of the new technologies from the area of telecommunication, communication environment, the types of transmitted information and the equipments. The technologies of information and communication will affect the individual way of life, having a powerful impact upon work, education, science, health, spare time, transportation, environment and also other areas of daily life. The home is the environment in which a large part of our life takes place, being necessary to integrate it in the global system of the information society. The “intelligent” house will offer multiple connections to information highways, so, alongside the phone line, radio waves, TV cable, new means of communication will be available, such as optic fibre or infrared radiations, which will be used for communication. The intelligent house will offer access to electronic services, which are: telework, telemedicine, teleeducation, telegoverning and e-commerce.

Connecting the house to the information highways will also give the possibility of supervising and controlling the household appliances and devices from distance.

Due to the recent improvements, through the use of specialised microprocessors and of some concepts that are specific to automation (such as feedback and fuzzy logic), the household appliances, based on the information that is received from sensors, will be able of establishing their own optimum functioning regime.

The use of specialised microprocessors that are based on fuzzy logic is limited only to some groups of products: washing machines, vacuum cleaners, microwave ovens.

In conclusion, the apparition and application of home automation represents a premise for the increase of the quality of life and the change of lifestyles. Microprocessor systems, that reduce human intervention at minimum, are at the basis of more and more household appliances. Home automation also brings the possibility of supervising all the household appliances from great distances, through the communication networks.

Currently, the fierce competition from this area causes the producers of household appliances to organize their own laboratories of research and innovation, in order to discover and create new models that can be more and more efficient and attractive regarding their qualities.

All the companies that produce refrigeration equipment have common preoccupations regarding the following quality characteristics: no Freon; “No Frost” system (without ice – the cooling is achieved using streams of cold air, that do not allow the forming of ice in the refrigerator); a separate control for the refrigerator and freezer; electronic temperature control; LCD display; automated defrosting; acoustic and optic alarm when the interior temperature is not achieved and when the door is open for more than one minute; a warning signal for power shortages; programming the temperature according to the food that must be preserved and that also indicates the deadline until which it can be eaten; reversible doors; interior illumination; shelves that are light, transparent, adjustable etc.

In order to exemplify the newest and most modern particularities of household appliances, we have selected a group of products, namely refrigeration equipment.

The south-Korean corporation *Samsung* presented, at the Consumer Electronics Show (CES) in Las Vegas, a refrigerator that allows the clients to access the Twitter micro-blogging site.

The clients can visit the portal and can also use the eight inch multi-touch screen in order to access the Pandora music service or Google Calendar, according to *Daily Business*, citing Mashable. This refrigerator that is considered revolutionary allows the members of the family to leave messages check the temperature outside or inside the refrigerator or access culinary recipes.

The Arctic company, a part of the Arçelik group (Turkey), through the *Beko* brand, invented an ingenious technology, *Smart Blue* and integrated it into a new and complete variety of household appliances, which includes refrigerators, washing machines and dishwashers. The *Smart Blue* technology is based on the blue light which, integrated in a unitary set of functions and programmes, significantly improves the quality of life.

The *Active Fresh Blue Light* function of the *Smart Blue* refrigerator, by the specifics of the blue light, which is permanently active inside the fruit and vegetable compartment of the refrigerator, maintains the photosynthesis effect in that area and preserves the freshness, vitamins and nutritional properties of the fruits and vegetables for a longer period.

The *Infinity I-Kitchen* refrigerator, launched in Brazil by the *Electrolux* company, has the *touch screen* on the door as a particularity.

The interface of the *touch screen* of this refrigerator is efficient due to the GNU/Linux operating system. Even back in 1999, the Electrolux Company launched *Screenfridge*, a refrigerator that helps the user maintain a detailed record of what he buys the menu for dinner, the food that is still left in the fridge. This refrigerator can also work as a message service for the entire family. This household appliance can be considered among the first *intelligent household appliances*.

Furthermore, Electrolux has organized its own design laboratory, through which it annually attracts talented young designers from across the world, as a result of organizing a competition for innovations. Consequently, during the last few years, *Electrolux* has managed to amaze the world with some concepts that integrated “entertainment” devices and online tools, such as *Rendez-vous*, *Volare* and *Heart of the Home*.

In 2010, Electrolux presented the concept of an application that supports the user when trying to control nutrition, through which the users can observe the quantity of food they buy and reduce the quantity of unused food.

Moreover, Electrolux is involved in several countries in projects that test systems for intelligent household appliances, respectively energy systems that can communicate with the appliances in order to detect and automatically stop consumption in the peak periods of the day.

The *Infinity I-Kitchen* refrigerator was very well-received, both by the tech-savvy community and by many inhabitants of Brazil that also acquired it. This refrigerator follows the trends in the technology of household appliances and has a special feature the application that contains over 600 sophisticated recipes that were published in collaboration with a famous Brazilian magazine. The menu is grouped in seven different categories, from hors d’oeuvres and main courses to light menus and cocktails, offering the users the flexibility of deciding their own menus for the meals.

Again with the help of the *touch screen* panel, anyone has access to programs such as *Notes*, *Calendar* or *Telephone Information*. The display may also work as a digital frame with a slide show. The refrigerator also has intuitive commands and a versatile compartmentalization. The “Express” space can be used to cool drinks and desserts a lot faster, while the “icemaker” produces ice without the need for hydraulic connection.

This product was inspired by the “*Electrolux Infinity*” refrigerator, which received awards in three international design competitions: “iF Design” (Hanover), “Good Design Award” (Chicago) and “Brazilian Home Museum” (Sao Paulo).

Using the *Whirlpool* refrigeration equipment, as a consequence of applying the 6<sup>th</sup> *Sense for Freshness Control* technology, consumers can have their food as fresh as the day they bought it for up to four times as much. Through this new freshness control technology, the refrigeration at a correct humidity is guaranteed in the entire interior, giving the possibility of keeping food fresh up to four times as much.

The 6<sup>th</sup> *Sense for Freshness Control with the Activ0° System* from *Whirlpool* is available both for individual refrigerators and the incorporated ones.

Activ0° is a system that is dedicated to meat and fish. Two sensors ensure a constant temperature of 0°C, the ideal level to keep the taste, aspect and nutritional value of these types of food.

*Whirlpool*, along with *Microban*, the market leader in antibacterial solutions, has developed an antibacterial system of air filtering. It is the best available technology, which protects food and helps remove bacteria and odour. This innovation is available in all the products with ventilation or Multiflow system.

The filter consists of a polymer layer that has the *Microban* antibacterial system.

The antibacterial filter has been successfully tested and approved by a famous German laboratory – “LGA”.

Could we imagine replacing the classical refrigerator with shelves and a freezer, with a special gel that can keep food fresh with almost zero energy consumption?

The refrigerator of the future has become a reality. A Russian designer, namely Yuriy Dmitriev invented the *Bio – Refrigerator* that suspends and cools the food that was inserted in the special gel. The food is inserted into the gel and it remains fresh for as long as necessary. The wonder gel manages to preserve the food using luminescence (light that is generated at small temperatures), has no scent and is not sticky. Along with these qualities, the refrigerator can even be hung from the ceiling, thus becoming an extremely interesting design piece.



### **Conclusion**

The technologies of information and communication affect the individual lifestyle, having a powerful impact upon work, education, science, health, spare time, transportation, environment and other areas of daily life. The home is the environment in which a large part of our life takes place, being necessary to integrate it in the global system of the information society. Creating some household appliances with the highest performances will ensure in the future a growth in the individual degree of comfort and security, a high level of the quality of life and of the people's degree of information.

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## **Aspects of the Capital Markets' Development from the CIS Member States and Republic of Moldova**

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### **Abstract**

Evolution of capital markets is an important process for the all economies, irrespective their degree of development, while the trends emphasized during the last decades marked some common tendencies of evolution. Practically, most of the tendencies manifested on global capital market are also relevant for the securities market of the CIS member states, still, one of them possessing a more relevant character (capital concentration and centralization; regulation and deregulation of capital market; capital market informatization), while the other ones – a lower degree of relevance (ascension of institutional investors on capital market; implementation of financial innovations; capital market integration and international cooperation; compartmentalization of secondary capital market and development of alternative secondary market etc). This article emphasizes some of the tendencies specific for the development of the capital market from the CIS member states and the Republic of Moldova.

**Keywords:** capital centralization, capital concentration, regulation of capital market, privatization, institutional investors, institutionalization of capital market, stock exchange, capitalization of stock exchange, financial integration

### **Introduction**

At any stage of the economy's development, capital market identifies some directions of its evolution and traces some tendencies.

At present, the main principles of global capital market are represented by the following directions: capital centralization and concentration, institutional investors' ascension, informatization, integration of capital markets and international cooperation, globalization, implementation of financial innovations, securitization and reciprocal penetration on other market' segments, disintermediation, regulation and de-regulation, compartmentalization of secondary capital market and development of alternative secondary markets.

Practically, most of the tendencies manifested on global capital market are also relevant for the securities market of the CIS member states, still, one of them possessing a more relevant character, while the other ones – a lower degree.

This work emphasizes the most important tendencies, which had a pronounced character in the development of capital market in the CIS member states, as well as in Republic of Moldova. Thus, the paper is structured into 5 sections that relate the general developments and evolution within: capital concentration and centralization processes, institutionalization of capital market, securities markets' regulation within the process of EU integration, reduction of stock markets' capitalization. All the most important statements are totalized in the section of general principles of capital markets development within the CIS member states. Conclusions and references end this article.

### **Capital concentration and centralization processes**

Capital concentration and centralization processes on the capital markets can be considered as premises of *investors' institutionalization*. Thus, in Republic of Moldova, as in the majority of another CIS member states, *the processes of capital concentration and centralization in form of securities, was launched within the process of mass privatization of state ownership, at the beginning of 90s*. Thus, a good part of capital was concentrated within population (over 3.2 million citizens of the Republic of Moldova), while the privatization model being based on the following principles, forms and methods:

- Transfer to collectives for patrimonial vouchers the volume of up till 20% of ownership;
- Privatization for cash, with participation of foreign investors;
- Free transfer (up till 50%) from the ownership of processing enterprises to suppliers of raw materials.

In such a way, during the 1993-1996 period, more than 2235 Moldovan companies from industry, trade and social service sectors, as well as agricultural branch, were privatized for patrimonial vouchers.

At the same time, as a result of the privatization process, the first type of owners appeared – companies with a big number of shareholders, whose stocks were in free circulation. As a result of privatization by investment tenders (1998), the second type of owners appeared – companies with a sole shareholder and an insignificant number of „external” shareholders.

*The capital concentration process in Moldova* in conditions of mass privatization determined the creation of the securities market. Already, at the end of 1997, the total volume of shares’ issues on the capital market exceeded 6.8 billion Lei (total volume of shares’ issues from 1992 till 2009 registered 21.2 billion Lei). In 1992, first closed joint-stock companies (JSC) were created. The given period can be considered as the start of the national primary securities market development.

In short time, professional participants institutions of securities market were created, while once with the approval of The Law of financial institutions of Moldova (1995), the professional activity on securities market was allowed to commercial banks.

Appearance of various professional participants on the securities market (trust companies, independent resisters and brokers), the respective public organizations: Joint-Stock Companies Association, Professional Representatives Association led to the accumulation of work experience with securities, while the existence of different issuers and shareholders (having a different interest) on the capital market forced the creation in 1995 of the Stock Exchange – the institution with the role of activity’s equilibration and regulation’s insurance of capital market.

Thus, institutionalization of capital market took place by the appearance of market institutions, professional participants, issuers, as well as investors, including institutional investors.

### **Institutionalization of capital market**

The *phenomenon of institutionalization* should be considered from the level of organization of different companies, mostly determined by the increase of capital mobility.

Within the *CIS member states*, the increase of number of institutional investors, which represent the main type of investors from the securities markets, determines the growing demand for financial instruments (see table 1).

**Table no. 1.** Number of institutional investors and volume of assets from the CIS member states

Country	Number of institutional investors		Volume of assets, thousand USA Dollars	
	At 01.01.2008	At 01.01.2009	At 01.01.2008	At 01.01.2009
Armenia	66	68	2.713	3.615
Belarus	61	65	25.400	51.200
Kazakhstan	527	588	2.960.000 (580.000)*	3.690.000 (1.140.000)*
Kyrgyzstan	6	8	-	1.224,9
Republic of Moldova	<b>At present, none of active institutional investors exists</b>			
Russia	1.430	1.595	32.089.984	22.707.919
Tajikistan	16	17	13.435	17.521
Ukraine	796	1.177	4.976.583	7.865.768

\* in parenthesis - volume of investment assets

**Source:** adapted by authors in base of data from [www.cnpf.md](http://www.cnpf.md)

Analysing the data of table 1, it can be mentioned that the reduction of number of institutional investors' assets during 2008-2009 was attested only in Russia. Practically, all the countries registered an increase in the number of the professional participants on securities markets, representing the improvement of market's infrastructure (see table 2).

It is to mention that the most dynamical growth of the number of professional participants was registered in *Armenia* (nearly 3 times) and in *Ukraine* (by 19%), due to the increase of the number of organizations

that perform the trust, brokerage, dealer, investment portfolio management activity.

In *Moldova*, the number of professional participants on the market attested a reduction (by 20%). Thus, if the number of professional participants during the period of national securities market development (middle of 90s) exceeded 140, in 2010, it was limited only to 44 organizations, without considering investment funds, which, at present, are in process of liquidation. Practically, the securities market does not possess force operators, as institutional investors – efficient administrators of investments.

**Table no. 2.** Number of organizations that perform a certain type of professional activity on securities market<sup>1</sup> from CIS member countries

Country	At January 1 <sup>st</sup> 2008	At January 1 <sup>st</sup> 2009
Armenia	29	87
Belarus	171	179
Kazakhstan	212	217
Kyrgyzstan	72	81
Republic of Moldova	68	55
Russia	3.670	3.710
Tajikistan	4	7
Ukraine	1.631	1.942

*Source:* adapted by authors in base of data from [www.cnpf.md](http://www.cnpf.md)

The most representative institutional investors on the Moldovan capital market appeared in conditions of privatizations and were privatization investment funds. Although already by 80s, the tendency of institutional investors' ascension on the capital market was strongly pronounced; in *Moldova*, this tendency still now is poorly manifested. The legal attempt to create an investment bank (in 1991) had no success. The activity of other institutional investors (like non-government pension funds, insurance companies etc.) on domestic capital market is not essential and poorly sizable, although legal provisions relating to them exist.

<sup>1</sup>In case if any organization doesn't perform some of the types of professional activity, this organization is considered in this table according to each type of activity

The concentration and centralization processes on the capital market were also extended over the professional participants. This tendency was manifested through: consolidation of professional participants' organizations, augmentation of the volume of managed funds, extension of the assortment of rendered services, as well as through the minimization of their number in conditions of a strong competitiveness.

### **Securities markets' regulation within the process of EU integration**

Cooperation among CIS member states in the domain of securities markets' regulation offers the possibility of exchange the experience and contributes towards the improvement of the principles of the activity and the continuous development of stock exchanges. The necessity of such collaboration is explained through the possibility of re-distribution of investment means and credit flows from the CIS markets and other developing ones towards countries and financial instruments with a low level of risk, which corresponds to the process of globalization, characteristic to the global capital market.

In *Republic of Moldova*, the process of national capital market integration into the European Union financial sector is associated with conformation of national legislative framework towards the European Union directives and foresees a radical restructuring of market infrastructure. Majority of directives establish „minimal standards” that should be practiced by member states, each country having the possibility to fix more severe provisions on its territory. Thus, the scope of directives is to homogenize and create certain common standards, regulating only those aspects of the capital market that are connected to relations among different states. A major part of regulations is mostly related to the legislation of each member state, but that are not contrary with the Community legislation.

For the achievement of this objective, *the Strategy of non-bank financial market development for 2011-2014* was developed, which purpose is the conformation of the national legislation in the domain of non-bank financial market to European standards, and, as a result, the realization of the European integration objective, while the principle domains of development stipulate the adjustment of national policies, towards the best practices at international level. Thus concrete legislative

measures were elaborated and created<sup>2</sup> in relation with the regulation reform, having as major objective the *development of a well regulated and transparent market, financial stability and implementation of a new architecture of non-bank financial supervision.*

At the same time, in Moldova, as well as in other CIS member states, a less restrictive tendency of market regulation is attested for its significant liberalization, expressed through: liberalization of *transactions* with securities (for ex., existence of legal provisions on using multilateral trading systems (MTF)), possibility of introducing new financial instruments (derivatives, municipal bonds etc.), attraction of new market operators with a high potential, inclusively the ones from EU, as well as the access of national operators on European markets, while the existent legal framework is going to be substituted with the one specific to European standards.

### **Reduction of stock markets' capitalization**

Another tendency characteristic for the development of the capital market from the CIS member states (from the end of first decade of the XX-th Century) is the diminishing of liquidity, limitation of access to credit and investment resources, increase in credit costs, worsening of financial estate of many issuers, reduction of securities' costs traded on national stock exchanges, as well as, as a result, the reduction of stock markets' capitalization (see table 3).

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<sup>2</sup>Appearance of a whole set of legislative acts' projects like: Law on National Commission of Financial Market; Law on capital market; Law on non-bank financial organizations; Regulation on the prior approval of large transactions, investment of own capital in social capital of a commercial company and taking credits by insurers (re-insurers); Regulation on derivative financial instruments and requirements for their disclosure; Regulation on the principles of an efficient organization of the Governing system; Law on facultative pension funds; Law for modification and completion of Law nr. 397-XV of 16.10.2003 on local public finances; Instruction on state registering of securities; On changing and completion the Instruction on public securities offering on secondary market.



**Table no. 3.** Capitalization of stock markets from CIS member states

Country	Capitalization of stock markets (million USA Dollars)		Capitalization of stock markets /GDP (%)	
	According to situation of 01.01.2008	According to situation of 01.01.2009	According to situation of 01.01.2008	According to situation of 01.01.2009
Armenia	105	176	1,00	1,50
Belarus	Data is not available	103	Data is not available	0,18
Kazakhstan	53.830	31.130	40,84	23,64
Kyrgyzstan	1.057	1.216	25,24	25,91
<i>Republic of Moldova</i>	663	716	14,04	11,85
Russia	1.266.442	365.413	99,80	26,40
Tajikistan	4	430	0,1	8,4
Ukraine	109.164	23.542	76,48	19,08

*Source:* adapted by authors in base of data from [www.cnpf.md](http://www.cnpf.md)

According to the data reflected in table 3, the highest reduction of capitalization of stocks traded on the organized market was registered on markets with a high integration degree in the world economy, like *Ukraine* (with a 4,6 times reduction), *Russia* (with a reduction of over 70%) and *Kazakhstan* (with a reduction of over 40%). Securities markets from other countries were lower exposed to the influence of crisis. For example, the markets of *Armenia*, *Kyrgyzstan* and *Tajikistan* registered a capitalization growth.

In *Republic of Moldova*, once with the increase of stock market's capitalization, its weight in GDP was diminished (from 14.04% to 11.85%). Beginning with 1998, the ratio of cumulated volume of issues to GDP registered: in 2005 – 48.5%, in 2006 – 42%, in 2007 – 37.1%, in 2008 – 32.8%, while in 2009 – 35.3%. The indicator of stock exchange capitalization to one Leu of GDP registered 14-15 bani during 2009-2010. In the developed countries this indicator registers higher levels and even exceeds the GDP volume. The rotation speed of stock exchange and OTC transactions in Moldova is low in comparison to the same indicator from developed countries.

**Table no. 4.** Volume and number of securities issues, registered by national regulation bodies of securities markets from CIS member states

Country	Number of issues		Volume of securities at placement price, thousand USA Dollars	
	At 01.01.2008	At 01.01.2009	At 01.01.2008	At 01.01.2009
Armenia	6	14	8.119	36.840
Belarus	5.347	5.094	8.052.100	15.303.700
Kazakhstan	2.788	2.792	11.510.000	14.200.000
Kyrgyzstan	79	95	53.723	150.958
<i>Republic of Moldova</i>	87	155	112.598	78.283
Russia	2.291	10.358	-	-
Tajikistan	27	55	3,6	430
Ukraine	2.698	2.614	14.178.530	12.489.075

*Source:* adapted by authors in base of data from [www.cnpf.md](http://www.cnpf.md)

On the other hand, during 2006-2007, the annual growth of capital market of Moldova was more accelerated, in comparison to GDP growth. As a result, in 2007 the weight of 5.88% of capital market penetration in national economy was reached. During the previous year, the growth of penetration level reached 4.07% (with a 1.58% increase from only 2.48%). This rhythm is too slow and represents insignificant results in comparison to very high levels of this indicator in developed countries or the ones with developing capital markets.

Still, a positive moment results from emphasizing an uptrend in the evolution of penetration level of capital market in national economy of Moldova, the fact that promises a growth of foreign direct investments (FDI) in future in the national economy, by means of capital market.

The number of securities' issues registered by national regulation authorities, practically, increased in all CIS member countries, against the augmentation of transaction cost on stock exchanges (see table 4).

Given changes on securities market were generated by a relatively limited access to credit funds from bank sector, as well as, in certain measure, by the development of securities market and an increasing financial qualification, both if issuers and investors.

**Table no. 5.** Volume of transactions with financial instruments on organized market of the CIS member countries

Country	Total volume of transactions on primary and secondary market (thousand USD)	Volume of transactions /GDP (thousand USD)
Armenia	13.516	0,001
Belarus	571.900	0,010
Kazakhstan	230.351.246	1,749
Kyrgyzstan	234.625	0,049
<i>Republic of Moldova</i>	95.842	0,016
Russia	2.037.110.000	1,462
Tajikistan	6 000	0,001
Ukraine	4.870.650	0,040

*Source:* adapted by authors in base of data from [www.cnpf.md](http://www.cnpf.md)

According to the volume of transactions performed on the organized securities market, the biggest markets are the ones from Russia, Belarus, Kazakhstan and Ukraine. At the same time, the volume of transactions in GDP, in most of countries remains at minimal levels (see table 5).

According to data from tables 3 and 5, a low ratio of capitalization level and volume of transactions to GDP is attested in all CIS member states, that demonstrates a low degree of development of securities markets. Still, this fact also determines the existence of a considerable potential of the national markets future development, in conditions of their competitiveness insurance, comparing with the markets from the developed countries.

### **General principles of capital markets development within the CIS member states**

Development of capital markets of some CIS member states can be characterized by the following *principles*:

1. Insufficient integration of the capital markets of CIS member countries in the world's economy that allowed *the avoidance of the direct and immediate effect of global financial crisis*. Only prices of

stocks issues in *Russia* and *Kazakhstan* suffered changes, the bills of exchange and deposit receipts of which are traded on London Stock Exchange.

2. Improvement of legislative framework on capital market takes place on the following directions:

- Creation of a unique record basis of rights on securities;
- Improvement of evidence of ownership right transfer over securities;
- Modification of recognition order of transactions performed on the organized market with the scope of manipulation and implementation of the sudden reaction system, development of the collective investments system (for example, adoption in *Ukraine*, at December 18, 2008, of the Law „On collective investments institutions, mutual and corporate investments funds”), which refer to assets management companies of venture organizations);
- Development of corporate bonds market;
- Granting facilities for income taxation, as a result of transactions with securities on an organized market;
- Establishing a taxation mechanism of transactions with derivative financial instruments, inclusively, those with the scope of hedging.

3. Sources' extension of creating the companies' social capital and of financial instruments' types that are traded on market. Thus, in *Republic of Belarus*, the main source for social capital creation of companies and banks in 2007 was from own resources, while in 2008, the situation totally changed: 71% from investments in the social capital of the companies was financed on account of stocks' issuance. Also, stock exchange bonds were implemented on the market of Belarus. These ones are issued without any state registration, insurance or prospectus' publication, but only in the dematerialized form with the maturity of till one year.

4. Activation of the information activities regarding the securities market functioning and increasing the professionalism degree of its participants.

### **Conclusions**

Peculiarities of development of CIS member states' securities markets characterize them as the developing ones from economic and

organizational point of view. It can be supposed that regulation of the given markets, by consideration of the related characteristics, will encourage the liquidities' growth and national securities markets' attractiveness.

At the same time, it is important to mention that the capital markets from developed countries have multiple common characteristics, distinctions related to their peculiarities of activity being unessential, while in the transition countries, depending on the degree of their economic development, the given peculiarities are more significant, with well pronounced specific characteristics. Determination of these peculiarities allows identifying the main development tendencies of the national capital markets, as well as their impact over the whole economy.

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## **Implementation of the Eco-label for Tourist Accommodation Units in Arad**

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### **Abstract**

This study examines tourist accommodation managers' attitude towards implementing the eco-labeling scheme; and, also, the degree of awareness regarding the necessity of directing businesses towards sustainable development by adopting the following: limited water and energy consumption, reduced waste production, the use of renewable resources and low-environmental impact substances, the promotion of the environmental protection education.

**Keywords:** eco-friendly products, eco-label, environmental criteria, tourist accommodations

### **Introduction**

Legal imperatives regarding environmental protection and, also, the financial leverage, made available for the functioning of environmentally compatible economic activities have brought about the launch of eco-friendly products and services as alternatives to conventional products.

Despite all of this, in the present, tourist services in Arad are trying to reach the minimum EU standards. The fluctuating quality of the services and poor personnel training are the main current issues in this sector.

### **Material and Methods**

The research was made in August 2012, on a sample of 36 tourist accommodation units; the research instrument used being the questionnaire. The purpose of this direct selective research is to find out if tourist accommodation managers from Arad are willing to implement the eco-label for their services.

The objectives of this research are:

- identifying managers' knowledge regarding the EU eco-label
- identifying managers' knowledge regarding the criteria for obtaining the EU eco-label
- identifying managers' willingness to implement EU eco-label quality systems
- identifying the degree of environmental protection enacted by the accommodation units

In order to get the data, the direct method was used, where the interview operator presented the respondents, the questionnaire.

### **Literature review**

An eco-friendly product is „that product which can satisfy consumer needs and wants and, at the same time, harmonizing their short, middle and long term interests”(Iosif et al. 1999, p.225) or „that product or service whose environmental and societal performance is, generally, significantly better than their conventional alternatives”(Pettie Ken, 1992, p.175).

„The EU Ecolabel is a graphic symbol and/or descriptive text applied to a product or package, in a brochure or another informative document which comes with the product and offers the needed information regarding the environmental criteria of the products or services”.

Lehtonen (1997) suggest that the purpose Ecolabel is “...to raise consumer awareness about the environmental effects of products, to inform consumers about the environmental characteristics of a product and to promote the adoption of more environmentally sound production methods and technologies”.

The ideal solution, which is at the managers' disposal, is the introduction of eco-labeled tourist accommodation services in the touristic circuit. Sheth and Parvatiyar, cited in Polonsky and Mintu-Wimsatt (1995, pp.11-14) considered that directing companies' activities towards sustainable development assumes the assimilation of certain

commitments to sustainable development from top managers down to the last employee. Thus, by running this research, I found necessary to apply a set of questions regarding personnel training and preparation as well.

Even no human activity can be completely environmentally friendly; there is always a possibility to reduce the environmental effects of certain products or services. The EU eco-labeling system is part of the policy on sustainable production and consumption, which has as main objective the reduction of the negative impacts of consumption and production on the environment, on health, on the climate and on natural resources.

Thus, the eco-labeling scheme has been created along with environmental and performance criteria which underline the evaluation of the touristic products and services. According to CE no.66/2010, when there is intent to start the eco-labeling process, tourist accommodation facilities must comply with the following criteria:

- limited energy and water consumption
- waste reduction
- use of renewable resources and low-environmental impact products
- promoting environmental protection education.

The sums needed to implement the eco-labeling scheme for touristic accommodations are rather high and not in hand for all touristic accommodations, reflected in the small number of eco-labeled facilities. At a national level, there are only four eco-labeled facilities, up to August 2012 (The Saturn Hotel in Saturn resort, Crowne Plaza Hotel in Bucharest, Vega Hotel and Piatra Șoimului Villa in Mamaia) (Green Report, 2012; <http://www.ecomagazin.ro/pensiuni-certificate-ecologic/>).

The facilities' effort towards implementing the eco-labeling scheme is remarkable and it must be said that clients appreciate the efforts.

Also, implementing the ISO 9001:2001 and ISO 14001:2005 offers clients safety and comfort, it improves their experience and it improves the image of the facility that uses these standards, both among existing clients and potential clients. Satisfying the needs and expectations of ever more fastidious clients will ensure the long-term success of the facilities.



### Results and Discussion

After running the study based on a questionnaire measuring the degree of implementation of the eco-labeling scheme among tourist accommodation facilities in Arad, the following results were obtained:

- of the total of 36 facilities, 72% are aware of the EU eco-label and 28% are not. We can say that, even though the promotion of the eco-label has been going on for years, the eco-label is not yet very well known to all managers; this could be the result of insufficient promotion or inadequate use of promotion techniques.

- only 46% are aware of the environmental criteria used by the eco-labeling scheme for tourist accommodations.

- none of the facilities were eco-labeled, only the Phoenix Hotel of Arad had made inquiries for eco-labeling

- managers' degree of understanding regarding the role of the eco-label can generally be seen as favorable. The statements *The eco-label is useful for the environment* and *The eco-label offers clients accommodation which is beneficial for their health* got favorable feedback (with a mean of 1.58 and 1.55), over the general score of 1,33. Nevertheless, the statements *The eco-label's purpose is to repay tourists that respect the environment* and *The costs of the facility will fall after implementing the eco-label* scored under the mean score (with a mean of 1.16 and of 1.06), thus being necessary an improvement of these aspects in the opinion of the managers, especially among those that want to direct their activity towards sustainable development.

- regarding the energy use, 28% have high-efficiency appliances, 32% have proper thermal isolation, 58% collect data regarding energy consumption, 17% have lights and heating that switch automatically, 8% don't meet any environmental criteria and 12% use renewable energy.

- regarding the water use, 38% use low-water-consumption dishwashing and washing machines and toilets, 54% change the sheets and towels properly, 48% reduce the flow of water from taps and showers and 7% treat waste water correctly.

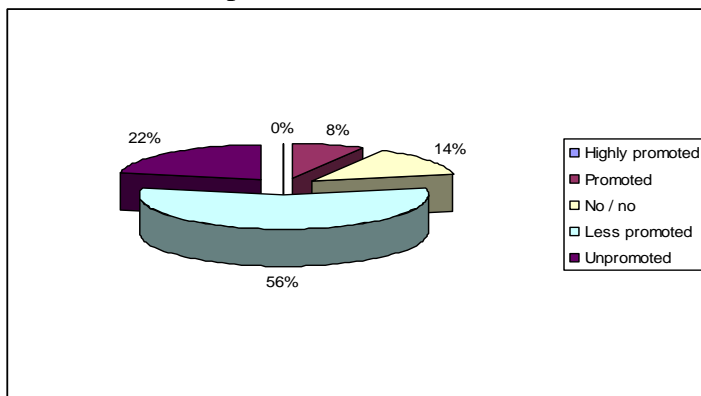
- regarding personnel training, 35% are trained regarding use and maintenance of equipment, 31% use correct dosages of detergents and cleaning products, 17% are trained regarding environmental protection issues, 12% have implemented an efficient energy and waste management and 5% do not meet any of the before mentioned.

- regarding the communication activities, 18% give clients information on events and local news regarding the environment, 21% inform clients regarding the environmental protection measures taken during their accommodation, 15% inform clients on their low energy and water consumption management, 5% inform clients on their waste separation activities, 18% inform clients regarding the use of public transportation and 23% do not give clients any kind of information.

- regarding the managers' opinions upon the degree of awareness of the EU eco-label among accommodation services providers, this study has shown that the eco-label is not well promoted, only 8% consider it to be well promoted.

### Chart no. 1

Opinions regarding the promotion of the EU eco-label among the accommodation services providers



*Source:* Own interpretation upon the results of the study

- regarding the intention to implement the eco-label in the future, 76% of the managers say that they are willing to adopt the labeling scheme, 13% are not sure and 11% are not interested in adopting the scheme.

### Conclusion

An efficient management in tourist accommodation facilities must reduce energy and resource consumption. In the future, many facilities could adopt the eco-label if top managers would become aware of the benefits of implementing it. Despite the fact that implementing

the EU eco-label implies rather large investments in photovoltaic energy production systems, in renewable thermic energy production systems, like heat pumps and solar panels, in selective waste collection, all reflecting eventually the reduction of costs and ensuring a sustainable growth economically and ecologically.

To benefit from the eco-label, on the one hand there must be a reduction in the inputs, in the process of acquisition by minimizing the use of materials, energy consumption, water consumption etc., and on the other hand a reduction in the outputs, reducing waste and residue disposal.

Despite the fact that in Arad there is no eco-labeled accommodation facility, among managers of such facilities there is willingness for environmental protection and for the protection of the clients' health. The Phoenix Hotel will implement the eco-label no later than next year. It is remarkable the fact that 76% of the managers of the accommodation facilities are willing to implement the eco-labeling scheme.

Upon these considerations, I think it is necessary to adopt viable laws regarding the establishment of economic mechanisms in order to stimulate the adoption of the eco-label thus promoting and developing sustainable tourism on a local and national level. Also, it is necessary to strongly promote the eco-label and the criteria's for obtaining it, and also the benefits that come from implementing it, both on the staff and the consumers.

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## **Social Responsibility in the Romanian Medical Sector**

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### **Abstract**

As an inspiring and strategically important development, social responsibility (SR) is becoming an increasingly important priority for the companies of all sizes and types. Occupational Safety and Health (OSH) is an essential component of SR and it requires managers and OSH professionals with a variety of opportunities and challenges. With increasing globalization, greater environmental and social awareness and more efficient communication, the concept of companies' responsibilities beyond the purely legal obligations or profit-related objectives has gained new impetus. Businesses need to be seen acting responsibly towards people, planet and profit. The paper presents the actions taken by the Romanian companies in the medical sector to define their social responsibility performance.

**Keywords:** constraints, social responsibility, principles, opportunities, actual context

### **Introduction**

In the context of globalization and increasing awareness of social and environmental issues, the concept of social responsibility exceeds the purely legal issues and focuses its attention towards people, planet and profit.

SR involves voluntary actions of companies that follow their interest in a long term growth through socially responsible initiatives. Companies must have objectives and actions that take into account the protection of workers under the national and community law, but also the needs still perceived as external to the company, such as balance between professional life and private life, aspects of the environment or public health and safety.

According to ISO 26000, in applying the SR concept are needed to be followed a set of principles which should be reflected in the organization's policy and activities. These principles are generic and interdisciplinary and can be applied to each of the SR components, including OSH.

*Accountability* – The organization should be responsible for its impacts on society, economy and environment, identify applicable laws and ensure compliance with all the identified provisions.

*Transparency* – The organization should ensure transparency of its decisions and activities that have impact on the society and environment. It should provide stakeholders information on internal structure, policies, rules, responsibilities and other information that may affect sustainable development.

*Ethical behavior* – The behavior of an organization should be based on the values of honesty, fairness and integrity.

*Respect for stakeholder interests* – The organization must take into consideration and respond to the stakeholder interests.

*Respect for the rule of law* – The organization must comply with legal requirements in all fields, even where laws and regulations are not implemented properly.

*Respect for international norms of behavior* – The organization must comply with the international norms of behavior.

*Respect for human rights* – The organization must strive for human rights, even if it carries out activities in countries where these rights are violated.

All these principles resonate with the OSH legal provisions and policies. Being a highly regulated field, occupational health and safety

is used to being monitored internally and externally and assessed for legal compliance. Management systems according to OHSAS 18001 or other standards enhance the accountability for OSH performance beyond legal requirements. Integrated management systems (ISO 9001 & ISO 14001 & OHSAS 18001) correlate OSH issues with those regarding quality and environment. SR goes one step further, with an even broader approach.

Considering the experience in obtaining health and safety performance, companies can use this expertise when building a strategy for SR. OSH specialists have an important role to play because they know well how important it is to win trust of employees and their involvement in company initiatives.

### **Material and Methods**

After launching the concept of Sustainable Development at the 1992 summit in Rio and adopting it by the European Council of European Strategy for Sustainable Development, the growth of social responsibility (SR), first mentioned in the Strategy from Lisbon in 2000, was a reflection of sustainable development at organization level.

In 2001, the European Commission developed the “Green Paper on CSR” and launched “Multi Stakeholder Forum” which established principles for social responsibility practices. A number of instruments for measuring, evaluation, improvement and communication of social responsibility performance were developed and best practices were proposed/promoted in areas such as lifelong learning, work organization, equal opportunities, social inclusion and sustainable development.

In 2006 the European Commission supported the launch of the “European Alliance for European Enterprises’ Responsibility” in order to give fresh impetus to initiatives in the RS field.

On November 1<sup>st</sup>, 2010, ISO 26000 standard was officially launched in Geneva under the name *Guidance on Social Responsibility*, which provides guidance on social responsibility, both for private sector organizations and for public sector taking into account the principles, key topics and issues of social responsibility.

In October 2011, the European Commission publishes the new strategy of social responsibility which emphasizes that enterprises “should have in place a process to integrate social, environmental, ethical and human rights concerns into their business operations and

core strategy in close collaboration with their stakeholders". The new policy of the EC in the RS field is an action program for 2011-2014 that focuses on eight priority areas: enhancing the visibility of SR and disseminating good practices, improving and tracking levels of trust in business, improving self-regulation and co-regulation processes, enhancing market reward for SR, improving company disclosure of social and environmental information, further integrating SR into education, training and research, emphasizing the importance of national and sub-national SR policies and better aligning European and global approaches to SR.

Under the new policy, SR' multidimensional nature concerns human rights such as training, diversity, gender equality, health and welfare of employees, but also environmental issues and combating corruption.

Already, many large companies have put into practice social responsibility measures. The number of such companies is growing and it seems that in the near future SR implementation will follow an upward trend that recalls the widespread implementation of quality, environmental and occupational safety management systems. These examples of initiatives are pleasing to ensure a successful widely implementation of the SR concept; Romania needs activities concerted of support from entities with experience in managing organizations and in concerned issues of social responsibility.

### **Literature review**

According to a report by Eurostat, the statistical data obtained with a source of "Labour Force Survey - Ad hoc modules on Accidents at work and work-related health problems" in 2007, exposure to risk factors affecting mental health workers is highest healthcare.

Synthesis of national occupational illness situation in our country INSPB performed during 2010, which shows that: incidence of occupational diseases per 100,000 workers in the health and social care is 16.40%, which is in 6th place after sectors like manufacturing, mining and quarrying, manufacturing and electricity supply activities, Arts, entertainment and recreation, transport and storage and Human health activities were 2nd with 48 cases, branches of economy in which the most frequently reported occupational diseases in women in 2010.

In 2010, there were 46 cases of infectious diseases in healthcare professionals such as: 8 cases of viral hepatitis in health sector



personnel (1 July hepatitis B and hepatitis C), 20 new cases of tuberculosis professional and a new case of occupational cancer - acute lymphoblastic leukemia due to ionizing radiation, gamma, X-ray, physiotherapy a nurse with 18 years experience in the field. [7]

### **Current Situation of Romania regarding SR and the Health Care System**

#### ***Constraints and opportunities for SR implementation nationwide***

The SR concept is relatively new in Romania and we can not specify an exact number of the organizations implementing or evaluating their involvement in SR. There is a series of events, like Business Ethics Conference, International Conference on Corporate Social Responsibility, now in its 3rd edition, Romanian SR Award, workshops on SR; however we cannot speak of a real SR network of all existing programs. Perhaps, the companies familiar with ISO family standards will understand the importance of a more systematic planning and be aware of the importance of implementing the SR standard.

##### *Constraints*

- From the legal point of view:

When becoming an EU Member State, Romania has quickly harmonized the existing legislation with the European Community legislation which led to a large volume of new regulations, published in a short period, increasing the effort of the concerned parts to adapt. The health care system underwent a major reform in 2006 and comments on legislative deficiencies are still quite often heard.

- From the economic point of view:

Romania's economy underwent profound changes and effects of the long transition are still felt. Low productivity, technological losses, low competitiveness of products and services has hindered economic development. Lack of investment funds for refurbishment has a direct impact upon the production and indirectly on the work and living conditions and on environment. In addition, a weak economy hardly adheres to principles such as responsible competition, responsible procurement and correct labor relations. The national health care system, dependent on the general economic performance, had suffered greatly from the effect of economic crisis.

- From the social point of view:

Romanian society has an underdeveloped middle class, still preoccupied with material stability. Unlike other countries where this class is dominant and is the engine of many changes, the middle class in Romania is quite thin and the interest and involvement in matters related to social responsibility is relatively recent. The current situation is reflected in the type of SR actions for hospitals, most of them with a social motivation.

- From the cultural point of view:

Modern civic culture is still under shaping and the involvement of population in issues of community interest is still poor. Perception of the risks to health and environment and even social life is more developed in the population with higher education from the urban areas, but very low in other environments.

*Opportunities*

- From the legal point of view

Romanian national legislation is harmonized with the community law which facilitates economic and work force exchanges, international partnerships and investments in Romania. Development and implementation tools as well as controls leads to the stimulation of a more systematic compliance with the law.

- From the economic point of view

The investment of leading firms with economic and technologic performance and with quality products or services may give a concrete example of responsible business approach.

Some of these companies have already implemented the concept of social responsibility. An example is the private medical sector companies who understood that they can adopt practical solutions of SR, by developing programs to pursue the well-being of employees (e.g. medical, psychological, recreational and sport facilities etc.).

Many of the SR actions in the public health care sector are supported by major companies, this sector often being the first recipient of SR actions of these companies.

- From the know-how point of view:

Romania's EU accession opened the door to EU funds for development projects, which are an important component of social responsibility.

The experience gathered in implementing environment management systems and occupational safety and health management

systems by more and more units can be successfully used in the implementation of ISO 26000.

- From the social-cultural point of view:

It is foreseeable that the consumption pattern of the population, which is still in progress, will be influenced positively by changes at international level. These changes are already felt in countries with traditional consumerism, that make efforts to adopt more responsible ways of consumption regarding resources, product life cycle, health and environment impact.

#### *The health care system*

Besides the general aspects mentioned already, the health care system has its own specific problems and needs.

One of the problems is the lack of personnel in health care units. Though it is a general situation in many countries (even in developed ones) the case of Romania is generally acknowledged as stringent and of real concern. Table 1 presents statistical indicators for Romania, as compared to Germany.

**Table no. 1.** Specialized workforce in the health care system of Romania and Germany (2000-2009, density per 10000 population) [2]

Physicians		Nursing and midwifery personnel		Dentistry personnel		Pharmaceutical personnel		No. of hospital beds
No.	Density*	No.	Density*	No.	Density*	No.	Density*	Density*
Germany								
288	35	661	80	63	8	49	6	83
182		000		100		528		
Romania								
41	19	90	42	4	2	901	<0.5	65
455		698		360				

Data in table no. 1 shows a shortage of medical and pharmaceutical workforce of Romania, as well as a reduced density of the hospital beds.

A more recent cause for insufficient personnel is the migration of medical staff. Exact figures are not available. Before 2007, 9.4% of the doctors already worked abroad. The percentage increased greatly after Romania's EU accession in 2007 and the implementation of the Directives regarding free labor market. [6]

Lack of personnel is also caused by economic factors, since Romanian expenditures for health are only around 5% of the GDP, while in Germany, for example, the percentage is double.

**Tabel no. 2.** Health expenditures in Romania and Germany [2]

Total expenditure on health as % of gross domestic product		General government expenditure on health as % of total expenditure on health		Private expenditure on health as % of total expenditure in health		General government expenditure on health as % of total government expenditure		External resources for health as % of total expenditure on health	
2000	2007	2000	2007	2000	2007	2000	2007	2000	2007
Germany									
10.3	10.4	79.7	76.9	20.3	23.1	18.2	18.2	0	0
Romania									
5.2	4.7	67.7	80.3	32.3	19.7	9.2	10.3	5.7	0

Health expenditures per capita are very low, as shown in table no. 3 where comparison is made to figures in Germany.

**Table no. 3.** Health expenditures per capita in Romania and Germany (PPP=Purchasing power parity) [2]

Per capita total expenditure on health at average exchange rate (US\$)		Per capita total expenditure on health (PPP* int. \$)		Per capita government expenditure on health at average exchange rate (US\$)		Per capita government expenditure on health (PPP* int. \$)	
2000	2007	2000	2007	2000	2007	2000	2007
Germany							
2 372	4 209	2 671	3 588	1 890	3 236	2 128	2 758
Romania							
87	369	298	592	59	296	202	475

Underfunding health sector does not have effects only on the workforce enrolment. As for other sectors, but even more in this case, it rather generates a vicious circle. The quality of medical and auxiliary activities is affected, which generates dissatisfaction among patients and personnel as well.

Stress is known to be an important risk in health care units everywhere. Work violence on behalf of clients (patients) is more common in the health system than in other civilian sectors. Working

under increased stress and the more demanding job tasks add to the factors that decrease work quality and work satisfaction while increasing occupational risk level.

Occupational health and safety measures that involve higher costs are hampered by lack of funding. Purchasing safer equipment is not possible when they are more expensive and this is not only the case of sophisticated apparatus, but also of devices that are used in large quantities, like syringes with needle protection.

### **Results and Discussion**

In order to take full advantage of the existing opportunities and to cope with constraints for the implementation of the SR concept in Romania in more organizations, the following steps are required:

- Promoting the concept of SR, the advantages and positive examples of its implementation;
- Defining an institutional framework to provide support to organizations in evaluating implemented SR measures and measuring the performance obtained;
- Training of stakeholders and those involved in implementing the SR measures;
- Public awareness on the importance of its involvement in supporting the SR measures.

For contributing to the success of implementing the concept of SR, a consortium of research, academic and public opinion polling institutions have developed in a project a model for defining the institutional framework for implementing ISO 26000.

Lack of funding is not always used as argument for giving up actions that help improve the overall performance of the hospitals and other sanitary units.

Priority is given to the most vulnerable groups and activities like those dedicated to help the population with no or very low incomes.

Other activities are also included in the SR approach [4]. They are especially aimed at the general public, like events promoting safe eating habits or sports, or like encouraging people to regularly check their health.

An example of a company concerned with social responsibility is MedLife, a private clinic in Bucharest, which organized two campaigns, namely blood donation campaign "Share the joy of living!", organized in collaboration with the National Institute of Hematology

and Blood Transfusion, and a campaign to divert 2% from the salary tax to PRO Sănătatea (MedLife Foundation) to help children from St. Demetrios PRO Health Center, called “Help the birth of a chance!”[1]. Activities for higher medical performance of the present and future generations of professional are carried out by some medical units or networks. Free workshops are organized for students, or employees, for example: WOTCHE project (Working with Online Training Content in Healthcare Education) was implemented by collaboration between a large health care network and an NGO [3].

However, in order to take full advantage of the existing opportunities and to cope with constraints for the implementation of the SR concept in Romania in more organizations, more coordinated steps are required:

- Promoting the concept of SR, the advantages and positive examples of its implementation;
- Defining an institutional framework to provide support to organizations in evaluating implemented SR measures and measuring the performance obtained;
- Training of stakeholders and those involved in implementing the SR measures;
- Public awareness on the importance of its involvement in supporting the SR measures.

An example of initiative regarding SR in the health care system is COMPEFSAN, a three year project funded by EU on Sectorial Operational Project – Human Resources Development (POS DRU) entitled “Increasing the Competitiveness, Efficiency and Occupational Health and Safety of the Personnel in the Health Care Sector to Ensure Better Opportunities of Participation in a Modern Labor Market”. The project is implemented by a consortium of research and academic institutes: INCDPM “Alexandru Darabont”, Bucharest, in collaboration with “Carol Davila” University of Medicine and Pharmacy of Bucharest, IRECSON – Bucharest and the Academy of Economics Studies of Bucharest as well [5].

The major objective of this project resides in improving and developing the OSH related competences of the personnel working in the health care sector. The project also promotes the most suitable means to ensure the adaptability of the personnel OSH competences to an increasingly changing socio-economic environment.

The target group is constituted of managers of health care units, physicians, nurses, specialists in occupational medicine.

The COMPEFSAN team prompts good practices like responsible purchasing and updating the supply procedures according to OSH criteria. Safer reagents for laboratories are available on the market lowering the risk for personnel and for the environment. Devices that avoid using mercury reduce concerns for patients and personnel health and cut expenditures for managing hazardous wastes. Green materials for construction and for maintenance, disinfecting and cleaning are also recommended for the reviewed supply procedures [5].

Physical hazard as well as measures and facilities that avoid musculoskeletal disorders, so common in hospitals, are disseminated by COMPEFSAN. Biological risks, including those associated with needle stick injuries are discussed and protection measures and devices are presented.

Managing hazardous hospital wastes has been improved over the years but still an important problem for OSH as well as for the environment. Good monitoring and safety practices are described in the mentioned project.

The experience of health care units in EU countries is used by COMPEFSAN as well as practical examples published by other sources.

Biological diseases ranked seven in the national morbidity [7] in 2010 therefore specific measures are needed to protect health care workers. Good practices on biological hazards include specific measures of prevention and protection such as:

- Best hand hygiene and use of personal protective equipment;
- Carefully handling and disposal of sharp medical instruments and medical waste;
- Isolating patients, when it is suspected or already established the presence of a serious infectious disease;
- Intensive training of staff in respect to strict hygiene measures;
- Monitoring the use of disposable gloves and its usage as an indicator of hygiene, checking at the same time, compliance;
- Antibiotics administration and disinfection only with strict medical recommendation, in order to combat multi-resistant pathogen agents;
- Good communication – with other employees, patients and visitors.

Considering the busy working life of medical personnel, a platform for distance learning will be developed and experimented for a pilot training alternative during the COMPEFSAN project.

### **Conclusion**

The health care system in Romania is mostly the beneficiary of SR because of the underfunding that has become a chronic situation over many years.

However, healthcare units begin to show their interest in adhering to SR principles and planning their own activities. Due to the economic and social problems, many of these activities are focused on providing help to the most vulnerable groups, like children in foster houses, elderly or unemployed population.

Issues like OSH and environment are reconsidered in the perspective of SR and measures are taken to integrate them better and to make them more visible to the interested parties.

Implementation of ISO 26000 will help achieve the goal of sustainable development by adopting SR measures by the organizations in Romania. Economic and social transformations through which Romania has recently been, facilitates the adoption of the new concept.

Experience gained in implementing quality, environment, health and safety at work management systems, can be an advantage in adopting the provisions of ISO 26000.

The financing of development projects by the Community funds will help build a generation of project managers to consider social responsibility as part of current activities, in accordance with the Community Strategy and with explicit qualification requirements of the projects.

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## **The Pension Reform Proposal for Tunisia - the Case of the general NPSIF Scheme**

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### **Abstract**

Given the results of population projection indicating an inevitable aging in the coming years for Tunisia, the general scheme of the National Pension and Social Insurance Fund (NPSIF) which operates according to a mode pay-as-you-go enters a very difficult phase. Thus, its financial results are currently in deficit and also that we perform the simulation until the year 2030 show the increase of the deficit in the case of maintenance of its current legislation. For this reason, we propose reform scenarios to alleviate the most possible deficit of the general scheme of NPSIF.

**Keywords:** pension projections, Pay-as-you-go, aging

### **Introduction**

The Tunisian pension system is complex because that consists of a large number of schemes. The financing of these schemes is based on an ordinary principle corresponding to pay-as-you-go. This principle is assumed to determine the obligations of every present and future generation and by the government to assure the sustainability of the pension system viability.

After independence and until the 90s, the financing of the Tunisian pension system enjoys a favourable demographic help to expand coverage and improve gradually the retirement rights. Indeed, the growth of the labour force during this period contributes to the persistence of the population ratio between contributors and pensioners.

During these last years, the sustainability of pension became an essential problem for the public authorities. The financial problems may get worse because of the demographic transformations such as reduced fertility and longer life expectancy, as emphasized Houssi (2003) and Houssi (2005). This demographic change is not the only cause of worsening of the financial problems. There are other factors such as the deterioration of the economic situation, anticipated retirement; the entry of young people on the labour market is late due to the longer duration of the studies. Our study focuses on the general scheme of the National Pension and Social Insurance Fund (NPSIF) covering the public sector employees.

Our paper is organized as follows. First, we describe the evolution of the financial situation of the general scheme of NPSIF. We turn then to the projection of the state financial scheme showing the gravity of the future situation under unchanged legislation. And finally, we propose reform scenarios to alleviate the possible maximum deficit of the scheme.

### **The evolution of the financial position of the general NPSIF scheme**

The financial results managed by the general scheme of the NPSIF are characterized by several changes since 1990, until our days. To describe this situation, we divide this period into several intervals:

- 1990-1992: the budgetary balance had weak results; on the other hand, a tendency to fall causes a deficit.

- 1993-1998: the overall balance of NPSIF was deficit in the years 1993 and 1994. Subsequently measures were taken to gradually increase the contribution rate of the general scheme and to restrict the cases of voluntary early retirement with the aim of improving the results. Therefore, these measures were awarded until 1998 to improve the results of the general scheme.

- 1999-2000: the results recorded again a remarkable decline during this period and therefore a new deficit appeared in 2000.

- 2001-2005: this period was characterized by the following financial situation:

**Table no. 1.** Financial situation of the general NPSIF scheme during the 2001-2005 period  
(Unit: thousand dinars)

	2001	2002	2003	2004	2005
<b>Income</b>	578953	651606	747298	843631	907865
<b>Spending</b>	591757	666627	737136	825766	920766
<b>Result</b>	(12804)	(15021)	10162	17865	(12911)

*Source:* Activity Report of NPSIF for 2005

At the successive challenges of pensions in 2001 and 2002, measures were taken regarding the increase of 2.5% of the contribution rate to the general scheme from July of 2002. These measures have improved the financial regime in 2003, but returned again in deficit in 2005, since the evolution of growth rate of the beneficiaries of pensions was higher than that of the evolution in the number of the active members of the scheme.

- 2006-2010: this period knows the following financial situation:

**Table no. 2.** Financial situation of the general NPSIF scheme during the 2006-2010 period  
(Unit: million dinars)

	2006	2007	2008	2009	2010
<b>Income</b>	1067,736	1202,868	1357,622	1527,198	1694,676
<b>Spending</b>	1105,704	1270,292	1385,680	1547,370	1777,700
<b>Result</b>	(37,968)	(67,430)	(28,058)	(20,212)	(83,024)

*Source:* Activity Report of NPSIF for 2010

During this period, we can see a deficit, but also a slight improvement with the measure applied in July 2007, to increase the contribution rate. However, this improvement is limited because the deficit increases widely in year 2010 to reach 83,024 million dinars.

The financial difficulty of the general NPSIF scheme is due especially to two essential classes of factors. The first is an endogenous factor in the pension system which is explained by the generosity. This notion of generosity can be measured by the level of pension benefits as the level of annual pension developed by Zaidi et al (2006) or the level

of replacement rate as Hachon (2008). The second is an exogenous factor in the pension system, which is explained by the changing demographic circumstances including the decline in fertility and the increase in life expectancy as emphasized Ben Braham (2009).

### **Simulation of the general NPSIF scheme, horizon 2030**

#### *Methodologies and Assumptions*

In order to test the financial position of a pension scheme, it must project over time expenditures and revenues in order to determine the evolution of its result. For this reason, in recent years different models have emerged to achieve this type of simulation. The models developed by the World Bank and the International Labor Office are considered the most appropriate. The actually model used here is called PROST "Pension Reform Simulation Toolkit" developed by the World Bank. PROST model allows us to simulate the evolution of financial and demography parameters of the general NPSI scheme. The use of the PROST model helps us first to determine the expenditures and revenues of our general NPSIF system in the next 20 years and secondly, whether our system is viable and sustainable in the short and medium term.

In our paper, year 2010 is taken as a basis for projections. Concerning the projection of the number of active, we assumed that it grows on average 2.5% per year according to the latest statistics of the national Institute of Statistics. For the projection of the pensioners<sup>1</sup>, we have based on the statistics of the general NPSI scheme over the last 5 years and therefore, we have assumed that retirees evolves of 4.5% on average per year, widows increase of 4% on average per year and orphans is growing by 7% per year. For the financial projections, we assumed an evolution of the average wage rate of 4.5% per year according to the Tunisian economic context. Also, the pensions of retirees, widows and orphans are supposed evolve at the same rate as the average salary according to the principle of equalization<sup>2</sup> performed by the public sector.

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<sup>1</sup> We take account of these different categories of pensioners because collected contributions are designed to cover the different risks. This means that there is no contribution to each risk.

<sup>2</sup> Equalization allows the pension to revise by incorporating into the base of liquidation. The result increasing in the surcharge is a former permanent part of the remuneration, or an allowance or bonus that the retiree had not seen in his retirement

From the data on the number of assets and the average wage, we calculated the payroll for each year. The latter is multiplied by the rate of contribution respecting the general scheme of CNRPS. To determine the contributions are written the follows:

$$COT_t = SM_t \tau_t L_t$$

where:

$COT_t$ : contributions;  $SM_t$ : the average wage;  $\tau_t$  the contribution rate and  $L_t$ : the number of active.

On the other hand, we multiplied each average pension with the relative number of pensioners, to obtain the total expenditure for each category of the general NPSI scheme. Subsequently, we added these different expenditures to the total expenditures of benefits that are formalized as follows:

$$PREST_t = PMR_t \times R_t + PMO_t \times O_t + PMSS_t \times CS_t$$

where:

$PREST_t$ : benefits;  $PMR_t$ : the average pension of retirees;  $PMO_t$  the average pension for orphans and  $PMSS_t$  pension average of surviving spouses

Finally, the projection of cash flows comprise firstly the technical result which is defined as the difference between contributions and benefits, on the other hand, the net result is obtained by summing the initial technical result reserves and financial product<sup>3</sup> and by deleting the management fees. These management fees represent a certain percentage of payrolls. They are 1%<sup>4</sup> of payroll. Thus, the nominal interest rate used in the calculation of the financial products is estimated at 5.5%.

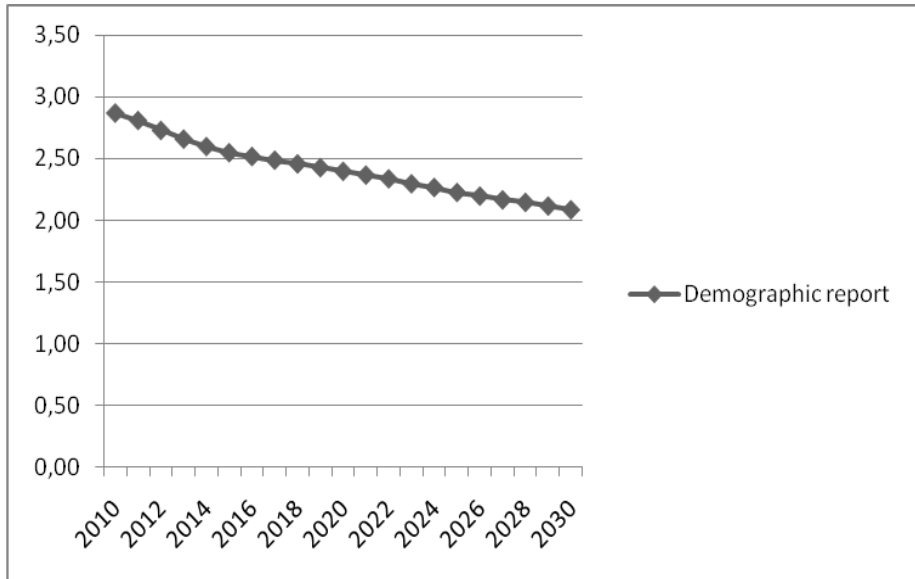
### *Result of projection*

The projection of the demographic report showed that the general NPSIF scheme is in a state of maturity since this report would mark a decline during the projection period. Indeed, the number of contributors compared to pensioners regress continuously during the forecast period from 2.87 in 2010, to 2.09 in 2030, as shown in the graph below.

<sup>3</sup> Compensation investments are money market rate

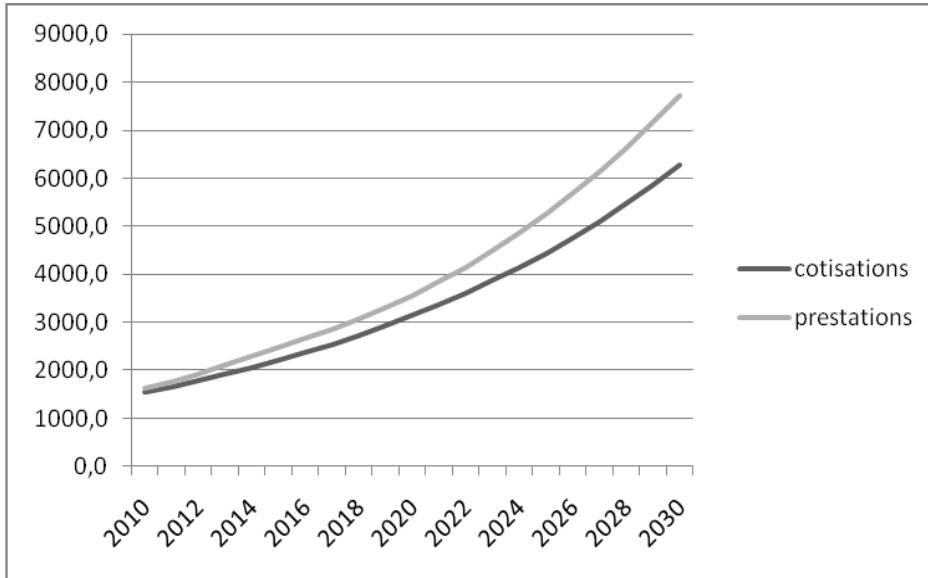
<sup>4</sup> According to the estimation made by the Centre for Research and Study of Social Security in Tunisia.

**Figure no.1.** A demographic report projection of the general NPSI scheme



With the PROST model, we simulated the level of contributions and the benefits of the general NPSI scheme based on the assumptions mentioned above. The evolution of the contributions and benefits will follow this pattern.

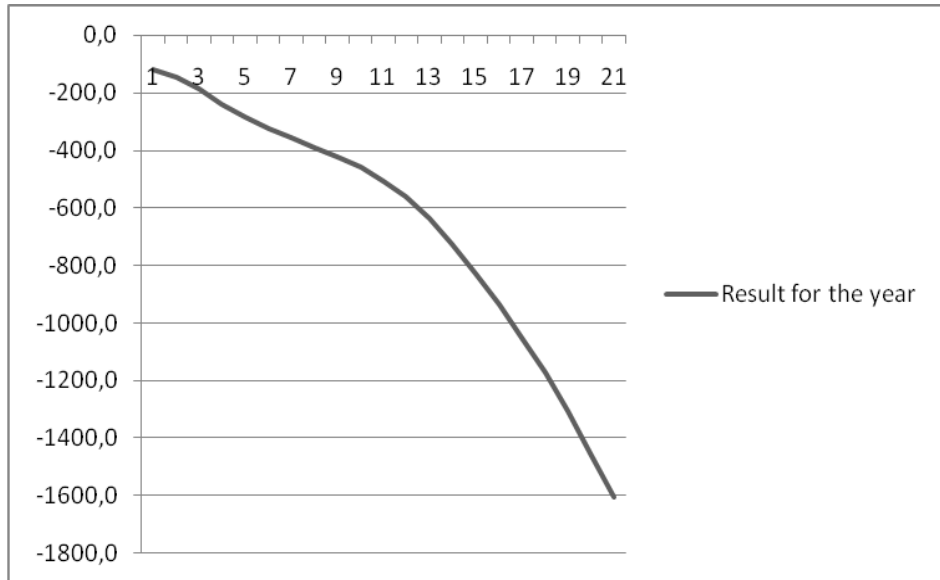
**Figure no. 2.** Projection of the contributions and benefits of the general NPSIF scheme (millions of dinars)



According to this graph, we noticed that there is a discrepancy between contributions and benefits. Thus, the significant increase in benefits is a cause of simultaneous two variables: the average pension and the number of pensioners that are positively correlated and follow the same trend. The slight increase in contributions is due primarily to maintenance the contributing population growth throughout the projection period. Therefore, this mismatch between contributions and benefits will lead to a deficit in the net result for the projection period, as evidenced by the graph below.



**Figure no. 3.** Projection of the net result of the general NPSIF scheme (millions of dinars)



According to the simulation, we found that the general NPSIF scheme have already a deficit in the first year of the projection. Also, this deficit will accumulate from one year to another until the last projection period to reach the value of 1606,3 million dinars.

Finally, the simulation results in the case of unchanged legislation will prove that this scheme will lead to a complete failure. For out of this situation, it is essential to reform the general NPSIF scheme.

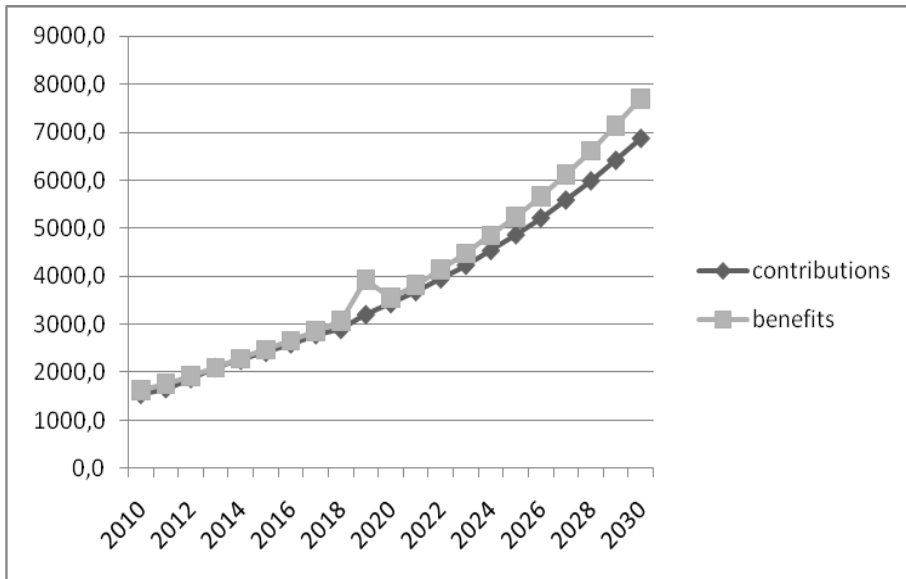
### **Reform proposal**

In what follows, we will simulate various reform proposals to reduce the maximum possible deficit of the general NPSI scheme which visualizes in the context of legislation unchanged along the projection period. During this part, the assumptions are not changed. On the other hand, the reforms that we have proposed start either in 2011 or 2012.

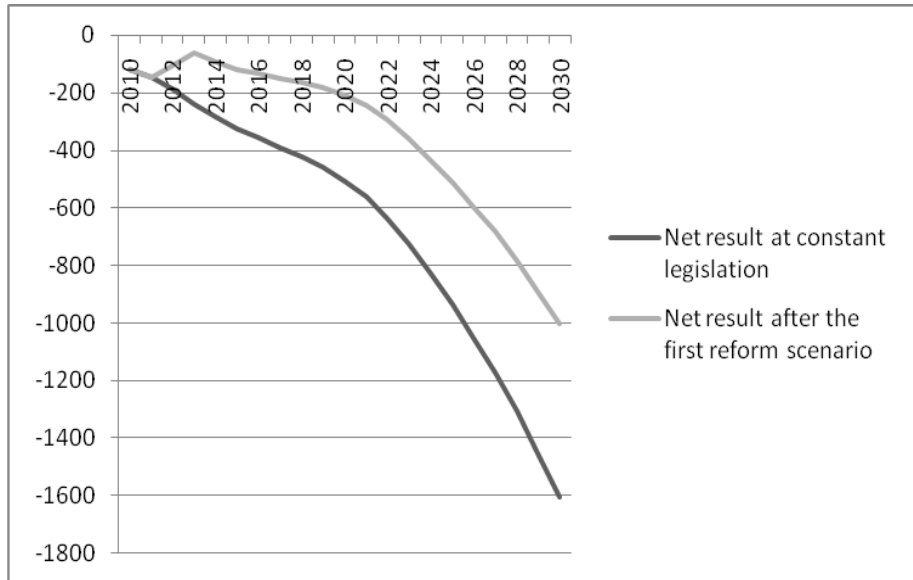
The first reform scenario serves to increase the contribution rate of 1 point, respectively for the year 2012 and 2013 to stabilize the threshold of 19.2% from that date and until the end of our projection period. This type of reform allows increasing contributions without

affecting benefits and therefore helps to reduce the divergence between these two variables. We noticed during the reform period that contributions and benefits will be approximately similar with a slight delay that will begin in the year 2020 (see figure 4). The impact of such measure on the net result of the general NPSI scheme simulations stipulate a clear improvement in the reduction of budget deficit as compared to the net result in the case of unchanged legislation (as indicated in the figure below).

**Figure no.4.** Evolution of the contributions and benefits after the first reform scenario (million dinars)

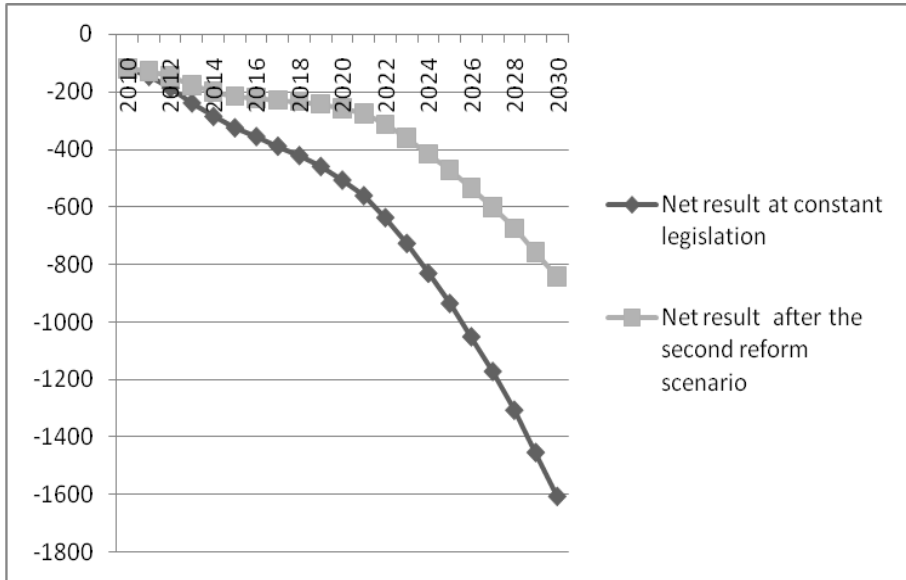


**Figure no. 5.** Projection of the net result of the general NPSIF scheme after the first reform scenario



The second way of the reform is based on the reduction of the maximum pension rate. From 2011, the rate of evolution of the pension is 3%, instead of 4% during the first 10 years and remains 2% for 20 years. In other words, the maximum rate of pension after 30 years work will become 70%, when it was 80%. The benefit of this measure is to curb the increasing level of increase in benefits without being accompanied by a change in the amount of contributions. The simulation will stipulate that this measure will have a greater effect on reducing the amount of deficits compared to the first reform scenario. Indeed, a 70% decrease in the maximum pension will cause a continuously increase in the deficit reduction in the year of reform 2011, until the end of the projection period.

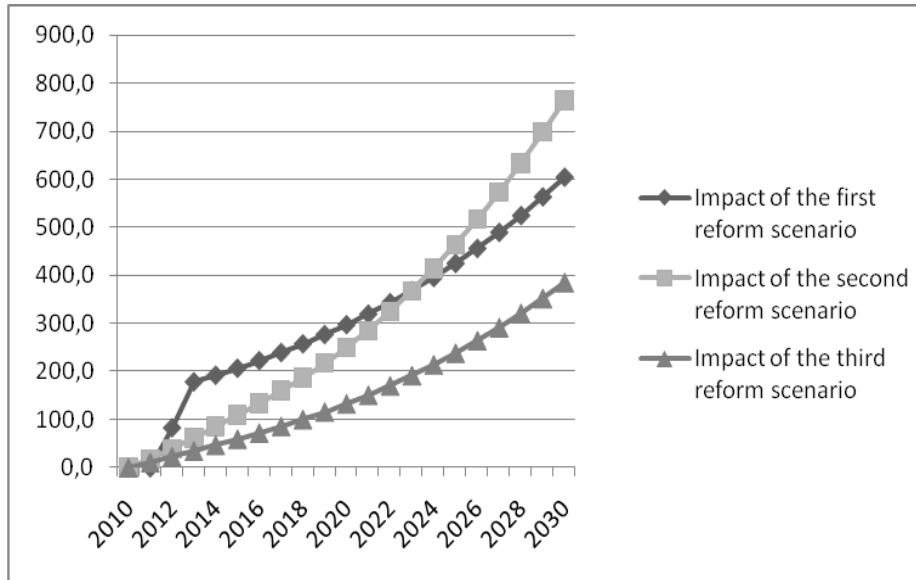
**Figure no. 6.** Projection of the net result of the general NPSIF scheme after the second reform scenario



The third reform proposed to reduce the rate of pension to 2% per year of anticipation, during maximum 5 years, started with 2011. This measure is compatible with the current situation which saw our country following the revolution which emphasizes employment. Indeed, this measure helps to provide jobs for young people and reduce the unemployment rate. This reform is totally different from the reform that encourages the gradual increase in retirement age.

This reform allows both, to moderate the increase in benefit levels and to increase the number of contributors, and therefore, the level of contribution. But, this reform has a less significant impact on the decrease of the level of deficit in the general NPSIF scheme, compared to the other two scenarios. The second reform scenario has the greatest effect on reducing the deficit, as shows the graph below.

Figure 7: The impact of the various proposed reforms on deficit on the general NPSIF scheme



### Conclusions

According to the projection of the population results that indicate an inevitable aging for Tunisia over the next years, the general NPSIF scheme which operates in a pay-as-you-go mode risk to enter in a very dangerous situation.

For this reason, we studied the future of the general NPSIF scheme through the PROST model. The projection results showed us that the deficit will accumulate from one year to another until the final projection period, in the case of constant legislation. For this, we considered three parametric type scenarios to alleviate the more possible deficit of the general NPSIF scheme over the projection period.

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## **Price-Level Targeting versus Inflation Targeting. A theoretical Approach**

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### **Abstract**

This paper provides a comparative analysis on IT strategy and targeting the price level assesses the implications and highlights the challenges of an eventual transition to a new monetary policy strategy. Balancing the advantages (mainly better anchored inflation expectations) and disadvantages (communication difficulties) generated by following a potential price-level targeting strategy and the necessary prerequisites for its functionality (predictive agents, fully familiar with the implications of such a strategy and with complete confidence in the monetary authority) has led us to the conclusion that there is no common acceptance that price level targeting strategy might replace the present IT framework.

**Keywords:** price-level targeting, inflation targeting, inflation expectations, deflation, zero-lower-bound

### **Introduction**

The outbreak of the financial turmoil in 2007, the subsequent financial crisis and the collapse of the economic activity led to the need

of rethinking the monetary policy framework. This approach underlines a series of monetary policy principles unchanged under the international financial tensions, but also a number of elements to be reconfigured. Custom academic discussions on the global turmoil in terms of monetary policy strategies center on three potential modifications: setting a higher inflation target, monetary policy horizon broadening and the shift from IT to price level targeting.

The present paper focuses on the third aspect mentioned, in order to identify the opportunity and feasibility of adopting a new monetary policy strategy, namely the price-level targeting, in the context of at least the temporarily abandonment of inflation targeting. Under an IT regime, after a shock hits the economy, the Central Bank acts to bring inflation back to the target level, regardless of the permanent effects of that shock on the price level. In contrast, a price level targeting strategy implies that the Central Bank would act to restore the price level to its initial value. This difference, although it might be considered minor, has complex implications to the formation of price expectations, the leadership, credibility and communication of monetary policy.

Our paper, which aims to identify and analyze the potential impact of price-level targeting, is structured as follows. The first part illustrates the main ideas in the literature, the second part offers a comparative approach of the two monetary policy strategies, the third explains the consequences in terms of the new strategy benefits; the fourth part presents the associated challenges and the fifth highlights the conclusions and future directions of analysis.

### **Literature review**

The academic literature focused on the subject of price level targeting is broad enough, sharply in contrast to the lack of practical experience in the field.

For the present paper, mainly oriented to emphasize the strengths and drawbacks of the potential application of price-level targeting, it is extremely important to balance the theoretical and empirical approaches in terms of implications arising from the use of such a monetary policy strategy.

Thus, the first advantage of price targeting compared to the IT is the uncertainty limitation on the future long-term price level (Fillion and Tetlow, 1994), which leads to a whole plethora of positive effects.



Besides the obvious positive effects of accentuated price stability, reduced uncertainty generates strong anchored price expectations; thus, the price level targeting strategy manifests as a true automatic stabilizer (Fisher, 1994; Mishkin, 2011). The stabilization of inflation expectations increases the short-term macroeconomic stability (Svensson, 1999; De Resende et al., 2010).

Another positive effect associated to the price level targeting feature of automatic stabilizer, of great interest in the present context, is the limitation of cases frequency related to zero-lower-bound issues, i.e. an easier exit from the liquidity trap (Eggertson and Woodford, 2003; Mishkin, 2011; Coibion et al., 2010). Moreover, a better anchoring of inflation expectations due to the new monetary policy strategy implies a greater flexibility in addressing financial stability (Carney, 2009).

However, the potential benefits of targeting the price level are conditioned to a number of mandatory prerequisites. The emergence of these advantages depends on the anticipatory nature of agents decisions (Vestin, 2006; Amano et al., 2011). At the same time, the implied benefits of price-level targeting require a full agents' understanding of its functioning (Bank of Canada, 2011). Therefore, the process of learning plays a key role (Gaspar et al., 2007). The full credibility of the central bank's commitment ends the series of preconditions necessary to achieve the benefits of a potential use of price level targeting. Only a credible Central Bank will be able to firmly anchor inflation expectations to provide the outcomes of price-level targeting as automatic stabilization mechanism (Masson and Shukayev, 2011).

The major weakness of the new strategy compared to inflation targeting is the complicated communication of monetary policy, both of the target itself and the current decision-making process (Kahn, 2009; Ambler, 2009; Mishkin, 2011). Another impediment in the implementation of price-level targeting is considered to be the strong exposure to time inconsistency problem (Evans, 2010; Masson and Shukayev, 2011). In addition, another challenge to a potential new strategy would be determined by the increased volatility of relative price shocks, respectively higher output volatility (Fillion and Tetlow, 1994, Svensson, 1999) and/or a growth in inflation volatility (Coletti et al., 2008; Murchison, 2010).

Also, another obvious disadvantage of a possible shift from IT to PLT concerns the lack of practical experience in the use of such a monetary policy strategy (Bohm et al., 2011).

### Comparative analysis of the two monetary strategies functioning

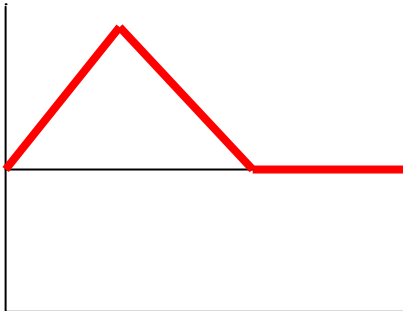
The contrast between the IT and price level targeting occurs due to the different impact of their application on inflation and price level.

Under an IT framework, the emergence of a temporary shock which leads to an inflation rise would make the central bank to pursue a restrictive monetary policy, of increasing the nominal short-term interest rates to bring inflation down to the target. In this case, in the absence of other additional shocks, inflation growth will be only temporary; the indicator would return and remain at its initial value. But, while inflation is only temporary, the corresponding increase in price level would be permanent, displaying a *base drift*, as shown in Figure no. 1.

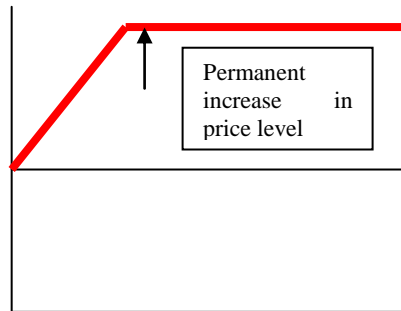
#### Figure no. 1

Time evolution of inflation and price levels under an IT regime

a) inflation



b) price level



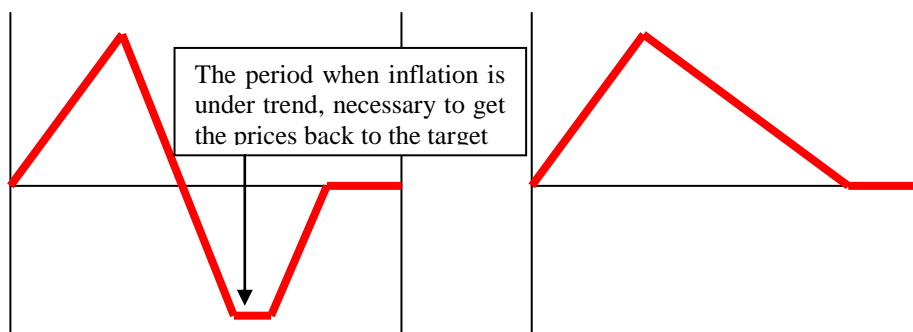
**Source:** Bank of Canada, „Renewal of the Inflation-Control Target”, p.15, [http://www.bankofcanada.ca/wp-content/uploads/2011/11/background\\_nov11.pdf](http://www.bankofcanada.ca/wp-content/uploads/2011/11/background_nov11.pdf)

**Figure no.2**

Time evolution of inflation and price level under a PLT regime

a) inflation

b) price level



**Source:** Bank of Canada, „Renewal of the Inflation-Control Target”, p.15, [http://www.bankofcanada.ca/wp-content/uploads/2011/11/background\\_nov11.pdf](http://www.bankofcanada.ca/wp-content/uploads/2011/11/background_nov11.pdf)

Instead, under a price-level targeting regime, the manifestation of a temporary shock that increases inflation, thus implying a price growth, the Central Bank would seek to promote a restrictive monetary policy, but with a more pronounced degree of tightness to get inflation below the trend, bringing the price level back to the determined value. In this way, the base drift is removed, as demonstrated by Figure nr. 2. The Central Bank does not aim to correct inflation to follow the trend, but to make the price level go back to the target.

The existence of a base drift under an inflation targeting strategy creates uncertainty about the future price level (the Central Bank doesn't consider a reversal in the evolution of prices

### **The evaluation of positive implications of price-level targeting**

Research conducted on various models show that the major advantage of the transition from IT to price level targeting is the increase of economic welfare. The new strategy would enhance this trend based on its ability to provide greater certainty about the long-

term price level and on its features of truly automatic stabilizer. The latter leads to other two positive effects, namely the increase of short-term macroeconomic stability and the avoidance/limitation of zero-lower-bound of nominal short-term interest rate problems and as such, to the economy removal from the deflation trap.

At the first level, the reduced uncertainty about future price levels contributes to achieving higher growth rates due to superior results in terms of relative prices improved transparency, less arbitrary redistribution of income and wealth, diminished risk premia with a positive impact on the capital cost, avoiding the defalcation of resources from production to cover unnecessary operations against rising prices.

Of course, the IT strategy has led to price stability, as the experience of adopting states clearly demonstrates it; however, it is estimated that the use of price level targeting would enable a further strong reduction of long-term prices uncertainty.

Moreover, the capacity of price level targeting strategy to provide greater certainty would lead to a better anchoring of inflation expectations, particularly important when flexibility is needed to address the financial stability. Well anchored expectations would allow an increase of short-term nominal interest rate in order to prevent the formation of asset prices bubbles, without compromising the fundamental central bank's objective of ensuring and maintaining the price stability.

In fact, inflation expectations have a vital role, enhancing the nature of the new framework as automatic stabilizer, the second tier that supports the benefits of such a monetary policy strategy. And this is because the implementation of price level targeting requires the Central Bank to ensure that periods with above trend inflation are followed by periods when inflation is below trend (and vice versa). The anticipation of this inflation dynamic may lead firms to behave in a stabilizing manner under a price level targeting strategy. For example, if at a certain moment, the price level is above the target, firms and households will expect a future level of inflation below the trend.

These anticipations will operate through two channels. The first one is represented by the way firms pricing discourage them to raise prices in response to the initial shock, as expectations of future lower inflation would attenuate the impulse of increasing the current raise. The second channel is the real interest rate changes. Expectations of lower inflation in the future will raise the real interest rate which will

affect consumption decisions, household and businesses savings and investments. Both channels will require to lower inflation, small adjustments of output values.

Thus, the identified stabilizing, auto-correction character of price level targeting, determines a level of employment, output, interest rates and inflation less volatile compared to the figures under an IT regime. The explanation is that in an IT framework the estimations do not play a vital role as agents have no reason to expect that periods of over trend inflation will be followed by under target inflation.

At the same time, the stabilizing nature of price level targeting strategy could lead to a decrease in the frequency of possible confrontation with situations of zero-lower-bound than under an IT regime, and the automated evolution of expectations specific to price-level targeting should result in a smooth exit from a deflationary situation, something of great interest today, when many Central Banks of developed countries are faced with the zero-lower-bound issues.

Thus, the more prices fall below target, the more Central Banks will have to stimulate the economy to offset the price level decrease under the target. In this case, one would image inflation expectations to rise and real interest rates to fall, thereby facilitating the exit from the liquidity trap.

### **Challenges for the monetary policy in the context of price-level targeting**

The positive implications resulting from the potential application of a strategy targeting the price level are, however, strongly counterbalanced by a number of obvious difficulties associated with its implementation. We underline the communication difficulties, much stronger than in the case of an IT regime, a possible exacerbation of monetary policy time inconsistency problem, external shocks of relative prices, and the lack of practical experience in the effective adoption of the new framework.

On the other hand, the successful application of price level targeting, as demonstrated by various econometric models is based on a number of preconditions: it requires that agents pro-actively form their expectations (forward-looking), they are fully familiar with the strategy implications and also have a high degree of confidence in the monetary authority. If these conditions are not met in full (in fact a very likely situation in the real world), the net benefits of price level targeting

mentioned in the previous section will be smaller or even completely canceled.

Price level targeting communication implies a significant communication challenge. Unlike the IT regime, where communication is direct and focused on the inflation target, price level targeting communication is more difficult. In the first place, the difficulty arises when the Central Bank targets an upward trajectory of the price level, which translates into the impossibility to present a single number; the target would be in constant motion and thus more difficult to explain to the audience than an inflation target maintained at a constant level.

A second challenge to price level targeting is time-inconsistency problem. Conducted in a flexible way, the IT strategy does not face this weakness. The same is not true for price level targeting, which may face this problem as follows. Considering the example of a price level targeting strategy at a given time, following a shock, the price level is above the target, which requires the Central Bank to commit to a future inflation below the long term average. This has a positive effect on inflation expectations and lowers the costs to absorb the shock.

However, once the shock disappears and inflation (not prices level) reappears at its optimal long-term level for the Central Bank, and the whole economy is tempted not to comply with the Central Bank announced policies (of not compensating the positive shocks prices by pushing inflation below its long-term average, since this would harm domestic product), prices will not return to the established path. In other words, in real life it may happen that both - the public and professionals - consider short-term gains more attractive. In this context, the Central Bank would be under strong pressure to violate the principle of time consistency

A third problem of the potential implementation of price-level occurs in the event of external shocks in relative prices, very common especially to small open economies. To offset the shocks, the new strategy should produce relative changes of other prices to counter the negative impact. For example, a significant increase in oil prices would make necessary a relative drop of other components in the considered index price to restore the desired trend. To the extent that these other prices prove to be rigid, the adjustment could lead to a higher volatility of output, inflation and interest rates than under an IT regime.

A fourth disadvantage of a possible shift from IT to price level targeting is the lack of practical experience in the use of such a

monetary policy strategy. The experience of Sweden, whose monetary policy during the '30s is often labeled as the only case of price level targeting, it doesn't help a lot because of its short duration and vague implementation elements. All positive and negative implications of price level targeting drawn from the application of different econometric models are based on questionable assumptions and, therefore, remain far too simple to represent a real economy. Therefore, the results returned imply a high uncertainty degree.

Fifth, the success of such a strategy critically relies on a set of assumptions: forward-looking agents' decisions, a strong understanding of its functioning and full confidence in the monetary commitment of the monetary authority. Thus, if in the models identified in the literature, the assumption that agents make decisions in a proactive manner is relaxed, eliminating the stabilizing effect of expectations that prices will systematically return to the target, the advantages of this potential new strategy against an IT regime rapidly diminish.

However, for the price level targeting to produce the expected beneficial effects it is highly necessary that agents completely understand its mechanism. Households and firms should see that medium-term inflation expectations increase (decrease) when current inflation decreases (increases) in order to generate the specific advantages of price level targeting strategy automatic stabilization. If their expectations do not follow this path, the price level targeting could prove to be destabilizing compared to the IT regime. Closely related to the need for a full agents' familiarization with the new strategy implications, as an essential precondition for the success of price level targeting, one of the challenges is determined by the length of time during the agents learn about its functioning mechanism, given that the benefits would be drastically reduced if the learning process is too slow.

Obtaining the comparative advantages also involves the credibility of the Central Bank's commitment to fully compensate for past deviations from the price targeted trajectory. If agents doubt the willingness of the Central Bank to limit the output by tightening monetary policy in order to reverse the trend of rising prices, expectations will not move enough to provide the automatic stabilization feature benefits of price level targeting strategy. In this context, the IT framework could prove more appropriate than the new strategy.

### **Conclusion**

The fact that the recent financial crisis has highlighted the idea that the problem of zero lower bound monetary policy interest rate may be more serious than previously thought, has brought to the forefront of discussion the potential shift from IT to price level targeting, at least temporarily, until the disappearance of deflation threat.

While applying an IT strategy has reduced uncertainty and costs associated to high and volatile inflation, the adoption of a price level targeting regime would make the long-term price uncertainty reduction even stronger. Thus, while the IT approach is *bygones is bygones*, the price level targeting approach is *history dependent* (dependent on the past). This difference, although it may be considered minor, has complex implications for the leadership, credibility and communication of monetary policy and price expectations formation, a better expectations anchoring on their future level, as the core of the price level targeting strategy.

Bringing together the associated benefits (uncertainty reduction on long-term price level leading to better anchored inflation expectations, automatic stabilizer manifestation with two favorable results: greater short-term macroeconomic stability and limited likelihood of zero-lower-bound of short-term nominal interest rate occurrence and respectively, the smooth exit out of this situation) and challenges (difficulty of public communication, high exposure to the problem of time inconsistency and volatility due to relative prices shocks, the lack of practical experience in the use of such a monetary policy strategy, predictive agents, familiar with the strategy' implications and confidence in the willingness and ability of the monetary authority to meet its commitments) leads to the idea that, in the real world, under normal circumstances, we could make a fully covered statement on the price level targeting strategy superiority over the IT regime. If the economy fell into the liquidity trap, potential benefits may predominate and therefore we propose as future research direction, the analysis of price level targeting strategy behavior in the context of deflation risk zero-lower-bound of short-term nominal interest rate.



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## **Progressive tax or flat tax**

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### **Abstract**

The state tries to achieve a balance between efficiency and equity, by using fiscal tools. On the one hand, the state must ensure through fiscality, the collection of funds for social, economic, international cooperation, etc. programs. On the other hand, taxation should be organized so that it does not put excessive pressure on the disadvantaged, which translates in a redistribution of income.

**Keywords:** fiscal tax, flat tax, progressive tax

### **Introduction**

Progressive taxation defines a system of imposing a progressive tax on personal income by which the tax rate increases as the taxable base amount increases. Taxation using percentage rates of income tax is widely applied, being contemporarily the main method used as it ensures a proper correlation between tax burden and both: the taxpayer's economic strength and personal financial status.

### **Material and Methods**

Taxation is complex in measures and operations, conducted by law, aimed at determining the tax to be imposed on an individual or legal entity. Taxation involves both - a political side which identifies the taxpayer and the tax base and a technical side which includes the

methods and techniques for measuring the taxation base and for determining the tax amount.

Through taxation, the state tries to achieve a balance between efficiency and equity. On the one hand, the state must ensure, through fiscality the collection of funds for social, economic, international cooperation, etc. programs. On the other hand, taxation should be organized so that it does not put excessive pressure on the disadvantaged, which translates in a redistribution of income. As for efficiency and equity, some financial and economic theories emphasize efficiency, while other focus on equity. Taxation is achieved by virtue of principles which have been defined by many economists over time.

### **Literature review**

The modern financial theory formulates and promotes principles of fiscal equity, financial policy principles, economics principles, social and political principles, each translated into several components which emphasize certain attributes and characteristics of their content.

Based on the fiscal equity principle, there are two main taxation methods: the lump sum taxation and the percentage tax rate. The lump sum taxation is quite limited because it does not properly address the correlation between fiscal burden and the taxpayer's economic strength. It is used with indirect taxes, such as excise duty on cigarettes and alcohol or on certain local taxes.

The percentage tax rate is widely used today as it ensures a proper correlation between tax burden and both, the taxpayer's economic strength and personal financial status. There are three basic types:

- proportional tax;
- progressive tax, with the following variations:
  - simple progressive tax,
  - compound progressive tax or progressive tax in installments;
- regressive tax.

*The proportional tax* implies using the same percentage rate regardless of the taxable base amount.

*The progressive tax* requires different percentage rates according to the taxable base amount variation. It allows the division of taxable base using tax brackets, which are cutoff values for taxable income.

*The regressive tax* does not appear as a practical way of taxation, but only as a consequence of indirect taxes. These taxes are calculated as marginal percentage or lump sum rates, becoming a constant burden for each consumer of a certain product indirectly imposed.

The variety of consumer's income types relatively implies that taxes should be smaller as the income increases. Thus, taxation becomes regressive. Tax calculation is a set of operations regarding identification of tax base, determination of tax amount and tax collection.

When referring to flat tax, one can say that it involves replacing the complex set of various taxation types depending on income with a system in which the state declares a single tax rate for all income exceeding a certain predetermined level. In general, the minimum taxation level is quite low in order to stimulate the taxpayers to fulfill their tax obligations. Thus, global income is subject to single taxation. A smaller tax rate implies a better cash flow and leads to an increased willingness' to pay due taxes, a decrease in taxes leading inevitably to lower revenues for the state budget. Many economists consider that implementing a progressive taxation system will have a negative impact on the economy. Reviving the economy requires increased consumption and investment, a higher level of taxation leading to opposite results. The current volatile international context limits the capital flows needed for financing economic growth and the saving rate of those with higher earnings will strongly decrease, further reducing the funds available for domestic investment.

### **Results and Discussion**

Statistics show that the budget revenues collected from income tax are higher for the period in which the flat tax applied, compared to the period when Romania applied the progressive taxation system.

Introducing progressive taxation rates, which will probably require a set of tax deductions, will increase bureaucracy.

The experience of the European countries shows that progressive taxation is useful only accompanied by a deductions system that allows the state to direct private expenditures toward certain areas of social interest, such as education, health or to reward families with children.

Most European countries apply substantial deductions for employees with dependent children. In countries with progressive taxation, these deductions are managed by the global income statement. Some economists suggest, in the case of progressive taxation, a

deduction system for the employees with high earnings, taking into account the amounts voluntarily paid to private pension and health funds. It is a good proposal considering the tendency of concealing high incomes, leading to tax evasion.

### **Conclusions**

A differentiated taxation system will level financial inequalities, generating additional social benefits. In this regard, Richard Wilkinson argues that the more unequal a society, the more damaged the lifestyle of middle and lower class people becomes: they are likely to be less healthy, less likely to be involved in community life, more likely to be obese and more likely to be victims of domestic violence.

Differentiated taxation is a solution for governments with budgetary issues, as it allows determining a more efficient number of taxes to be collected, but at the same time, these governments are exposed to the risk of enabling fraudsters to identify new ways for tax evasion.

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## **Transfer pricing file- a contextualized Approach. Case Study**

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### **Abstract**

The transfer price is basically the price used for transfer of tangible and intangible assets between related parties and it should be determined on the basis of market value without being influenced by the relationship of affiliation. However, if for services or tangible assets, the comparison of the transfer price to the market one is relatively easy to achieve, for the intangible ones, quantifying future benefits waived by the affiliated person compared to the situation in which it would be independent is harder to be established.

**Keywords:** multinational, transfer price, market price, transaction, intra-group transactions

### **Introduction**

The transfer price is basically the price used for transfer of tangible and intangible assets between related parties and it should be determined on the basis of market value without being influenced by the relationship of affiliation. However, if for services or tangible assets, the comparison of the transfer price to the market is relatively easy to achieve, for the intangible ones (patents, trademarks, brand etc) quantifying future benefits waived by the affiliated person compared to the situation in which it would be independent, is harder to be established.

According to the Tax Code, the tax authorities may reconsider transfer pricing and, consequently, to adjust income or expense related to any of the persons involved in a transaction, if the price at which the transaction was effected is not a market price, respectively the price at which the transaction would've been completed under the same or similar conditions by independent persons. According to the Methodological Norms for the application of the Tax Code, transactions between the Romanian legal entities are not subject to adjustment by the tax authorities, only those signed by Romanian legal entities with affiliated non-resident persons as well as with Romanian individual persons.

This research topic was chosen for the following reasons:

Transfer prices regime is the "end point" of ingenuity on exploitation of tax legislation, as it is the glue that connects existing tax rules in different national markets. Moreover, starting from the assumption that in the cost structure of the products can also be found fiscal influences (sometimes not insignificant), 'host' firms of the transfer mechanism of taxable material achieve, although not exactly in an "orthodox" manner, an "additional income", which can then be used to obtain a "Power" position in a particular market.

Starting from the premise that legislative measures are the central pillar in the fight against cross-border tax evasion in the area of transfer prices, it is understood by itself that it is necessary to eliminate redundancies existing in the legal framework, both nationally and internationally, and from the desire of an uniform treatment of the matter, it is necessary the legislative "matching" of the referential domestic tax laws of the Member with the regulations contained in the OECD transfer prices Guidelines and also with the principles structured in the Code of Conduct of transfer prices.

The subject of transfer prices has become increasingly discussed over the last two years, and the attention of the tax authorities in this area had a very important role in this respect.

In Romania, justification by taxpayers of the transfer prices is based on the Fiscal Code, on its implementing rules, as well as on the provisions of the OECD Guidelines on Transfer Prices. In short, under these provisions, a taxpayer's transactions with related parties have to be undertaken in market conditions, i.e. respecting business and financial conditions that are to be expected and agreed between independent persons, on the background of comparable circumstances.



## **Case Study: transfer prices file at SC. Romvag S.A**

### **1. Company Overview**

SC. Romvag S.A is a company for the production of freight wagons, of the Railways Industries International Group.

SC. Romvag SA is a joint stock company founded in 1990, headquartered in Bucharest, Calea Vacaresti, no. 88-103, Romania, whose main activity is the production of freight cars.

SC. Romvag SA is certified as a producer of freight wagons by the Romanian Railways and by relevant entities in other European countries such as Germany, Belgium, Switzerland, Austria, France, Great Britain, Slovakia, Italy, Sweden, Hungary, the Netherlands and the Czech Republic.

### **2. Financial data**

Main consolidated financial data of the Group for the period 2006 - 2010 are shown in the table below:

**Table no. 1. Financial data of the group for the period (2006-2010)**

<i>Financial information</i>	<i>In 2006</i>	<i>In 2007</i>	<i>In 2008</i>	<i>In 2009</i>	<i>In 2010*</i>
<b>Turnover</b>	67,284	110,260	176,146	188,696	67,818
<b>The net result</b>	53,796	-8,922	-5,661	-14,004	-49,422
<b>Total assets</b>	196,523	118,285	171,875	188,541	146,404

*Source:* own compilation

### **3. General description of transactions between related parties from the European Union in the IRS group**

During the 2006 – 2010 period, within the IRS Group were developed the following main categories of transactions between related parties from the European Union:

- production and sale of freight wagons;
- production and sale of bogies;
- selling axles;

#### **4. Transfer prices and advance price agreement methodology**

##### *Transfer prices methodology*

The methodology applicable for the setting of transfer prices within the major categories of related party transactions carried out in the IRS Group is, as follows:

- production and sale of wagons by the producing entities from the freight wagons Division to related parties.

Transfer price is set at recorded production costs level plus a profit margin of up to 5%.

- production and sale of bogies by the producing entities from the freight wagons Division to related parties.

Transfer price is set at recorded production costs level plus a profit margin at market value.

- selling raw materials and materials between affiliated entities.

Transfer price is set at recorded production costs level (acquisition cost or standard cost) plus a profit margin at market value.

- selling subassemblies and components between affiliated entities.

Transfer price is set at recorded production costs plus a profit margin at market value.

Transfer price is set at the unamortized book value level plus a profit margin at market value.

- transport services carried out by entities in the transport division to the producing entities from the freight wagons Division.

Prices charged for transportation services are established using a methodology similar to that used in setting tariffs for companies providing these services in relation to independent parties.

#### **5. Advance Price Agreements**

During the period covered by this case (i.e., 2006 to 2010), there is no information about requesting or obtaining by any entity in the Group IRS of an advance price agreement.

#### **6. Holders of intangible assets**

All intellectual property rights related to the Group's products are owned by other companies in the Group.

SC. Romvag SA does not have significant intangible assets and also pays no royalties to related parties for the use of intangible assets.

## **7. Description of related party transactions**

In the period January 1, 2006- December 31, 2010, SC. Romvag was involved in the following types of transactions with related parties from the IRS group:

- production and sale of freight wagons by SC. Romvag S.A to IRS Industries;
- production and sale of bogies by SC. Romvag S.A to IRS Industries and Meva.

## **8. Application of transfer prices method**

After selecting the transfer price method, the next step is to apply this method to analyze compliance of the tested transaction with the principle of market value.

To test compliance with the principle of the market value of the sale transaction of finished products by manufacturers to their affiliated parties by applying the net margin method must be taken the following steps:

- identifying the party that will be subject to analysis (the tested part);
- developing a comparability study (i.e. identification of comparable companies and choosing an indicator of profitability);
- setting a market range;
- testing compliance with the principle of market value by comparing the profit margin applied by the tested part to the values included in the market range.

### **8.1. Identifying the party that will be subject of the analysis**

In order to analyze the compliance of the tested transaction with the principle of market value, you must first select the affiliated company that shall be subject to review (the tested part). The tested part is that participant in a transaction between related parties whose profits will be analyzed for compliance with the principle of market value.

After the functional analysis performed, we determined that producers are the least complex part of the transaction analysis perspective, being without marketing or sales functions and not taking risks related to market evolution.

## **8.2. Comparability study**

### *Search Strategy*

According to the Romanian legislation, the search was first done at a local level, on companies with headquarters in Romania.

As there weren't identified comparable companies in Romania that can be used as a comparability reference for Producers, in accordance with the provisions of the Order 222/2008 on the content of the transfer prices file, we expanded our geographic search at EU level.

The search process involved examining companies from the Orbis database, eliminating companies that do not meet the selection criteria and identifying those companies that could be used as a comparability reference for the production of wagons or similar products.

A summary of the search strategy is presented below:

- Geographic criteria
- Activity code
- participants in subsidiary
- stock
- turnover
- negative exploitation result

## **8.3. Selection of the profitability indicator**

Profitability indicator used in this comparability study is the profit margin related to operating costs (of exploitation), which express a company's profitability by reference to the total operating costs. This profitability indicator accurately reflects manufacturer's profitability, considering the costs that it registers for adding value to products.

## **8.4. Setting market range**

After identifying a set of companies performing comparable activities to those held by Producers and selecting an indicator of profitability, the next step is to establish the market range. In accordance with local regulations, market range is defined as the interval between the lower quartile and the upper quartile.

Results for companies in the final sample were calculated as a weighted average using financial data for a period of five years (i.e. 2006-2010) and are presented in the table below.

**Table no. 2. Profit margin related to operating costs (2006 - 2010)**

<b>Profit margin related to operating costs (2006 - 2010)</b>						
	<i>No. companies</i>	<i>Minimum</i>	<i>Lower quartile</i>	<i>Median</i>	<i>Top quartile</i>	<i>Maximum</i>
Final sample	9	1.58%	<b>3.01%</b>	<b>3.72%</b>	<b>11.01%</b>	11.92%

*Source:* own compilation

The profit margin related to operating costs for the independent companies included in the final sample for the period 2006 - 2010 range between 1.58% and 11.92%, calculated market range is between 3.01% (lower quartile) and 11.01% (top quartile), with the median at 3.72%.

In accordance with the local law, this period (i.e. between 3.01% and 11.92%) is considered to provide a relevant estimate for the market value.

### **8.5. Analysis of compliance with the principle of market value**

#### **■ Results of the tested company**

In the period under review, according to the methodology for setting the transfer price, for the sale of finished products to related parties Producers have applied a 5% profit margin.

#### **■ Analysis of the compliance of the tested transaction to the principle of market value**

In order to analyze the compliance of the tested transaction with the principle of market value, we compared the results obtained by independent producers with limited functions and risks from the final sample with the profit margin applied by producers. As you can see the 5% profit margin is within the range of comparison (between 3.01% and 11.01%) which shows that the market value of the transfer prices charged was not distorted by the influence of transfer prices.

### **Conclusion**

The objective of this case was to determine whether transfer prices applied to transactions carried out between Astra Wagon and its related parties during 2006 and 2010 are based in accordance with the principle of market value.

Checking the consistency with the principle of market value of intra-group transactions undertaken by Astra Wagon was made for each type of intra-group transaction separately and included:

- Understanding of the economic context in which the Company operates and has generated the need to conduct transactions;
- Feasibility analysis of applying each method for setting transfer prices in order to assess the market value of intra-group transactions performed, considering the circumstances and characteristics of each type of intra-group transactions in part;
- applying the selected transfer price method in order to establish the compliance of each intra-group transaction with the principle of market value.

Following the analysis, we concluded that intra-group transactions carried out between Astra Wagon and its affiliates during 2006 and 2010 were conducted respecting the principle of market value, as it is defined in the OECD Guidelines and national legislation.

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- \*\*\* N.A.F.A. President Order no. 222/2008 regarding the contents of the transfer prices file

## **Trade Companies and their Classification**

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### **Abstract**

The Romanian legislation does not define anyhow the concept of companies. It was the merit of the doctrine, which attempted such a definition, starting usually from the provisions of the Civil Code, which in art. 1491 defines the civil society, for the purpose of the memorandum of the association<sup>1</sup>. For that matter, also in the specialized foreign doctrine (ex. the French doctrine) companies are defined based on similar concepts, but standardized by the Civil Code<sup>2</sup>. The two meanings that the company has to be regarded through, also explain the very specific legal matter, a matter of concepts resulting from understanding the concept of memorandum of association and the company-institution. Thus, the contractual conception, imposed by the development of the contract theory in the last century, explains the existence of the companies starting from the validity conditions imposed to any contract and from the contractual techniques that establish the relationships formed within the society (for example, the company management is based on a mandate contract under which the executive operates).

**Keywords:** social capital, national companies, economic interest groups

### Introduction

The company can be seen in at least two ways:

- A legal institution itself, considered as a body, usually set on associative bases, in order to obtain a certain profit for those who have joined, and in pursuit of commercial activities;
- A contract with its own characteristics, determined by the specific purpose for which the agreement was reached. To be observed that the Romanian legislation does not define anywhere, in none of the means, the concept of company. It was the merit of the doctrine, which attempted such a definition, starting usually from the provisions of the Civil Code, which in art. 1491 defines the civil society, for the purpose of memorandum of association<sup>1</sup>. For that matter, also in the specialized foreign doctrine (ex. the French doctrine) companies are defined based on similar concepts, but standardized by the Civil Code<sup>2</sup>. The two meanings that the company has to be regarded through, also explain the very specific legal matter, a matter of concepts resulting from understanding the concept of memorandum of association and the company-institution. Thus, the contractual conception, imposed by the development of the contract theory in the last century, explains the existence of the companies starting from the validity conditions imposed to any contract and from the contractual techniques that establish the relationships formed within society (for example, the company management is based on a mandate contract under which the executive operates).

The disadvantages of generalization of such a theory lie in the specific issues that shape a company, issues that can not be explained only by contractual arrangements (for example, a company enters actually in the commercial circuit only after its registration at the Trade Register, meaning based on an administrative formality, so that the simple manifestation of the will of the shareholders would not be sufficient to enable the company itself).

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<sup>1</sup> St. D. Cârpenaru, *op. cit.*, p. 143 and O. Căpățină, *Societățile comerciale*, 2<sup>nd</sup> edition actualized and complete, Ed. Lumina Lex, București, 1996, p. 57-66; R.P. V on i c a, *Dreptul societăților comerciale*, Ed. Holding Reporter și Albastră, București, 1998, p. 19; R. Petrescu, *Constituirea și modificarea societății comerciale*, Ed. Oscar Prinț, București, 1998, p. 9-11; Elena Cârcei, *Drept comercial român*, Ed. AII Beck, București, 2000, p. 46 and next

<sup>2</sup> Ph. Merle, *Droit commercial, Societes commerciales*, 3<sup>rd</sup> edition, Dalloz, Paris, p. 1



However, such a conceptualization could not give any explanation of the existence of the sole proprietorship type companies (limited liability company with sole shareholder, standardized by the Romanian law) because the agreement will, fundamental to any contract, is missing.

This explains why it was tried to define the company through the institutional prism, given the fact that the judicial institution is a set of rules that organizes, in a sustainable imperative way, a group of people having a well defined purpose.

### **Classification of the companies**

A first classification of the companies was achieved through the Law no. 15/1990, regarding the transformation of the former state socialist units in autonomous companies. Given the time when this law was passed, it tried to make a division of the companies, taking into account the equity holder. According to the Law no. 15/1990, the companies were classified as follows: state owned companies; companies with mixed capital (public and private); privately owned companies.

Regarding the situation of the companies owned by the state (which at the time the law was adopted, were the majority), these lacked the quality of being public legal persons. The assets of the company belonged to the company (the company having ownership), the state being nothing else but sole shareholder, holder of the company's capital<sup>3</sup>. Such a solution, moreover, is fully justified, since the law itself, in art. 20, sets out the way in which, after an evaluation of the assets, these will become the property of the company.

After the adoption of Law no. 31/1990, it was reconsidered the classification of the companies by their nature, in companies with equity and companies with partnership. Along with the equity and partnership companies, as a bordering company, which borrows also specific features of equity and partnership companies, was founded the limited liability company, a company that, particularly in the current socio-economic circumstances in Romania, is the most commonly used form.

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<sup>3</sup> P. Filipescu, *Dreptul de proprietate și alte drepturi reale*, Ed. Actami, București, 1993, p. 56

The doctrine of specialty<sup>4</sup>, proposed also other criteria for the classification of the commercial companies, namely:

- based on the **liabilities of the associates**:
  - Companies where the associates have limited liability;
  - Companies where the associates have unlimited liability.
- based on the **social capital structure**:
  - Companies with social capital divided into shares;
  - Companies with social capital divided into shares of interest.
- based on **securities**:
  - Companies that issue securities;
  - Companies can not issue such securities.

To observe that in reality, all these classifications are circumscribed to the separation of the companies in partnership and equity companies, taking into account of the specific features of the limited liability company. Thus, for example, concerning the liability of the members, it is unlimited in case of partnership companies and limited at the contribution to the social capital, in the case of the capital companies. Limited liability companies as their name indicates, borrowed this feature from the capital companies, associations, with limited liability. Similarly, the capital companies require a social capital divided into shares, while the partnership companies have the social capital divided into shares of interest. For limited liability companies, the social capital is divided into shares, which represent a specific form of the shares of interest<sup>5</sup>.

The companies can be classified also by their **settlement mode**. From this point of view, there are:

- Companies settled by the **General Law** (Law no. 31/1990, republished);
- Companies governed by **special laws**: Banking companies governed by Law no. 58/1998; Agricultural companies, governed by Law no. 36/1991 and Insurance companies, governed by Law no. 32/2000.

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<sup>5</sup> In theory have been pointed out the similarities that exist, especially in terms of the legal status between the social shares and the shares of interest. To see, I.L. Georgescu, op. cit., vol. II, p. 15-16. This very high similarity between the two structure elements of a social capital makes us believe that ultimately, the social shares constitute an evolved form of the shares of interest, specific to the partnership companies.

Through the Government Emergency Ordinance no. 30/2000, the very **existence of the autonomous administrations** was fundamentally changed, as they were governed by Law no. 15/1990. Under these circumstances, part of these administrations was dissolved, another part was transformed, and finally, those considered functioning in key areas relating to the state interests continued to exist in its original form. In the case of the transformed autonomous administrations, they were reorganized as **national companies** and national societies, which have been founded, are considered trade companies, according to Law. 15/1990. Moreover, such companies with a certain specific are also found in other states. For example, in **France**<sup>6</sup> (Ph. Merle, *Droit commerciales. Societes commerciales, op. cit.*, p. 12-14) are considered to be **companies with a specific legal status**:

- **Co-operative companies**, in which the associates are at the same time either workers employed in the service of that company (in the case of production co-operatives) or suppliers of products for the company, or customers (in the case of consumption cooperatives). The decisions in these forms of companies are adopted under the "one man, one vote" rule;
- Companies that involve the **participation of the workers**, who, necessarily, are established as **joint stock companies**, and allowing the participation of the employees at the benefits and at the effective management of the company.

Similarly, when in Romania through the law was intended to ensure the acceleration of the privatization, a similar formula was introduced by the Law no. 77/1994 regarding the associations of the employees and of the managers of the companies to be privatized, abolished by the Government Emergency Ordinance no. 88/1997 regarding the privatization of the companies, a law through which, among other things, were established the P.A.S.

- **Companies with variable capital**, companies where the capital varies constantly, either by increasing it from payments made by the existing associates or by those who wish to acquire such a quality, or by regularly reducing the capital, after the withdrawal of some associates. Such capital variability clauses are prohibited by the French law, for the case of the joint stock companies, other than the co-operative ones or those founded as such, specifying the variability of the capital, beginning with 1981, when in the French law were assimilated the provisions of the second European Directive from 13 December 1976.

• **Mixed economic companies**, founded by associating the private capital with a public collectivity.

Since 1983, such associations were admitted also at a **local level**, being founded local mixed economic companies. Such companies could be compared with the state-owned companies, given the fact that they necessarily must be founded in the form of joint stock companies, and the majority of the capital is held by the public power. Also, inside the decision system, the majority vote belongs also to the authority, whether local or central. The purpose of founding such companies is the joint exploitation of some public services of commercial or industrial character, or other activities of general interest for the society. To be observed that the **Romanian law** recognizes such associations, but only under **joint venture agreements**, the association thus created, according to the Commercial Code, being without legal personality. The intervention of the state or its organs within such companies is possible, but only if the state participates as a simple legal entity and not as an authority.

• **Nationalized companies**<sup>7</sup>, in which the state owns the full capital. Even though after 1986, as a result of new regulations, it was aimed to transfer ownership from the state to the private area, such companies have continued to exist. But to exist, they must expressly and restrictedly be provided by the law.

It can be noticed that, practically such companies are similar, in principle, with the existing autonomous administrations in Romania, in activity areas of highest interest for the national economy, and these, according to the Government Emergency Ordinance no. 30/1997, being nothing else but those expressly and restrictedly provided by the law. Also, in the French doctrine, companies are classified according to the **scope of business**, namely real estate, agricultural area, banking and credit companies, regional development companies, founded as specialized financial institutions, of private law, joint stock and listed on the Stock exchange companies<sup>8</sup>.

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<sup>7</sup> It is the case of the Renault plants, which from 1945 became National Administration of the Renault plants, as a result of the manifestation of the national will for a national reconstruction, subsequent to the Second World War. However, after the association with the Volvo company, Renault has turned into a joint stock company (with shares), of common law, in which the state holds at least 3/4 of the voting rights.

<sup>8</sup> For further information see P. Guillemin, D. de Margerie, *Les sociétés de développement régional*, Bulletin Joly, 1991, p 675

Also, **partner companies inside the liberal professions** could be founded. In most of the times, these companies are founded as civil companies, but beginning with 1991 they have been created companies for the exercise of the liberal professions in the form of specific companies<sup>9</sup>.

At the origin of the creation of such companies, subject practically to the trade regime, was the consideration - as absolutely necessary - of granting for the liberal professions of some specific means to cope with the international competition, to allow the professional groups to build up enough capital to achieve successfully the professional activity, but also to enlist them in a more advantageous tax system.

#### • **The Economic Interest Groups**

By the Law no. 161/2003, inspired by the French law (the Economic Interest Groups) the legislature regularizes for the first time the Economic Interest Groups (EIG) and the European Groups of Economic Interest (EGEI) Title V, Chapter II, Art. 232-238, provisions that are supplemented by the Law no. 31/1990, with the Government Emergency Ordinance no. 76/2001, as amended, regarding the simplification of some administrative formalities for the registration and the functioning authorization of the traders.

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<sup>9</sup> Until now, there was the possibility of creating under the form of companies of some associations of liberal professions (such as the accountants, architects or legal advisors). For further information, see J.J. Daigre, *Les sociétés en participation de professions liberales reglementees et la reforme des sociétés civiles professionnelles*, Bulletin July 1991, p 369

## **The Effects of Remittances on Inflation: Evidence from Bangladesh**

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### **Abstract**

Like many developing countries, remittances are relatively larger capital inflows in Bangladesh in the recent years. Hence, understanding the impact of remittances on the macroeconomic variables such as inflation is essential for the policy makers of the recipient economy. Incorporating remittances as an exogenous variable to the standard inflation function, this paper verifies how it affects the inflation rate in Bangladesh in the 1972-2010 periods. Applying Vector Autoregressive (VAR) techniques, the empirical results find that a one percent increase in remittances inflows increases inflation rate by 2.48 percent in the long run, whereas no significant relationship is evident between these two variables in the short-run in Bangladesh.

**Keywords:** remittance, inflation, Bangladesh, vector Autoregressive

### **Introduction**

Remittances are relatively larger capital inflows in many developing countries in the recent years. The World Bank reports that the officially recorded remittances received by developing countries rose to US\$ 240 billion in 2007 from US\$ 75 billion in 2002. Like many other developing countries, there has been manifold increase in

remittances flow into Bangladesh in the last decade. The remittance inflow has increased from US\$ 2.0 billion in 2001 to US\$ 4.3 billion in 2005 and US\$ 10.8 billion in 2010. The growth of remittances inflows has outpaced foreign direct investment (FDI) and other official development assistance (ODA) in Bangladesh (Nabi and Alam, 2011). As a major source of foreign exchange, it has growing the development potentials in Bangladesh. Hence, understanding the impact of remittances on the macroeconomic variables such as inflation is essential for the policy makers of the recipient Bangladesh economy.

### **Literature review**

Literature on the effects of remittances mostly focuses on the exchange rate (e.g. ‘the Dutch Disease’) and terms of trade issues. Adelman and Taylor (1992), also Balderas and Nath (2008) pointed out that through their direct and indirect effects on aggregate demand, remittances may have effects on inflation. Remittances are spent partly on consumption and partly on investment. The direct effect of remittances on aggregate demand is resulted by the increase in consumption expenditure of the receiving households. In the case of Mexico, Durand et al., (1996) find that almost three quarters of the total reported remittances are spent on consumption. The scenario is almost similar in Bangladesh. A large portion of the wage earners working in the Middle East, are mostly member of the lower strata of the society. Their families have modest means; because of that, they are likely to spend most of the remittances to finance large durable goods such as furniture, appliances, housing, medical care and education (Balderas and Nath, 2008). The increase in the consumers’ durables shifts in demand which creates an inflationary pressure in the economy.

Aggregate demand may also increase if remittances increase investment and resulted in demand-pull inflation. Several empirical studies on different countries (Martin, 1991 and Taylor et al., 1996) find that remittances fail to contribute to the substantial capital formation, only a very small percentage of remittances devoted to investment and savings. Like many developing countries, in Bangladesh, remittances are channeled into real estate and consumers’ durable goods. However, a good number of studies (Gilani, 1998; Adams, 1998; McCormick and Wahab, 2001; Dustman and Kirchkamp, 2001) indicate that remittances rather consistently contribute to significant gains in saving and investment, although the recipient’s economy come under inflationary

pressures and prices rise significantly in certain sectors (Kazi, 1989). In Bangladesh, while remittances are targeted primarily to consumption, a significant share goes to non-trade goods, like land and housing. The very sharp rise in land and housing prices in recent years in Bangladesh is also explained to be resulted by the fast growing remittances inflows. Besides boosting excess demand through increase in consumption and investment, remittances raise reservation wages which also results in an inflationary pressure (Feiler, 1987; Looney, 1990).

Amuedo-Dornates and Pozo (2004), Bourdet and Falck (2006), Lopez, Molina and Bussolo (2007), Jansen, Naufal and Vacaflores (2007) and Narayan, Narayan and Mishra (2011) show that increase in remittances generates an increase in inflation. While Katseli and Glytsos (1986) in their study on Greece find that remittances affects negatively the inflation in the home country. Ball, Lopez and Reyes (2012), investigating the relationship between remittances, inflation and exchange rate regimes in 21 small open economies concludes that under fixed exchange rate regimes, an increase in remittances generates an increase in inflation, while under flexible exchange rate regimes it decreases inflation. The objective of this paper is to investigate the relationship between remittances inflows and inflation in Bangladesh, including remittances as an exogenous variable to verify how it affects the inflation rate.

### Methodology and Data

Since the issue of causality is at the foundation of any study that examines an economic relationship, the empirical analysis starts with the Granger-causality tests to determine if Remittance (RM) Granger-causes Inflation (P) and/or inversely Inflation (P) Granger-cause Remittance (RM).

A formal test for Granger-causality running from RM to P is:

$$P_t = \alpha_1 + \sum_{j=1}^t \beta_j P_{t-j} + \sum_{k=1}^t \varphi_k RM_{t-k} + v_t \quad (1)$$

A formal test for Granger-causality running from P to RM performed using a symmetrical test is as:

$$RM_t = \alpha_2 + \sum_{l=1}^t \theta_l RM + \sum_{m=1}^t \rho_m P_{t-m} + \omega_t \quad (2)$$



Based on the results provided by the Granger-causality tests, this study draws an empirical relationship between the variables concern. In modelling empirical relationship between remittances flows (RM) and inflation (P), the study uses a Vector Autoregressive (VAR) methodology, including control variables based on the standard theory of inflation. Following Balderas and Nath (2008), Balderas (2009) and Ball, Lopez and Reyes (2012) and a number of other papers (Fama 1981; Eita 2011; Aggarwal 1981; Joseph 2002; Vygodina 2006; Yau and Nieh, 2006; Kamin 1996; Klau 1998; Kamas 1995) this study includes money supply ( $M_2$ ) and nominal effective exchange rate (NEER) as monetarist variables and government expenditure (G) as structuralist variable of demand-pull inflation in the empirical model.

Therefore, the empirical model of interest of the study is:

$$P = f(G, NEER, M_2, RM) \quad (3)$$

The inflation ( $P$ ) function based on equation (3) is expressed in log-linear form for estimation, incorporating the disturbance term ( $u$ ) which according to standard time-series model is assumed to be white-noise process. Adding time subscripts ( $t$ ) the estimating equation becomes:

$$\ln P_t = a_0 + b_1 \ln G_t + b_2 \ln NEER_t + b_3 \ln M_2 + b_4 \ln RM_t + u_t \quad (4)$$

Equation (4) outlines the long-run relation between inflation and the variables determining inflation. The short-run dynamics has been incorporated by specifying equation (4) in an error-correction modelling format of Vector Autoregressive (VAR) model. The empirical analysis has been done following standard time-series econometric techniques.

#### *The Data*

Annual data of the variables of the model over the 1972 – 2010 period in Bangladesh are collected from various secondary sources. Data on Money Supply ( $M_2$ ) and Nominal Effective Exchange Rate (NEER) are taken from various issues of the Bangladesh Economic Review and the *International Financial Statistics 2011* CD-ROM of IMF. The data on Consumer Price Index (CPI), which is taken as the measure of Inflation in this study, is obtained from the *International Financial Statistics 2011* CD-ROM of the IMF. The data on Government Expenditure (G) and Remittance (RM) are collected from various quarterly and monthly reports of the Bangladesh Bank. For this

study, each of the series of data is taken in natural logarithmic form so that their first differences approach the growth rates.

## The Empirical Results

### *Causality between Inflation and Remittance Flow*

This study examines the relationships between inflation and remittance flows first, using Granger causality analysis for Bangladesh over the period 1972-2010. The Granger causality approach provides a plausible technique to consider both lagged and endogenous relationships. The F-statistics of the tests does not reject the hypothesis of ‘P does not Granger cause RM’, but reject the hypothesis of ‘RM does not Granger cause P’ at 5% level of significance. This indicates that there is unidirectional causality from remittances flows to the inflation rate in Bangladesh. Hence remittance (RM) is incorporated as a variable in the empirical model explaining inflation.

### *The Unit root Test*

Following standard practice, empirical analysis starts with the test of stationarity of variables of the model (4), using unit root test procedures. The Augmented Dickey-Fuller (ADF) test has been used to perform the unit root test in all the series of the model and examine their order of integration. The test has employed automatic lag length selection by *EViews 6* statistical software using a Schwarz Information Criterion (SIC). Schwarz Information Criterion (SIC) is considered to be more appropriate for studies with small numbers of observations like this study. Test statistics of the variables in the model at level and in first differences are presented in Table-1.

**Table no.1:** ADF Statistics for Testing for Unit Roots in Level

Variables	ADF Test Statistics at Level		ADF Test Statistics at 1 <sup>st</sup> Difference	
	t-ADF	P- value	t-ADF	P- value
$\ln P_t$	-1.299191	0.1756	-6.432779	0.0000
$\ln G_t$	2.718335	0.9978	-5.354029	0.0000
$\ln NEER_t$	1.442170	0.9604	-3.629083	0.0006
$\ln M2_t$	-0.271876	0.9187	-4.818145	0.0004
$\ln RM_t$	3.710934	0.9998	-6.514915	0.0000

The estimated statistic for all the variables at level does not exceed ADF test statistics. It shows that the null hypothesis of unit root cannot be rejected at 5% level of significance for all the variables at level. To test for the presence of more than one unit root in all these variables, the unit root test of the variables at first difference has been checked. The results show that the unit root hypothesis is rejected at the first differences for all the variables. This result from unit-root tests provides strong evidence of non-stationarity at level and stationarity at first difference and that all five series are integration to degree one,  $I(1)$ .

### ***Inflation in Bangladesh in the long-run***

As all the variables in the model are found non-stationary and integrated with the same order  $I(1)$ , the co-integration analysis is performed to infer the long-run relationship among variables in the model. The cointegration between variables reveals the existence of the long-run stable (equilibrium) relationship. Results of the Johansen Maximum Likelihood procedure of cointegration test applied to a vector autoregressive (VAR) version is presented in Table no. 2. Table 2 reports the Trace statistics and Maximum Eigen statistics of the unrestricted cointegration rank test among variables under study to identify number of cointegrating vectors, assuming a linear deterministic trend and an optimum lag length of 1 as determined by all lag selection criteria (LR, FPE, AIC, SC and HQ). Both, the Trace statistics and Maximum Eigen statistics reject the null hypothesis of no cointegrating relationship between variables of the model of equation (4). Both statistics indicate two cointegrating equation among the variables. This result confirms the existence of the long-run equilibrium relationship between the variables of the model. It also gives an indication that there exists Granger causality in at least two directions.

**Table no. 2: Johansen Cointegration Tests Results**

Hypothesized No. of CE(s)	Trace Statistics	Critical Value	p-value	Max-Eigen Statistics	Critical Value	p-value
None*	87.80709	69.81889	0.0010	36.49244	33.87687	0.0238
At most 1*	51.31465	47.85613	0.0228	4.288488	3.841466	0.0384
At most 2	24.97266	29.79707	0.1624	26.34198	27.58434	0.0714

\* denotes rejection of the hypothesis at the 0.05 level.

The parameter estimates representing the cointegration between the inflation and its determinants is specified as:

$$\ln(P_t) - 4.99\ln(G_t) + 5.78\ln(NEER_t) - 0.75 \ln(M_{2t}) - 2.48\ln(RM_t) + 35.87 = 0$$

$$\text{or, } \ln(P_t) = 4.99\ln(G_t) - 5.78\ln(NEER_t) + 0.75 \ln(M_{2t}) + 2.48\ln(RM_t) - 35.87 \dots\dots\dots (5)$$

(-1.93)
(0.33)
(-5.29)
(-3.04)

Equation (5) represents the long-run relationship between inflation rate ( $P$ ) and the determinants of inflation in Bangladesh. It is found from the values of the numbers in parentheses representing  $t$ -statistics of the respective coefficients that except  $\ln NEER$  all other variables have significant impact on the rate of inflation in Bangladesh in long-run. The positive value of the coefficient (at 10% level of significance) of  $\ln G$  indicates that the elasticity of inflation with respect to the government expenditure is positive, that is, the inflation rate weakly responds to the increase in government expenditure in the long-run. It confirms the structuralist view regarding the cause of inflation.

The low value of  $t$ -statistics of  $\ln NEER$  indicates that nominal effective exchange rate does not have significant effect on the rate of inflation in the long-run. But the money supply ( $M2$ ) has significant positive impact on inflation in Bangladesh in the long-run, which is consistent with the monetarist view.

The impact of the variable of interest of this study, the  $\ln RM$  on inflation is found positive and significant at 5% level in the long-run. That is, the remittances inflows result in an increase in inflation rate in Bangladesh and the elasticity of inflation with respect to remittance inflow is found more than proportional (2.48).

### ***The Error Correction Model (ECM)***

With the existence of cointegration established, equation (4) is re-parameterised as an error correction model (ECM) to estimate a model for improved forecasting. The error correction model alone also can make direct inference both about the long-run and short-run relationship. Since there existence of cointegrating equation, the Vector Autoregressive (VAR) needs to include an error correction term involving levels of the series, and this term appears on the right-hand side of each of the VAR equations, which otherwise will be in first differences.

The estimated equation of the model in error correction form including the  $\ln RM$  to capture the effects of remittance on inflation of Bangladesh is:

$$\begin{aligned} \Delta \ln(P_t) = & -0.27 - 0.07 \Delta \ln(P_{t-1}) - 3.34 \Delta \ln(G_{t-1}) - 1.45 \Delta \ln(NEER_{t-1}) + 3.40 \Delta \ln(M_{2t-1}) + 0.74 \Delta \ln(RM_{t-1}) \\ & (-0.38) \quad (-1.78) \quad (-0.50) \quad (1.43) \quad (1.42) \\ & -0.26 [\ln(P_t) - 4.99 \ln(G_t) + 5.78 \ln(NEER_t) - 0.75 \ln(M_{2t}) - 2.48 \ln(RM_t) + 35.78] \quad \dots (6) \\ & (-1.73) \quad (-1.93) \quad (0.33) \quad (-5.29) \quad (-3.04) \end{aligned}$$

The values in parentheses represent the  $t$ -statistics for the respective coefficients. The coefficients of the short-run differenced estimation variables indicate that only the coefficient of government expenditure with 1-period time lag is significant at 10% level. The negative sign of the coefficient of  $\ln G$  indicates that the increase in government expenditure reduces the inflation in the short-run, though it increases the inflation in the long-run as seen from equation (5).

No significant effects of the variables NEER, M2 and RM of the model have been found on inflation in the short-run. That is the money supply (M2) and remittances inflows (RM), which do not have any impact on the inflation rate in Bangladesh, in the short-run. But no significant impact of nominal effective exchange rate is found both in short-run and long-run on inflation rate, in Bangladesh.

An increase in remittances growth leads to a statistically significant positive increase in inflation rate in the long-run, whereas no response of inflation to remittances is found in the short-run in Bangladesh. These results match with Narayan, Narayan and Mishra (2011) that remittances generate inflation in developing countries including Bangladesh, and the effect of remittances on inflation is found more pronounced in the long run.

The negative and statistically significant (at 10% level) of the error correction term (-0.26) means that the speed at which the rate of variation of the inflation rate  $\Delta \ln(P_t)$ , the dependent variable in the first equation of the vector error correction (VEMC) system (6), adjusts towards the long-run cointegrating relationship differs from zero. The short-run disequilibrium of inflation rate is corrected at the rate of 26% per annum.

### Conclusion

Over the last decade, workers' remittances played a crucial role in the economic development of Bangladesh and are expected to remain so over the coming years. Remittance plays a significant role in poverty

reduction and economic development of the country, but there is no empirical evidence whether remittance causes inflation in Bangladesh or not. In this paper, a moderate initiative is taken to explore the issue using a time series data set of Bangladesh over the period 1972 to 2010. The empirical result suggests that, there exists unidirectional causal relationship from remittances inflows to the inflation. The relationship is significant in the long run, but no relationship is found between them in the short-run. Results also indicate that any shock in the short-run inflation gradually adjusted to the long-run equilibrium.

Results of Balderas and Nath (2008) study on Mexico differ from the results of this study. Using monthly data over the 1995- 2005 period in Mexico, they found that remittances have significant positive effects on inflation in the short-run, which gradually tapers off in the long-run. The cause of such difference might be due to not considering the exchange rate regimes change, as different exchange rate regimes have considerably different effects on the macroeconomic variables (Reinhart and Rogoff, 2004). Future research proposes to account exchange rate regimes changes in investigating the effects of remittances on inflation.

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