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TAX HARMONIZATION VERSUS FISCAL COMPETITION

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Abstract:
Recent years have brought into discussion once again subjects like tax harmonization and fiscal competition. Every time the European Union tends to take a step forward critics enter the scene and give contrary arguments to European integration. Through this article we have offered our readers a compelling view over the "battle" between tax harmonization and fiscal competition. While tax harmonization has key advantages as less costs regarding public revenues, leads to higher degree of integration and allows the usage of fiscal transfers between regions, fiscal competition is no less and presents key advantages as high reductions in tax rates and opens a large path for new investments, especially FDI. Choosing tax harmonization or fiscal competition depends on a multitude of variables, of circumstances, the decision of choosing one path or the other being ultimately influenced by the view of central and local authorities. Our analysis indicates that if we refer to a group of countries that are a part of a monetary union or that form a federation, tax harmonization seems to be the best path to choose. Moving the analysis to a group of regions that aren't taking any kind of correlated actions or that have not signed any major treaties regarding monetary or fiscal policies, the optimal solution is fiscal competition.

Key words: fiscal competition, tax harmonization, fiscal integration, advantages, disadvantages.

JEL classification: E62; H71; H77

1. INTRODUCTION

The Tax harmonization and fiscal competition are two key subjects discussed in the literature on fiscal integration, but despite this fact, not all authors stopped to reveal what are the main advantages and disadvantages of each one, or put them one versus the other. In this regard, through this paper we want to revel the main characteristics of each one, joining them one near the other and crossing the main lines that separate them, revealing that in a large point of view, these two concepts lead roughly to the same result. Also, we want to give our readers a good view on what is tax harmonization and what is fiscal competition.

But before undertaking the task ahead, we need to mention that tax harmonization is an important part of the fiscal integration process. Fiscal integration is the process by which a group of countries agree on taking measures that lead to a higher level of fiscal convergence, the ultimate goal being the formation of a fiscal union. Starting from the definition given to the fiscal integration process, we can easily say that tax harmonization is the process by which a heterogeneous group of countries, federal states or even local governments agree on setting a minimum and maximum level of their tax rates, including also a higher degree of harmonization of tax legislation, in order to attract foreign investors and to encourage local development and investments. On the other hand, fiscal competition through taxes represents the particular situation in which a country reduces its fiscal burden imposed on taxpayers in order to enhance national economic competitiveness and to attract foreign direct investments (Zugravu, 2003).

When we thing about fiscal competition, we actually thing at what some authors describe as tax competition. Through tax competition we understand the particular situation in which a group of countries, federal states or local governments compete on lowering their tax rates to attract more investors, especially foreign investors (FDI). So, fiscal competition isn't about which government is collecting more tax revenues or which government has the best budget balance, although the words "fiscal" and "competition" take our thoughts to this situation at a first glance.

We want to attract attention on the fact that competing governments have a choice to make: either to form a fiscal union, in this regard taking actions that lead to a harmonization of their tax rates, or to compete one each other in reducing their tax rates, in what is known in the literature as "race to the bottom", defining a continuous battle on lowering their tax rates, in particular those on direct taxes (income and corporate taxes). This decision needs to be based on the main advantages and disadvantages of each choice. In the first situation, agreeing to form a fiscal union and therefore lower their tax rates on the principles of tax harmonization, is the easiest way and the least expensive one, in matter of the possible impact on the budgetary balance. On the other hand, "racing to the bottom" can lead to negative effects on the budgetary balance, especially in those situations in which the forecasts on new local and foreign investments are too optimistic or not fulfilled, and therefore the reduced tax incomes collected aren't compensated by new investments. Choosing the tax harmonization path includes a much carefully planned series of actions, including preliminary studies on the impact of future decisions and coordinated actions. But this path depends on the governments capacity and commitment to collaborate on planning their actions in this regard, being after all a decision based on will. We do not specifically support one path or the other, this being a reflection subject for all governments before taking actions.

Although the tax harmonization and tax competition tend to lead to the same result, meaning reduced tax rates, things aren't quite like this. In this article we will reveal why the results can be a bit different, given the fact that different paths lead to different steps that need to be taken, so to different results, mainly because the of the secondary effects produced by each path in particular. Also, these side effects can be easily reveled by putting the advantages and disadvantages of each path one near the other.

Many authors who publish articles in this research field, as we will see in the literature review, tend to study the impact of tax harmonization and fiscal competition on different variables, but few stop and continue their conclusions by revealing which are the advantages and disadvantages of tax harmonization or tax competition, without also mentioning what was the starting point that lead to fiscal competition or tax harmonization.

Through this article we want to reveal some of the facts that the literature specific to this topic hasn't revealed or hasn't properly highlighted. Also, we want to offer our readers a complete perspective on the subject, the main contribution being that of the author. Also we mention that the paper is structured as follows. Section 2 marks the literature review, in which we present some of the papers that argue the same topic as ours. Section 3 marks the methodology, continuing with Section 4 that represents our analysis. In the last section are described our key findings and conclusions.

2. LITERATURE REVIEW

We cannot continue our analysis without a proper review of the main research papers published in this research field. Through this, we want to highlight a part of the analyses made by other researchers in the field, and also setting a starting point for our own analysis.

Fiscal competition and tax harmonization are two important current issues, especially in an enlarged European Union. In this regard, Florin Oprea (2010) suggests that there can be a fiscal competition which may lead to distortions in allocating resources, the single rate implemented by some European countries generating differences that can have negative effects. This situation can continue in a negative way with problems regarding for example important public investments like those in infrastructure that may be ignored or reduced by authorities.

According to David E. Wildasin (2010), the now-large literature on fiscal competition has stressed that national and subnational (local) governments don't exist in isolation from the rest of the world, finding themselves competing for mobile labor and capital. His basic modeling structure has been exploited with other occasion in different forms and reinterpreted in many ways (Wilson, 1999; Wilson and Wildasin, 2004). By using a dynamic model, his analysis has revealed how the local fiscal policy affects the dynamic equilibrium allocation of both mobile factors of production, using just one of the two. According to him, the system adjusts gradually to a long-run equilibrium.

Another important related fact is being represented by firms' financial choices under corporate tax competition. In this regard, the decision of the companies to choose tax-efficient regions has been studied by Haufler and Runkel (2012). According to their study, each country chooses inefficient low tax rates and lax thin capitalization rules in order to attract more national and international firms. An extremely interesting conclusion of their research is that smaller countries tend to choose the lowest tax rate and the more lenient thin capitalization rule, probably because of a weaker economy, but mostly because having a smaller dimension means in general having smaller stocks of natural resources. A more interesting model was proposed by Hayato Kato (2015), the author using in his analysis a dynamic model in which two countries compete which each other to attract more firms, but not like the other models that use static models, the proposed model analyzes tax competition over an infinite time horizon in an economy with trade costs and internationally mobile industrial firms, according to the author the key factor being the credibility of the governments tax policies.

Expanding the research basis, some authors examined a trade model in which three countries compete for an exogenous number of companies. In this regard, they established the distribution of industrial activity in the absence of taxes and compared it to the equilibrium state when those countries compete in attracting companies. Using one of the three countries as a hub for international trade, in a situation in which all countries are equally sized, the hub country seems to be advantaged by the fact that by collecting some resources from trade taxes it can maintain lower tax rates while having enough fiscal incomes to fulfill all public expenses (Darby et al., 2014).

Some authors turned their attention to a federation with two heterogeneous regions that try to attract capital by competing through income taxes and public investments, the basic framework being the fiscal equalization schemes (Boadway and Flatters, 1982). Examining the issue of equalization grants among heterogeneous regions that compete through taxes and public investments under a perfect mobility of capital, indicates that equalization is desirable in a variety of settings, both for each region individually and also for a federation model (Hindriks et al., 2008).

We must emphasize the fact that foreign investors are not only attracted by lower corporate taxes but also by other important factors, as stated by some authors. Competition between regions over potential investors becomes an indirect one when there are in stake different infrastructure services (Justman et al., 2005), a recent example being the Dacia situation from Romania, in which the Renault Group threatened to move their production capacities in another country if the new highway will not be built, present costs of transportation being very high.

The consequences of economic integration, within international capital or labor mobility, were studied by Kessler, Lufesmann and Myers (2002). According to the mentioned authors, a step that leads to full integration may alleviate rather than intensify fiscal competition, especially in the context of similar political and economical conditions. Tax competition for mobile capital in these circumstances is softened as the labor market becomes more integrated, and according to the authors, may vanish if the two factors are fully mobile.

From another point of view, Massimiliano Trovato (2007) suggests that tax competition is more like a state rather than a process that has been designed from the top down, instead of being a freely evolving process within the "market". According to him, in the absence of tax competition, governments tend to set the amount of taxes to be raised and spent to the point where marginal cost equals the profit's marginal rate. Tax competition leads to a reduction of tax rates, and therefore to an underprovision of public goods, opinion that we believe to be correct.

In contrast with fiscal competition, tax harmonization is a more difficult process, especially when we consider a heterogeneous group of countries like those in the European Union. Some authors tend to view fiscal harmonization like a threat, completing with the fact that some European countries feel uncomfortable with the idea of European integration itself.

3. METHODOLOGY

The methodology consists mainly engaging in a qualitative research that includes a comparative analysis on the key advantages and disadvantages of tax harmonization and tax competition. Through highlighting the main features of each path we want to offer our readers a compelling view on the matters at hand, and also open a path to further studies and reflections. By putting the two concepts and their key features one near the other we want to offer a pertinent opinion on which of the two path is the most easiest to take and cost efficient.

The data will be presented in tables to offer a more complete view of our analysis, and also for a more easy identification of the advantages and disadvantages of fiscal competition and tax harmonization, so that our readers decide for themselves which is the best path to proceed in the near future. The methodology also includes references to empirical data, to real facts, that influence the fiscal integration process

4. ANALYSIS

Before we begin our analysis, we want to specify the fact that in large, both fiscal competition and tax harmonization tend to lead to the same result, but not necessarily in all situations.

Tax competition, pushing aside other variables or facts, designates a "battle" between two or more regions in attracting foreign investors, using taxation as a mean to reach this goal. In this competition, all regions reduce their tax rates in order to ensure that their country is the most attractive from the point of view of tax costs. But this battle has it's own price, the reduction of tax rates bringing with it a reduction in tax revenues. Having less money to spend means that central or local governments will have to reduce their public expenditures, therefore renouncing to some important public investments, the best example in this regard being those in infrastructure. A weaker infrastructure leads to a lower degree of competitiveness at a regional and international level. Also, a smaller amount of public expenditures may lead to reduction in the turnover of local companies who have contracts with the local or general authorities, thus determining a reduction in corporate taxes that are paid due to lower profits.

So, as we have seen so far, this competition in attracting foreign investments may lead actually to a lower economic activity in the region, and maybe to budget deficits. Looking things like this means that we are talking about a compromise that implies attracting foreign investors with a cost determined by a reduction in local economic activity for the short-run. Well, in reality things aren't like exactly like this, giving the fact that from the reduction of the tax rates local firms will also benefit. Lower tax rates leaves more money for local companies to invest, and therefore expand. With new investments come more money, larger profits, and also larger corporate tax revenues for the governments to spend. Losing revenues on one hand and gaining them on the other hand means a balanced budget, thus no budget deficits and no further increases in public debt. Unfortunately, there may be some short timed problems, given the period of time that firms need to invest and to obtain a larger turnover and higher profits. During this period, the soundness of the public finances may suffer, but the effect is temporary. There can be also situation in which the public budgets do not balance, especially in those regions in which tax evasion blooms. A reduction in tax rates that doesn't lead to balanced budget has negative effects on the long run, completing with the fact that governments will need more money to cover their expenses, thus having to take a step back and to increase their tax rates, drawing criticism from local firms and the general public.

Getting back to our main topic, we wanted to show our readers that the "race to the bottom", an effect of fiscal competition know in the literature that designs a high reduction in tax rates, may have unintended consequences with negative effects on local or general economy. Practically it all resumes to the social environment, the responsiveness of local firms and the quantum of new foreign and local investments. If the regions that engage in a tax competition are flooded with new investments, foreign and local, then those region will prosper economically. Unfortunately, low tax rates aren't the only motivation for foreign investors, infrastructure, tax deductions, bureaucracy and demand for goods and services having an important role as well. On the other hand, tax harmonization leads to a road that implies collaboration, prior thinking and research in advance, and most important will. Passing from fiscal competition to tax harmonization is only a problem of collaboration between different regions. A situation like this could eventually be met in a case where fiscal competition leads to extremely low tax rates, thus low tax revenues, affecting the balanced budget and leading to high deficits and liquidity problems. Through tax harmonization, the regions agree on setting up an optimal system, by which upper and lower limits of tax rates are established with a small difference between them, not only on direct taxes, but also on indirect and local taxes. In this case, the other variables that we mentioned intervene and make their case. Using this framework, the "battle" moves on the other factors that influence the decision of foreign investors, and here steps in the stage the central and local governments ability to provide with better public services, infrastructure, less bureaucracy and more fiscal facilities. Using the tax harmonization path automatically eliminates for the time being, fiscal competition. Using a path or another depends on the governments ability to communicate, to agree and to collaborate. Tax harmonization doesn't automatically leads to the formation of a fiscal union, the second part involving much larger scale project that includes fiscal transfers, a fully harmonized legislation and maybe some supervising institutions, beside a long-run agreement.

Till now, we've only talked about tax harmonization and fiscal competition only from the point of view of direct taxes, especially corporate and income taxes, but indirect taxes can also play an important role. Literature on tax harmonization and tax competition is mostly focused on direct taxes, few authors studying the role of indirect taxes in attracting foreign investors or give an advantage to local investors. Therefore, fiscal competition may as well take place on the ground of indirect taxes, fact rarely mentioned in the literature. In this new framework, regions compete in attracting foreign buyers, especially in those areas situated near borders. By reducing the tax rates of indirect taxes like VAT for example, regions attract buyers from outside and through this gain in indirect tax revenues. The new additional funds can be redirected to crucial public investments or can conduct to a reduction of other tax rates, for example those of direct taxes, moving the ground of the battle to a field that we already mentioned.

Fiscal competition through direct or indirect taxes isn't always a premeditated fact. There can be a situation in which a region starts reducing its tax rates, thus starting to attract more and more foreign investors, paving the path for entering in a fiscal competition with nearby regions. Excellent annual reports and newspaper articles do not go unnoticed by neighboring regions, which, remarking an important increase in its neighbor degree of national and international competiveness starts taking measures by which it also reduces its taxation rates. An extremely important point must be made. Fiscal competition doesn't exists without an awareness of the fact. When two or more regions engage in a fiscal competition, they all are aware of the process, and thus take actions in order to reduce their fiscal burden. Fiscal competition through indirect taxes tends to be more efficient on short term, but on the long run competing through direct taxes seems to be more advantageous. First of all, consumers tend to react faster to modifications in taxation than firms. Let's take the example of two small regions which are located side by side. We also state that the two regions are a part of a federal system, both using the same currency and subject to the same legislation. Also, we assume that both regions import goods from the same companies or regions, therefore acquisition costs are the same. A strong tax reduction in one area will be easily noted by costumers who live in the other region. As we said, given the fact that we talk about two related small regions, consumers will buy goods and services from the region with the lowest tax rates (indirect taxes). The advantaged region will have huge gains in matter of tax revenues, not only from indirect taxes as VAT, but also from corporate tax, given the fact that higher turnovers lead to higher profits, thus larger taxable matter. But fiscal competition isn't just about tax rates, an important piece of the puzzle being tax benefits. Giving investors advantages like deductibility, non-taxation of reinvested profit or tax deductions it amplifies the competition between regions, enlarging the area of the competition. In a framework in which capital is not mobile, fiscal competition has few space to unfold. But, even in such a framework, results ca be obtained as we discussed earlier through indirect taxes or if not, at least through labor mobility. A reduced mobility of capital doesn't necessary imply a lack of mobility on labor, thus lower tax rates specific to income taxes may attract skilled workers. Better prepared workers means a gain productivity, a gain in sales and profits for firms, and in tax revenues for local or central administrations.

In a federal state or in a fiscal union, fiscal competition has little ground to manifest itself because there are fiscal rules and at least one higher institution of surveillance. The tax harmonization path implies that regions agree with one each other to apply a common set of taxes and tax rates, with a small space for changes or adjustments. Also, the fiscal harmonization process implies that some countries reduce their tax rates and others increase them, including both direct and indirect taxes. Therefore, some regions will collect more tax revenues and others will collect less, with a major impact on public finances, especially public expenditures, underlining the previous statement that tax harmonization has problems of its own.

Sound public finances can be direct affected by tax harmonization, the process being often criticized by politicians, press and general public. This kind of argues can easily lead to a deepening of fiscal competition, mainly before the most important steps of tax harmonization being taken in order to ensure a higher level of FDI. After the tax harmonization is brought to an end, weaker economies or developing countries will still have a lot of disadvantages like those regarding capitalization of companies, development of the capital markets, infrastructure, political stability, public finances (public debt and deficit) and white collar, compared to developed countries, this being the case of the European Union. Weaker economies attract investors by using lower tax rates, so in general they are in a fiscal competition. But, with the tax harmonization process, there come sacrifices, developing countries renouncing to their fiscal advantages and rise they tax rates losing in this regard their key advantage in attracting investors and encouraging local companies, although they may profit from the new higher tax revenues and invest more, in an attempt to align with the developed countries in other strategic fields.

In times of crisis, governments that are engaged in a fiscal competition have a decision to make: either to continue the "race to the bottom" or to increase their tax rates, giving the fact that in times of crisis tax revenues are constantly reducing due to a decreasing in economic activity. We also need to mention that in times of crisis, attracting FDI cannot be the key reason to reduce tax rates, because in globalized world crises aren't reduced only to one region, therefore capital inflows are more likely not to encore giving the fact that each region will try to maintain the capital in its own yard. Also, fiscal consolidation will have to take a step forward and take its rightful place in the new context, authorities having two options: to increase their tax revenues or to reduce their public expenditures. In such a framework, fiscal consolidation strategies will intervene in order to take public finances to a healthy status (Oprea and Bilan, 2012).

Another important fact that we need to mention is the role of the democratic deficit. In an area like the European Union that is composed of a group of heterogeneous regions different opinions can be a huge problem. Giving the fact that European integration, including the fiscal integration process, has attracted a lot of critics, fiscal competition seems to be the easiest path, giving the fact that tax harmonization needs the agreement of the political decision makers and fiscal policy makers, which in most cases manifest a lack of interest and will. The democratic deficit can also be easily observed at the general public level, mentioning the attitude of the attitude of different countries like the United Kingdom, Denmark or even Switzerland. The degree of nationalism in these countries is very well placed, people refusing ideas like fiscal transfers, tax harmonization or fiscal integration. But, if the European Union really wants to become the United States of Europe, a tougher stance towards the carping regions is needed. Unfortunately, nationalism favors fiscal competition, fiscal decisions in this regard being widely appreciated by the general public.

The difficulty in implementing tax harmonization has been also noticed by other authors. For example, some state in this regard that each country faces a particular trade-off between fiscal revenues generated through taxation and the productive efficiency loss induced by their fiscal codes

(Fernandez-de-Cordoba and Torres, 2007). Others see in fiscal harmonization a threat, a realistic approach saying that in general, there are situations in which people feel uncomfortable only thinking about the idea of fiscal harmonization, not seeing the formation of a new kind of superstate as a great idea, so a new question rises: why should politicians support an idea that people are skeptical about? (Trovato, 2007). Also, the tax harmonization step may need some home measures, referring to the removal of fiscal barriers, a large area of instruments coming here at hand, from “negative integration” and “positive integration” to the two mechanisms of uniformity and compatibility (Velayos et al., 2008). But, even with these difficulties, economists have long recognized that ultimately the monetary union will have to embedded in a fiscal union (De Grauwe, 2013), existing papers providing the necessary proof (Dornean, 2009). Given the facts that we discussed so far, the next step is to set all the main facts in a table, for an easy view of the main advantages and disadvantages of tax harmonization and fiscal competition for our readers. So, in this regard, we will present first the main advantages of each.

Table no. 1. A comparative analysis of the key advantages of tax harmonization fiscal competition

Tax Harmonization Advantages	Fiscal Competition Advantages
Does not lead to the “race to the bottom”	A high reduction in tax rates attracts more FDI and gives an impulse to the local economic activity
Less costs regarding public revenues, due to the fact that tax rates are common set and do not disadvantage or advantage just one region	Doesn’t involve the collaboration of authorities, each taking the decisions that it thinks that are the best for the local economy
Can lead to a higher degree of integration, especially to a political union in the European Union	Doesn’t need the establishment of a new coordination institution
The harmonization of legislation will bring with it less costs for multinational companies	Harmonization of legislation, especially of tax codes, will not be needed
Opens the path for new collaborations between regions	Reduced chances of a democratic deficit appearing
Leads to the formation of a fiscal union, with all its advantages	Does not lead to tax evasion
Allows the use of fiscal transfers between regions, reducing borrowing costs on capital markets or from private or international lenders	Doesn’t automatically imply an increase of public spending on major projects, like those in infrastructure
For some countries, the increase of tax rates conducts to higher tax revenues, and therefore to more public investments	Reducing indirect tax rates attracts buyers form neighbor regions
Fiscal transfers help countries in reducing their exposure to crises and budget deficits	Opens a large path to new investments, with direct implications on the local economy growth with high benefits on a long run
Regions can compete through fiscal advantages that are offered to firms	Regions can compete thorough fiscal advantages that are offered to firms
Can lead to the implementation of international standards of fiscal governance or fiscal governance codes	More space for stabilization, giving the fact that countries members of the Eurozone cannot use the rate of exchange for stabilization
Determines the strengthening of fiscal discipline	Nationalism is a benefit not an obstacle
Companies will use the common consolidated tax base	Conducts to a reduction of the fiscal burden for firms and population
No fiscal barriers	Reflects the preferences of citizens and companies
Eliminates the possibilities of disloyal fiscal competition appearing	Presents more flexibility regarding the variety of taxes and tax rates

Source: Authors image

As presented above, both tax harmonization and fiscal competition offer a series of important key advantages. Regarding tax harmonization, its main advantages are that it doesn’t lead to “race to the bottom”, leads to a higher degree of integration, strengthens fiscal discipline and allows the usage of fiscal transfers. On the other hand, fiscal competition allows more flexibility for fiscal policies, is more advantageous in attracting FDI, does not lead to tax evasion and it doesn’t attract critics from citizens and firms.

Also, tax harmonization presents other less obvious advantages like the elimination of tax barriers and disloyal fiscal competition, for some countries leads to higher tax revenues and reduces multinational companies costs through harmonized tax rates and legislation. Fiscal competition on the other hand, has the advantage of a smaller fiscal burden, presents a smaller risk of a democratic deficit to appear giving the fact that citizens opinions matter and the harmonization of legislation isn't necessary.

In the previous table we have presented the main benefits of tax harmonization and tax competition but, in order to offer a clear and complete view over our analysis, we will present which are the key disadvantages of each.

Table no. 2. A comparative analysis of the key disadvantages of tax harmonization and fiscal competition

Tax Harmonization Disadvantages	Fiscal Competition Disadvantages
Needs fully coordinated actions	High tax reductions, like those that appear in the "race to the bottom" may lead to a budget deficits
Implies cooperation between different regions, fact that isn't always possible giving the fact that politicians and the general public are sceptic about fiscal integration	The incoming FDI may not meet the forecasts, giving the fact that FDI depend also on other variables beside tax rates (fiscal advantages, infrastructure, labor productivity)
In the case of the EU, involves working with the authorities of 28 countries, fact that tends to present a lot of difficulties	Giving the low collaboration between countries, fiscal transfers will not be available
A coordination and surveillance institution is necessary, thus presenting additional costs	Lower tax rates determine lower tax revenues, affecting the soundness of public finances on a short term.
Needs to solve the problem of the democratic deficit, especially in the case of the EU	Has little space to manifest itself in a federal union
Giving the fact in some regions tax rates will increase, tax evasion may spread	In conditions such as pour capital and labor mobility has reduced effects on attracting FDI
Regions will be obliged to invest more especially in infrastructure, in order to make a difference and to attract FDI, fact that leads to higher public expenditures	May lead to a lack of competitiveness of a region due to low public investments, especially in the case of too optimistic forecasts on FDI and new local investments
Doesn't resume to the harmonization of direct taxes, involving also the harmonization of indirect taxes	Smaller regions are disadvantaged compared to larger regions
Nationalism can become a big obstacle	Weaker fiscal discipline, depending on the authorities capabilities to maintain sound public finances
The advantage of low fiscal burden in developing regions will not be available	Fiscal barriers may be imposed
Less flexibility in establishing the variety of taxes and tax rates	Fiscal competition can become disloyal

Source: Authors image

Table 2 gives us a view over the main disadvantages of both fiscal competition and tax harmonization in a comparative view over their key aspects. The main disadvantages of tax harmonization are the need for cooperation, the fact that implies democratic deficit, increased tax rates in some countries and less flexibility in managing fiscal difficulties. Fiscal competition on the other hand, presents disadvantages like the "race to the bottom", depends on the meeting of the forecasts on FDI and new local investments, a reduction in tax revenues especially on short terms and disloyal fiscal competition.

Other disadvantages of tax harmonization are the fact that reduced tax burden will achieved so far by developing regions will not be available (giving the fact that these countries will have to increase their tax rates), nationalism and the need for more investments, because tax rates aren't a competitiveness factor. As disadvantages, fiscal competition implies weaker fiscal discipline, is conditioned by labor and capital mobility and can affect the soundness of public finances.

Choosing one path or another implies preliminary thinking and judgement. In the context of the European Union the choice is simple, the only path being tax harmonization giving the fact that Europeans fight for a deeper integration, fiscal and political. In other parts of the world, especially in developing regions, tax competition may be viewed as the best path in order to attract FDI and to give and advantage to local companies. So, the decision to take the one road or another depends on a lot of variables and conditions, like if there are previous agreements, the location of the regions, their level of development and the general public vision.

5. CONCLUSIONS

Although the tax harmonization and tax competition tend to lead to the same result, meaning reduced tax rates, things aren't quite like this. In this article we will reveal why the results can be a bit different, given the fact that different paths lead to different steps that need to be taken, so to different results, mainly because the of the secondary effects produced by each path in particular. Also, these side effects can be easily reveled by putting the advantages and disadvantages of each path one near the other.

In our point of view, tax harmonization represents the process by which two or more regions agree on setting up a minimum and maximum level of their tax rates, including legislative harmonization. When we thing about tax competition, we think at that particular situation in which two or more regions compete in lowering their tax rates in order to attract more foreign investors, but with benefits to the local companies as well, giving the fact that "the race to the bottom" has positive effects on local firms activity.

Taking one path or another is a matter of choice and will. In the particular situation of the European Union, the only path is tax harmonization, bringing into discussion the current indirect taxes harmonization and the steps taken to achieve direct taxes harmonization. In other situations or regions, especially in the case of developing ones, fiscal competition tends to be the most advantageous option.

Our goal was to present our analysis in form of tables that contain both the advantages and disadvantages of each path, putting side by side the key features of each of the two processes. Using this method, we wanted to offer our readers an easy solution to identify the good and the bad parts of each, for an easier understanding.

First of all, we wanted to attract attention on the fact that foreign investments do not only depend on tax rates or the level of tax burden, other factors being also important, of which we can mention: infrastructure, political stability, mentality, labour productivity and tax benefits. Also, we need to mention and attract attention on the fact that fiscal competition is an acknowledged fact by governments, and not something which just happens giving some circumstances.

As we said through our analysis, the main advantages of tax harmonization are the harmonization of legislation (a big advantage for multinational companies especially), the fact that it leads to a higher degree of integration, allows the usage of fiscal transfers and determines a strengthening of fiscal discipline. Also, another big advantage is the fact that through careful thinking and planning, it may lead to the implementation of international fiscal and budgetary standards or fiscal governance codes. On the other hand, fiscal competition presents advantages like lower tax burden and tax rates (in order to attract FDI and to give a boost to local economic activities), doesn't imply democratic deficit (nationalism isn't a disadvantage like in the case of tax harmonization) and regions can use fiscal policies in order to maintain sound public finances, giving the fact that there aren't present fiscal rules or restrictions.

Using the presented advantages as a method to say that one path is better than the other is one way to view things. Each of the two situation must be analyzed from its starting point. For example, saying that fiscal competition is better than tax harmonization in the Eurozone means taking a step backward, without seeing the whole picture and understanding that tax harmonization means to take another step forward toward a fiscal and political union. In the case of a heterogeneous group of regions that aren't bounded by any type of union or agreement, fiscal competition seems to have the upper hand, even with all its disadvantages.

Regarding disadvantages, those of tax harmonization are: cooperation between different regions, fact that isn't always possible, the need to establish a coordination and surveillance institution, less flexibility in establishing taxes and tax rates and the fact that it leads to an increase of the fiscal burden in some regions (those who have to reach the lower limit of the imposed tax rate). Fiscal competition on the other hand it is dependent on FDI and new local investments in order to achieve its purpose, it involves renouncing to fiscal transfers, its results depend on the mobility of labor and capital and presents a weaker fiscal discipline.

We do not say that in the future, the presented facts may not suffer modifications, giving the fact that new situations that may come can lead to new advantages or disadvantages to be discovered, which is why we hope that our readers will pursue this topic and add new improvements to the subject.

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