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EVOLUTION OF PUBLIC FINANCE IN SELECTED COUNTRIES

Abstract

This contribution deals with the evolution of public finance in two selected European countries. France and Germany were selected as countries to compare their evolution of public finance. The reason why the two countries were chosen is their general proximity to each other in many respects. From a professional point of view, i.e. from the point of view of the discipline of public finance, however, these are countries with different concepts of public finance disciplines. The contribution presents the historical background, context and consequences of this evolution. The relevant public finance evolution is divided into several historical stages in each country. The contribution focuses on each stage separately and points out solutions and effect of each stage. The main aim of the contribution is to confirm or disprove the hypothesis that the evolution of the public finance discipline was different in each of the selected countries. The scientific methods used in the article are analysis and synthesis, description and comparative methods.

Key words: evolution, France, public finance.

JEL Classification: K34

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1. Introduction

Nowadays, it is possible (and necessary too) to distinguish among more conceptions of public finance in the world. In general, there are primarily the Anglo-Saxon, German and French conceptions of public finance. It cannot be ruled out more conceptions or rather philosophies of public finance, but in the first place, it is about their social and scientific acceptance among the professional public. Unfortunately, these days terms as "financial law" or "public finance" are used *promiscue*, just as terms like "money" or "finance". In fact, it does not matter which conception of public finance (or rather financial law) we are interested in, because these conceptions have these mentioned terms in common [Bartes 2019, 38].

To understand current conceptions of public finance in different states, it is necessary to deal with the historical background of the evolution of this important discipline in various states. This research necessarily involves taking into account interaction, global context, reciprocal inspiration and consequences, which were happened during a long-standing evolution.

The uniqueness of each concept of public finance depends on the historical and political evolution of the country or region, in connection with culture, economy and social situation. All these aspects are ultimately linked by the discipline of public finance. For this reason, Paul-Marie Gaudemet noticed that the discipline of public finance is the discipline of crossroads [Gaudemet, Molinier 1996, 22].

The aim of the paper is to confirm or disprove the hypothesis that the evolution of public finance has varied from country to country and has had a significantly different impacts and results.

The partial aim of the paper is to analyse the evolution of public finance in selected countries (i.e. France and Germany) and to compare their differences or to point out the same features. The research methods used in the paper are analysis and synthesis, description and comparative methods. Foreign literature (especially the French one) is the primary source of the paper.

2. Evolution of public finance in France

In examining the historical development, or rather an evolution of public finances, in order to achieve its objective knowledge, in the case of France, it cannot be satisfied with a period of, for example, one hundred years. This fact is necessarily linked to the history of

France, as well as to the evolution of its political establishment, including the conditions which led to the creation of the basic concept of French public finance law.

Many economists and lawyers in France questioned whether public finance preceded the state or the state preceded public finance. For example, Maurice Hauriou considered public finance to be the most important element of public affairs in the state, although according to one of the "classical" French definitions (i.e. the definition used between 1814 and 1914) public finances were not among the basic elements of the state [Carré 1904: 89]. However, Hauriou conceived his doctrine in such a way that the phrase "state without finances" (i.e. without public revenues and expenditures) was completely unthinkable primarily from the point of view of practice, not only from the point of view of theory.

During examining the development of the French public finance discipline, or rather during the analysis of budgetary and financial history, most classical authors distinguished three periods. For example, René Stourm distinguished “the period of the States General, the period of the Parliament and the current period” [Stourm 1909: 216]. However, this examination should not be limited to history, as history is only one of the elements that form the basis of public finance discipline in France. For multidisciplinary approach, it is therefore possible to use sources not only of financial science, but also sources related to law and political economy.

The basic features of the history of French public finance law, for example according to Michel Bouvier, fluctuate between its immutability and modernization [Bouvier 2008: 103].

2.1. Pre-Classical Public Finance Law (1314 – 1814)

This initial stage in the evolution of French public finance discipline was characterized by the gradual evolution of state power from the monarchy period to the republic period. From the financial point of view in France, the division of the power meant, above all, the division of budgetary and fiscal powers between the competent authorities. Budgetary powers were often concentrated in the hands of a single entity (i.e., the case of the absolutist monarchy, the Consulate, the Empire) or a single assembly (i.e., the Convention or the Directory).

The period was also characterized by the fact that more and more people invoked the principle of consent to taxation, which was still overlooked by the then ruling elite. This principle was thus associated with many struggles to curtail monarchical or imperial arbitrariness, to establish a National Assembly, to reduce budgetary opacity and, last but

not least, to strive for a more democratic regime. The principle of consent to taxation was the subject of most political and legal discussions of this time.

During the Restoration and subsequently during the July Monarchy, the foundations of current public finance discipline emerged. At the same time, it can be observed that state expenditures have been growing since then. During this long period, which did not escape economic and political crises, in spite of many rigidities stemming from the budgetary and financial tradition, a "French-style" budget model emerged in 1814 that was different from the Anglo-Saxon model, although the French one was in its initially inspired by it.

2.2. 2.2 Classical Public Finance Law (1814 – 1914)

The period in question begins with the fall of the First Empire and represents definitively the end of the financial system of the Old Regime and the budgetary turmoil of the Revolution and the Empire. In the period of the Restoration and the July Monarchy, the foundations of public finance law are being built, which is based on budgetary clarity and equilibrium.

The rise of modern budget law in the Restoration period may seem relatively paradoxical, because according to the letter of the 1814 Constitution, the government was established not democratically and parliamentarily, but the so-called "divine law", which intended to restore monarchy sovereignty in its entirely. Even the political and social revolutions (especially in 1830 and 1848) did not affect the newly formed budget conception. The politics and moderate temperament of Louis XVIII, the English influence and brevity of the 1814 and 1830 constitutions of the financial and budgetary aspects contributed to the spread of parliamentarism, which laid the foundations for modern budgetary law.

Louis XVIII had a unique ability to surround himself with the right people. In this situation, it was mainly the Ministers of Finance, Baron Louis and Count de Villèle, and the Director of the *comptabilité générale des finances* Marquis d'Audiffret. Baron Louis and Count de Villèle are the authors of traditional budgetary principles, including:

- The annual budget rule (reaffirmed in 1822, budget or rather fiscal year corresponds to calendar year);
- The principle of unity of the budget (so-called extraordinary budgets are ended, i.e. budgets dedicated to always different areas);
- The principle of universality of the budget (in 1818);

- And the principle of specialty (presumes voting on expenditures not in general, but according to individual ministries; it has been applied since 1817, according to chapters since 1831 [Chotard 1890: 8].

These principles remain the basis of (not only) the French budgetary law until this day, despite its major reform of 2001.

As Beaulieu-Leroy notes, the liberal economic doctrine that was dominant and therefore influencing during this period consisted in ending state intervention in the economic sphere, which ultimately affected both budget neutrality and adherence to budgetary principles [Beaulieu-Leroy 1883: 352].

The typical idea for the classical period is that the state must limit its activities and interventions to a minimum. The state, on the one hand, will ensure the internal and external security of the country through the police force and the army, on the other hand, the state will ensure important economic infrastructure by building roads, railways, ports, etc. The state must simultaneously play an active role in economic life, which must be left entirely to individuals. In order for the state to fulfill its tasks, the state must have the necessary resources at its disposal, which the state draws primarily from taxes. Taxes are understood as a necessary evil, and therefore can only serve to cover the administrative expenses of the state. For this reason, the public finance discipline in this period is defined as “the science of state revenue and expenditure management” [Beaulieu-Leroy 1883: 354].

The application of the principles of Baron Louis and Count de Villèle meant that from 1870 to 1913, for example, the ratio between public expenditure (especially state expenditure) and national income was around 10% (more precisely between 10 and 13%). Economic growth was relatively weak (annual average around 1.4%) and public expenditure increased at about the same rate or at a slightly higher rate.

2.3. Modern public finance law (1914-1956)

This period began with the First World War and ended the classic period of public finance in France. During this period, the interventions of the state as well as territorial self-governing units in the economy intensified. After the First World War, social security bodies were set up to deal with the social problems of the population. This is how the welfare state was created.

The welfare state is responsible for ensuring the well-being of all citizens by permanently interfering in the economic and social life. The public finance discipline is now defined as "*the science that examines the funds used by the state, such as direct and indirect taxes, loans, financial activities to cover loans and to interfere with economic and social life*" [Hauriou 1933: 204]. In this context, we can speak of an interventionist state.

In contrast to the classical concept of public finance, it is possible to observe changes in the origins of the sources of financial resources within the modern concept of public finance. While the classical concept of public finance used taxes almost exclusively as a source, the modern concept of public finance relies heavily on loans. The state uses public money to finance economic, social, family, cultural and educational interventions.

In the economic field, the state ensured the balance of production, prices and currency; prevented price increases and maintained the purchasing power of the currency; dealt with transport (especially railways), interfered in its customs and credit policy; the state used taxes both to encourage and dampen economic activity. In the social field, the state ensured a fairer distribution of income; introduced a progressive tax; established social insurance (unemployment, pensions, illness). In the family area, the state provided family allowances and reliefs, or rather bonuses for newborns. In the cultural and educational field, the state provided grants for artistic activities or scientific research.

During this period, the public finance law gained a strength and, according to Orsoni, is characterized by four main features: "*interventionism in public budgets, increase in public spending, growth and diversity of resources, acceptance of deficits and public debts*" [Orsoni 2005: 376].

The budget model from the classical period has been reworked. In general, the economic and social changes of this period affected tax, budgetary and accounting law in France. During the Third Republic (1870 – 1940) and the Fourth Republic (1946 – 1958), Parliament's powers in the budgetary area were significantly strengthened. Paradoxically, this almost unlimited power of Parliament in the budgetary field has become a source of paralysis, while the economy has been subjected to great trials, such as global conflicts, the financial crisis and decolonization. The budget was often voted on late, and Parliament increasingly used the so-called provisional twelfths system[1], making the budget an increasingly opaque and less effective instrument. De Gaulle responded to this by adopting

[1] The system of the so-called provisional twelfths is, by its nature, close to the institution of a provisional budget, but with regard to the nuances of these institutes, they cannot be identified.

a new constitution and slowly ending the period of modern public finance and the beginning of the period of current public finance.

In terms of public expenditure, while on the eve of World War I, total public spending in France was 12% of GDP, in the interwar period it reached 24.9%, and by the end of the Second World War it was already more than 50% of GDP.

In the post-World War I period, the ratio between public expenditure and national income doubled in 20 years. The volume of public budgets grew sharply (due to the reconstruction of the state after the war, or due to economic interventions to mitigate the effects of the crisis), but with regard to fluctuations in GDP, the ratio of public expenditure to GDP changed sharply. After the Second World War, the process of accelerating public expenditure more than doubled the ratio of public expenditure to GDP from 1938 to 2016 (from 26.5% to 56.4%).

2.4. Contemporary Public Finance Law (1956-to this day)

This financial period began at the end of IV Republic. The mid-1950s were a legal turning point for current public finance discipline. The development of public finance law and its constitutional aspects (both the organic regulation on public finances of 1959 and the new constitution of 1958) developed, which became a significant discontinuity with the previous period. It was the new 1958 Constitution that limited Parliament's powers in the budgetary area in favor of the executive and set strict deadlines for the adoption of the state budget (in France, the so-called Finance Act[2]). However, the budgetary area was mainly regulated by a new organic regulation of 1959, on Finance Acts, which strengthened the already mentioned role of the executive (especially the Ministry of Finance) at the expense of parliamentary powers.

Another discontinuity with the period of modern public finance can be considered the Europeanization of public finance law. The International Conference on the Common Market and the Euratom, which began in 1956, greatly influenced the financial law of the member states, without being fully aware of it at the time. Since the signing of the Treaties of Rome in 1957, Community law has been incorporated into public revenue law and has gradually harmonized the system of indirect taxes (VAT and excise duties). During the reforms concerning monetary union, Community law had legal implications for Parliament's

[2] In France, the so-called Finance Act take a total of 4 forms: 1) the Finance Act on the State Budget; 2) the Finance Act, which amends the Act on the State Budget; 3) the Finance Act on the State Final Account and its Review; 4) the Finance Act on Social Security.

budgetary and fiscal sovereignty, as well as for the extent of the government's fiscal sovereignty by introducing limitation of deficit and excessive public debt restrictions.

On the contrary, French economic science considers the beginning of the period of current public finance discipline in 1973, which is associated with the so-called first oil shock, and the French economic science also claims that the period is slowly ending in the second half of the 1970s, i.e. with the end of the period in France known as the "*trente glorieuse*" (i.e. loosely translated thirty glorious years), as well as the influence of neoliberal economic theories. However, in view of the significant changes in the field of public finance discipline at the constitutional level, legal science dates the beginning of this period almost twenty years earlier, as this period represents an important milestone for the contemporary public finance law.

So far, the last major public finance reform in France has been linked to the Organic Act of 2001 (the *LOLF*), which replaced the aforementioned Organic Regulation of 1959 and is often referred to as France's "financial constitution". However, the term "financial constitution" is exaggerated, as organic acts do not reach the level of constitutional acts, rather divorce, and supplement constitutional acts more. The basic tasks of the LOLF were two, namely to modernize the French public financial management and to modernize the budgetary process. The LOLF has introduced a performance-oriented budgeting system (so-called performance budgeting), in which funds are distributed according to so-called public policies (such as education or health), for which the intended objectives to be achieved are set and indicators are also set to assess ex post how the objective had been achieved. The LOLF also strengthens the role of multi-annual planning, which has resulted in, among other things, increased transparency in the budgetary area. The second task of the LOLF was to strengthen Parliament's powers in the budgetary field (e.g. extending Parliament's right to amend amendments in the process of adopting a budget act or extending Parliament's scrutiny powers).

The adoption of the LOLF also literally shook the French "specialty", namely a public accounting. The LOLF is the new basic legal framework for French public accounting, followed by the Decree of 7 November 2012 on budgetary management and public accounting (the *GBCP*).

3. Evolution of public finance in Germany

Unlike many other nineteenth-century European states, Germany was not a state until its unification in 1871. For this reason, the period of development of the German theory of

public finance is not as long as the development of this discipline in France. In 1789, Germany consisted of more than three hundred territories, which were formally subjugated by the emperor from Vienna, but were virtually independent. Under Napoleon's pressure, Germany continued the policy established by the Congress of Vienna. The Central European political environment in 1815 was dominated by the Habsburg Empire and Prussia, to which were subsequently joined by a number of other central states, sorted by population, Bavaria, Hanover, Wurttemberg, Saxony and Baden. The territory, which should later to become Imperial Germany, consisted of thirty states, Frankfurt am Main and three Hanseatic cities.

With regard to public finance discipline, both the formal and the material criterion highlight important differences between these states. The basic criterion is whether the public finance system was based on the constitution. Although the three southern German states adopted the constitution relatively quickly after 1815, most of the northern German states were passive in this respect, with Prussia being a prime example. At this time, the institutionalization of public finance discipline was focused primarily on creating a basic framework for the tax system.

When German bureaucrats and politicians discussed the introduction of income tax, they always looked at the British experience. After William Pitt introduced an income tax in 1798 to fund the war against Napoleon, Prussian reformers wanted to follow the British case. After the defeat with France in 1807, Prussia had to pay considerable reparations and tried to reorganize its income. In 1808, Prussia introduced income tax, which was introduced as an emergency measure – taxpayers' resistance forced the administration to suspend tax collection. The second effort in 1811-1812 did not produce better results [Schremmer 1994: 329]. When Britain abolished income tax in 1815, the debate in Germany subsided.

The tax system of the southern states – Bavaria, Wurttemberg and Baden – was primarily based on so-called "impersonal" taxes on land, buildings and business, similar to France. In contrast, the Prussian tax system followed a rather English model and relied only partially on personal taxes. The third group of German states, largely small and poor states with little administrative control over the country, counted mainly on indirect taxes.

In the period before 1871 (i.e. before the unification of Germany), due to the great fragmentation of German states, it is practical to examine the development of German public finances in Prussia, representing 55 percent of the German population and in

southwestern Wurttemberg, a typical example of the South German personal tax system [Gerloff 1929: 52].

3.1. Constitutional and institutional framework

The public budget, as France, for example, knew it at the time, did not appear in Germany until the end of the 19th century. Legislation at the constitutional level was completely absent. Prior to German unification (i.e. before 1871), no German state had ever published budget data. Despite the fact that no German territorial state would be able to draw up a complete and unified budget, because the princely finances were usually divided into one or more treasuries.

The nobility, the church and the cities collected a number of taxes for local purposes, which were never recorded centrally. Even Prussia, known for its strict bureaucracy, was not able to compile a complete overview of all expenditures and revenues at the level under the central administration, i.e. in the provinces and municipalities before 1911. Since other German states were even less successful, the German Empire was never able to fully record total public expenditures and revenues.

During the relevant period, the discipline of financial sociology appeared, and one of its representatives, Rudolf Goldscheid, pointed out the strong influence of the budget by the power relations existing in the given state [Goldscheid 1926: 146].

3.2. The legacy of the Napoleonic Wars

During Napoleon's campaign in the German states, these states were forced to declare a constitution, which included a regular budget, which had to be prepared, adhered to and controlled. Furthermore, this reorganization concerned the annexation of smaller territories to larger German states. These changes required extensive administrative reforms, giving the highest priority to public finance reforms. The accumulation of large public debts by German states during the wars led to the introduction of new taxes and an increase in existing ones.

The states of southern Germany, which were strongly influenced by France, such as Bavaria and Baden in 1818 and Wurttemberg in 1819, were the first to adopt a constitution in Germany. The public revenues of these three southern German states consisted of revenues from "impersonal" taxes, which were created on the model of French taxes.

The case of Wurttemberg is illustrative. In 1821, the parliament created a system of property taxes on land, buildings and businesses on the basis of impersonal taxes inherited from the Old Regime. The system followed the principle of allocation, which meant that the total revenues from the three taxes was limited by parliament and, secondly, that shares in the revenue from the three taxes were set. The land tax originally contributed 71 percent, the building tax 17 percent and the business tax 12 percent. The determination of the tax for individual taxpayers was governed by a detailed regional division, which was based partly on the real estate cadastre, partly on "local use" [Spoerer 2004: 85].

An important element of the Prussian tax reforms around 1820 was the creation of a graduated head tax (*Klassensteuer*, a direct tax that was levied in rural and small parts of the city), and a mill and butcher's tax (an indirect tax that was levied in all other cities). The graduated head tax stood halfway between the election tax and the simple income tax. In order to remove the excessive burden on the tax authorities, the taxpayers were not taxed according to their actual income, but according to their social status (e.g. daily worker, baker, property owner, etc.). While the tax burden was heavily on day laborers (there was no exemption for low-income groups until 1875), large property owners did not pay more than the maximum amount of 432 marks per year. For comparison, in the first half of the 19th century, the annual wages of German builders were about 300 marks. This trend of adopting the concept of French public finance continued as a result of the political unrest caused by the July Revolution (1830) in France, with the adoption of the constitutions in Saxony, Hanover and Hesse-Kassel in 1830-1831. The Prussian kings resisted this trend until 1848, or rather 1849, when, after the tumultuous events of 1847-1848, a conservative constitution and the well-known three-class suffrage were adopted . Prussian three-class suffrage is the most important example of the relationship between political participation and taxation in 19th century Germany.

After Britain reintroduced income tax in 1842 – and this time permanently – more and more experts called on German states to follow the British model. However, the income tax has raised concerns and emotions. Liberal economists in particular have condemned income tax as bothering, confiscating or even terrorist. In contrast, an influential group of public finance economists adhered to the income tax, because it enabled the incorporation of redistributive elements into the tax system through progressive taxation. Moreover, once the tax was introduced, its positive financial results attracted bureaucrats and politicians. Most other direct taxes were inelastic; that is, revenues grew less than in proportion to revenues. Income tax has de facto kept pace with rising revenues and even offered the opportunity to draw more through tax rates

3.3. The impact of the 1848 revolution

The graduated head tax remained unchanged until the aftermath of the 1848 revolution. After the tax reform of 1851, the tax base changed from socio-economic status to actual income, and graduated head tax was limited to income groups up to 3,000 marks per year. Taxpayers whose annual income was more than 3,000 marks were subject to graduated income tax. This new tax, which also affected cities, represented a burden of around 3% of revenue, up to a ceiling of 21,600 marks.

While the graduated income tax imposed a much higher tax burden on wealthy taxpayers, it greatly changed their political views. The three-class suffrage introduced in 1849 combined the right to vote of taxpayers with the amount of direct taxes they paid. The system again divided voters into three electoral classes depending on the direct state taxes paid (graduated income tax, graduated head tax and impersonal taxes).

3.4. The fiscal structure of united Germany

The predecessor of the German Empire, which was founded in 1871, is a fiscal term – the German *Zollverein* (i.e. customs union), which was created in 1833 and came into force on January 1, 1834. The reason for creating the customs union was that the German states realized that customs duties were barriers to trade. For example, in 1818, Prussia abolished all inland customs offices. The geopolitical problem of Prussia was the fact, that its territory was divided and therefore had no common borders between the new and comparatively rich territory in the west and in the east. Prussia therefore tried to persuade neighboring states to create a customs union. This fact thus became a means of expanding Prussian political influence in Central Europe and pushing back Austria as its main competitor. The agreements that eventually led to the creation of the Customs Union (the Zollverein) stipulated that its customs revenues would be distributed among the states in proportion to their population. Increasing the gross ratio of revenues and costs of administering the customs line with the population, led smaller states to join this customs union. Increasing the gross ratio of revenues and costs of administering the customs union, led smaller states to join this customs union [Dumke 1987: 61].

Almost four decades later (1871), Germany was united and ruled by Prussia, which made up about two-thirds of German territory and population. Other important states in terms of population were Bavaria, Saxony, Wurttemberg and Baden. The southern states

reserved a number of exemptions for their consent to enter the empire, including the right to continue to collect excise duties on beer and alcohol.

The distribution of tasks between the newly created Empire and the member states was typical of a federal state. The empire was responsible for defense, international relations and the government of Alsace-Lorraine, which was annexed in 1871. In addition, a number of monopoly facilities were operated, such as the *Reichspost* and the Alsace-Lorraine railway. As for the public finances of the German Empire, its revenues consisted of customs revenues, a number of indirect taxes (which have been transferred from member states; in particular excise duties on the consumption of salt and on basic luxury goods such as alcohol, beer, sugar and tobacco) and some indirect transaction taxes.

A specific institute was the financing agreement between the Empire and the member states. The Reich Constitution of 1871 stipulated that if the Empire is not able to finance its activities with its own resources, the member states would have to pay so-called matriculation contributions, which were distributed among them in proportion to the population. When the Empire introduced so-called protectionist tariffs on these matricular contributions in 1879, member states began to fear that the empire's financial position would increase much more than they would have liked. Therefore, the Reichstag (Lower House) enacted the act obliging the *Reich* to repay the relevant amount of customs duties and taxes on tobacco, which exceeded a fixed amount of 130 million marks (increased to 143 million marks in 1896 and 180 million marks in 1897) to the member states [Dumke 1987: 34]. Thus, since 1880, matricular contributions and payments have been reciprocally sent between the Empire and the member states, greatly complicating the budget planning for the member states. For this reason, economists Adolf Wagner and Wilhelm Gerloff called for a thorough tax reform. However, the subsequent reforms did not fundamentally change the structural imbalance between the Empire and the Member States.

This imbalance was often the subject of debate both in the *Reich* and later in Germany. The traditional view is that the Empire was financially weak and the member states were unwilling to improve its financial position. The empire was responsible for the increased accumulation of central government debt in the run-up to the First World War [Schremmer 1994: 464]. For example, Niall Ferguson claims that the empire's weak financial position in response to arms races with major German adversaries (France, Russia, and Britain) was hopeless in the long run, and this fact forced the imperial army to declare a preemptive strike in the summer of 1914 [Ferguson 1994: 135-148]. Charles Blankart, on the other hand, stated his hypothesis: The fact that the Empire increased its debt as a result of its budget allocation is considered to be the result of a soft budget constraint, and

therefore retroactive financial assistance from Member States followed, which had to increase their matriculation contributions [Blankart 2007: 51-54].

3.5. Increase in public expenditures

The expenditure side of the classic early princely budget was dominated by three items that helped the prince gain, retain, and prove his power: the army, public administration, and the courts. As mentioned earlier, in addition to the prince, a number of other sub-central institutions also collected taxes and spent them on collective purposes, such as the general administration and maintenance of local roads and bridges.

During the 19th century, a number of items of expenditure gained in importance: education, administration, public services, transport and social welfare. The army lost its importance during the 19th century and regained it only a few years before the First World War.

Expenditure on education, which was primarily covered by municipalities, was increased due to the increasing importance of the following three factors. The first factor was the increasingly promotion of compulsory education introduced in Prussia as early as 1717. The second factor was the increasing population rate that Germany experienced in the 19th century [Guinnane 2003: 73]. The third factor concerned the quality of education, as at this time the teaching profession was becoming more professional, which was reflected in higher salaries. In Prussia in 1891, expenditure on basic education amounted to 66% of total public expenditure on education (and 69% in 1911). While Prussian municipalities and the state spent 33 million marks on basic education in 1864, in 1911 this amount increased to 421 million [Dumke 1987: 111].

Administrative expenditure in individual states has increased because major administrative reforms have been realized. The aim of this reform was both to unify the original territory with the territory acquired before 1815 (and in 1815), and to strengthen control over the state as such. This reform also included updating obsolete land registers (for example to allocate land tax) and increasing activities of individual states to improve infrastructure.

3.6. The fall and rise of Income Tax

A number of German states followed the British example, such as Saxony, then the most economically advanced German state in 1878, and Baden in 1884. However, other southern states have so far been stuck on their rather sophisticated impersonal tax

systems. In Germany, there has been a change in income tax with the famous tax reform of the Prussian Minister of Finance Johannes von Miquel. After Bismarck, a zealous enemy of direct taxes and especially income tax, left the function in 1890 (both as German Chancellor and Prussian Prime Minister), the path for income tax was open. The Prussian income tax was introduced in 1891 and increased revenues more than its proponents had hoped. This was followed by a property tax, which, unlike the current ones, also focused on financial assets. Revenues from existing impersonal land taxes and business taxes were transferred to the municipalities [Schremmer 1994: 443-448].

For many reasons, Prussian politicians wanted to keep income tax and reject the proposal to its transfer to the Empire. The first reason was simply its profitability. Second, the income tax, especially if it was reinforced by progressive elements, was considered as an uncertain tool that should not belong to Socialists, who were much more successful in the Reichstag elections than in the Prussian lower house, which was easier for ruling elites to control due to the three-class suffrage. Thus, unlike Britain, the German Empire did not have a central income tax on the eve of the First World War.

3.7. Public enterprises and state finances

Another peculiarity of German budgets in the 19th century – at the state level and after 1871 at the *Reich* level – was the high share of revenues from public enterprises. Among them, traditional enterprises were created, such as those responsible for land, forests, salt and coal mines, etc. Postal services expanded in parallel with the developing manufacturing and service sectors. Public enterprises have increasingly joined traditional public establishments. Expenditures and revenues from public enterprises have, of course, increased the budget. However, if we are interested in the financial burden of the taxpayer, it makes more sense to look at the surplus (or loss) of public enterprises.

3.8. Taxation and distribution

If, as financial sociologists claim, the public budget is a mirror of power relations in the state, then we should assume that the process of democratization in Germany in the 19th century is reflected in the fiscal system. From a theoretical point of view, it is necessary to estimate the impact of the budget, i.e. redistributive effects that occur on the revenue side (people pay the state) and on the expenditure side (people value public and private goods provided by the state). However, such a general assessment of the distributional effects of a public activity is not feasible even today. Given that the distributional impacts on the

revenue side are easier to assess than distributional impacts on the expenditure side, we have to focus on the former.

Eckart Schremmer states that the tax system at the beginning of the 19th century was very favorable for wealthy members of society [Schremmer 1994: 452-454]. He rightly argues that direct tax reforms in Germany in the 19th century had an increasingly progressive stance. However, the share of indirect taxes increased in the last quarter of the 19th century in both Prussia and Wurttemberg, especially when the public operating surplus is taken into account. As the tendency to save increases with increasing revenues, indirect taxes have a regressive distributional effect. In the 1980s, decades after Germany returned to high rates, the share of indirect taxes increased by 10 percentage points in Prussia and 15 percent in Wurttemberg. In 1886, when imports of grain and meat constituted for 15% of all customs revenue and imports of typical luxury goods for ordinary people such as coffee, coffee substitutes and tobacco constituted another 34% [Statistisches Jahrbuch fur das Deutsche Reich 1887: 185-187], the effects rates were probably also regressive.

The fiscal burden on ordinary German households thus remained high at the end of the 19th century. It was not until the turn of the century that the share of indirect taxes decreased significantly.

3.9. Migration and tax competition induced by taxes

Taxation always leads to escape measures by taxpayers: tax avoidance, tax fraud, tax revolts – or peaceful migration to a lower tax regime. This fact in turn encourages the legislator to reduce the tax burden on mobile factors so that wealthy taxpayers can come back. The tax breaks offered by medieval or early modern business cities to attract wealthy distance traders were the first example of tax competition.

The idea of tax competition is relatively simple. If the legislator reduces its marginal tax rate to a slightly lower rate than a competitive legislator does, it can attract wealthy taxpayers. If legislators do not harmonize their tax rates, but instead they compete by underestimating the competitor's rate, they are in a vicious circle and they are racing at the lowest tax rate level. Such a race may result in sub-optimal provision of public goods and empty public budgets, which no longer allow redistribution measures to be maintained [Sinn, 1989: 63]. In the 19th century, which experienced much more vertical and horizontal mobility than ever before, migration and tax competition induced by taxes became increasingly important. When Prussian bureaucrats discussed measures to reform the graduated head tax, which was introduced only a few months ago, tax-induced migration

was clearly a credible threat, especially in a country with many states of the same language. At the end of 1820, the director of the Prussian statistical office warned in a memorandum of the Ministry of Finance: "*How dangerous it is to get capital to emigrate to regions where its consumption is less taxed. The German will also be able to find his homeland outside the Prussian state, and migration from a German state to another state is easier than migration from England to France or Germany*" [Spoerer 2004: 169]. In fact, although the burden of the graduated head tax, which was levied mainly in rural areas, was only 432 marks (between 1821 and 1851) for the highest-income people, many wealthy property owners resided in a nearby town, which was subjected to milling and butchery tax which was negligible for them. If they were able to convince the financial administration of the fact that they had spent at least half a year in their city residence, they were exempt from graduated head tax.

As the tax burden increased during the 19th century, the problem of tax-induced migration and tax competition continued to increase. In the late German Empire, individual legislators did not compete for multinational corporations, as they do today, but for wealthy tenants at the local or national level. They did so because the Prussian local tax reform of 1893 gave municipalities the right to collect individual increased rates at the level of state direct taxes. When the local tax reform came into force in 1895, every Prussian city was entitled to levy increased rates on land taxes, trade tax, and income tax. While the country is motionless and corporations were less mobile than today, many wealthy taxpayers, especially tenants, were highly mobile.

In other words, wealthy taxpayers took the opportunity to reduce their income tax burden by choosing another place of residence, and thereby they forced municipalities to react to this behavior. For example, municipalities in the Berlin area actively promoted their low tax burden in the press. In 1904, Adolf Wagner, already an important old man of German public finance, called this race the "infinite thread" [Wagner 1904: 63].

For this reason, local politicians decided to merge the municipalities around Berlin to create a larger entity called *Gross-Berlin*, whose explicit purpose was to stop tax competition among these municipalities. It was not without reason that Matthias Erzberger, the first Minister of Finance of the Weimar Republic, centralized income tax and ironically explained in 1919: "The German taxpayer will no longer have to bother calculating whether he can reduce his tax burden by moving to Berlin, Grunewald, Coburg or Lake Constance" [Schmoller 1870: 39].

By centralizing income tax, Germany has solved the problem of increasing tax competition among its municipalities. At the beginning of the 19th century, when international migration was constrained by language problems, high transaction costs and nationalism, the above-mentioned harmonization was a political choice.

3.10. Recurrence of public debt

After the Napoleonic Wars, many surviving German states were deeply indebted and it would require decades to repay these debts. It was only after the turn of the century that more new debts arose than the old ones were paid off at the state and municipal levels. The main reason was the opportunity offered by existing (smelters, mining) or new (e.g. services or railways) public enterprises. Thus, the funds obtained from public loans could not fill the gaps between current revenues and current expenditures, but the funds could be used as a means for potentially beneficial investment projects.

The situation was different for the Empire. Since the inflow of matricular contributions was parallel to the large flow of payments, the Empire was often a net payer to the member states [Schremmer 1994: 468]. Thus, the Empire lacked ordinary income to maintain a strong army and build a navy which was the second strongest after the British.

On the eve of the First World War, the total debt in Germany was 29.5 billion marks: the Empire 5 million marks; member states 17 million marks; and the municipality 8 million marks [Schremmer 1994: 470]. In relation to the net national product, these statistics represented a total public debt ratio of 59%. Although the debt to gross domestic product ratio was around 52%, which is not far from 60% of the European Union's Maastricht criterion, the situation was different. *Grosso modo*, only the Empire's debt was unproductive, while the member states and municipalities had mostly balanced ordinary budgets and their debts were caused mainly due to investment projects.

3.11. Partial conclusion

Undoubtedly, German tax systems underwent a process of deep modernization during the long 19th century. Formally, the whole process of budget preparation, enforcement and control has been streamlined. Assessing the material aspect of these changes is not that simple. Although at the turn of the century, horizontal tax equity (in which the same solvency leads to the same amount of tax) was by no means standard in a particular member state, this equity was generally achieved before the First World War, except for differences due to tax laws among member states.

However, the implementation of the principles of vertical tax justice (greater ability to pay leads to higher taxation) was much more difficult [Buchanan, Musgrave 1999: 83]. Redistribution through the tax system has proved to be a very controversial principle and it has naturally found many political obstacles. This is well illustrated by the revenue side of public finances, which permits to discuss recent theories of fiscal stage models. Shortly before the end of the First World War, the Austrian economist Josef Schumpeter published the article entitled “The Crisis of the Tax State” (1918), in which he developed a three-phase model describing the development of fiscal systems. He used the term “manor state” for antiquity period, which degenerated the term “manor economy” in the Middle Ages. Rising military costs forced monarchs to accumulate debt in early modern times. To pay off debts, they expanded the tax system, which became the backbone of their finances soon: “*The tax has so much in common with the state that the term "tax state" could almost be considered a pleonasm*” [Schumpeter 1918: 19]. Schumpeter's model is generally considered to be the starting point for fiscal phase models, although other authors, such as Gustav Schmoller, formulated similar ideas four decades earlier [Schmoller 1870: 113].

Schumpeter's conception of the manor state and the tax state was defended in particular by Kersten Krüger (1987), who developed criterions for the characterization of the manor state and the tax state. It inspired Richard Bonney [Bonney 1995: 451] and W. Mark Ormrod [Ormrod 1999: 10, 16] to extend this phase model. They distinguished 4 phases in fiscal history: (1) tribute state, (2) domain state, (3) tax state and (4) fiscal state. Although they did not explicitly state which criteria they considered necessary, the mere fact that they adhered to the concepts developed by Schumpeter – the manor state and the tax state – suggests that the structure of income is crucial in their phase model [Dumke 1987: 78].

The taxation introduced by the Empire increased the relative burden on the poor, because many customs duties were paid by consuming grain, meat, and basic goods. The share of direct taxes, mostly paid by the rich, increased until the end of the 19th century, when Saxony, Baden and Prussia introduced a general income tax. These tax reforms have increased vertical tax competition and paved the way for breathtaking tax increases in the 20th century.

4. Conclusion

The contribution deals with the evolution of public finance in two selected countries – France and Germany. This contribution analysed the public finance evolution with regard

to the relevant historical context, or rather background and consequences of this evolution. There were introduced several historical stages in France and in Germany which were important for the evolution of public finance discipline.

A comparison of developments in these countries shows that the French history of public finance is much longer than the German one. While the history of the public finance discipline in France dates back at least to the 14th century, in Germany a gradual evolution of this discipline can be observed with certainty only from the 19th century.

In France, there are four main historical stages, in which it could be found out by observation crucial milestones such as (arranged chronologically) the division of budgetary and fiscal powers between the competent authorities, application of the principle of consent to taxation, the emergence of the welfare state and the development of public finance law and its constitutional aspects.

As it has already been stated, the Germany history of the public finance discipline is not so long. In the case of Germany, the situation was more complicated, as it was necessary to deal with the case of Prussia and other German states such as Bavaria, Wurttemberg, Baden or Wurttemberg. Public finance evolution in each state was different, which ended with the unification of Germany in 1871. The issue of the evolution of public finances in Germany was associated primarily with the customs union, increasing public expenditures and the fiscal system (especially the various types of taxes and the issue of tax competition). It can be concluded that Germany was significantly inspired by France due to Napoleon's campaign in the early 19th century. This fact was reflected mainly in the tax area.

The main aim of the contribution was to confirm or disprove the hypothesis that the evolution of the public finance discipline was different in each of the selected countries. This hypothesis was confirmed. The partial aim of the contribution was achieved thanks to appropriately chosen scientific methods.

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