

Editorial

EUCIT: For How Much Longer Will Political Objections Outweigh the Advantages?

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For the drafters of the EEC-Treaty of 1957, it was obvious that the indirect taxes that were raised by the Member States could have a negative impact on the establishment of the common market and could give rise to distortions of competition. In that period, moreover, the relative share of indirect taxes was more important in most Member States than the share of direct taxes. This explains why the Member States showed a great willingness to reach a far-reaching harmonization of these taxes in view of the establishment of a common market. In the EEC-treaty itself, stipulations were inserted that lead to, among others, the gradual abolishment of customs between the Member States and to the introduction of a common customs tariff. Additionally, concerning other indirect taxes (sales taxes, excise duties, indirect taxes on the raising of capital), the will to coordinate national policy was initially very strong.

Even though today it is taken for granted that also direct taxes (among which corporate income taxes) can have a negative impact on the establishment of the internal market, the drafters of the EEC-treaty in 1957 paid much less attention to these taxes at first sight. Direct taxes were apparently regarded as a distinctly national competence. Nevertheless, even at that time one was aware of the issues surrounding the question whether and to what extent differences between the Member States concerning direct taxes could hinder the creation of the common market. In the Neumark report of 1962,¹ special attention was paid to these questions. The report dealt with the disparities on *'the nature and level of direct taxes, including incentives, special treatments and measures taken for the avoidance of double taxation'*. However, the Fiscal and Financial Committee (FFC) noted that *'the aim under consideration is not uniformity, but solely harmonization of tax systems and of financial*

policy' (...) (p. 102): *'complete unification of the tax systems of the Member States – even if it is held ad inconvincendum that it is politically achievable – would not be considered as necessary for the aspect of integration policy, since experience proves that on many grounds moderate differences limited to the nature (structure) and to the rate of taxes do not hinder the free play of competition'*.² Almost prophetically, the report assumed rightly that in the course of the gradual achievement of integration as envisaged under the Treaty of Rome, the Common Market itself would bring into being strong forces which would press Member States to a certain extent towards harmonizing their tax policy.

However, during the following decades, the (harmonization) initiatives within the EU in the field of corporate income taxes, remained quite modest. In particular the following directives can be mentioned: the Parent-Subsidiary-Directive (1990), the Merger Directive (1990), the Arbitration Convention and the Interest and Royalties Directive (2003). For the time being, all the attempts since 1975 to introduce a kind of common consolidated corporate income tax base (CCCTB) remain unsuccessful. Even the latest proposal of March 2011 on the (optional) CCCTB which the European Commission has placed on the agenda remains, after a decade of preparation, without result till today.

Important recent developments, however, make it clear that, particularly in the area of corporate income tax, a more integrated policy within the European Union is becoming increasingly necessary.

On the one hand, multinational companies still succeed in minimizing the fiscal pressure on their globally acquired profits by pitting the fiscal regimes of countries in which they operate, against each other. The multiplicity of fiscal regimes and the inconsistencies between these regimes still offer numerous possibilities for fiscal optimizations. On the other hand, many countries (often smaller countries) – also in the European Union – use corporation income tax as a lever to compete with each other for attracting businesses against very attractive fiscal conditions by means of

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¹ That is, the Report of the Fiscal and Financial Committee (FFC). The EEC Reports on Tax Harmonization, Book II. The FCC had to *'study under what conditions tax frontiers can be eliminated within the Common Market or at least, reduced to an indispensable minimum'*.

² The Report of the FFC. The EEC Reports on Tax Harmonization, Book II, p. 100.

various techniques such as, among others, (niche-oriented) tax-friendly regimes (tax shelters), tariff reductions and rulings. The consequential ‘race to the bottom’³ has a pernicious influence on the fiscal revenues of corporate income tax. Moreover, this fiscal competition is not only harmful to government budgets, but also companies that do not operate or operate less cross-border have therefore less possibilities for such fiscal optimizations.

Some figures:⁴ the average highest rate of corporate income tax in the EU28 countries amounts to 22.9% while in 1995 it still amounted to 35.0%. The total revenue from corporate income tax in EU28 for 2012 amounted to EUR 323 billion or approximately 2.5% of Gross Domestic Product (GDP). This revenue represents only 6.3% of the weighted average of the total tax revenues in the EU28 countries. To compare:⁵ in 1997 the share of corporate income tax was 3% of the GDP and 7% of total tax revenues.

Since the beginning of the last century, many countries have undertaken numerous attempts to eliminate mutual inconsistencies between their tax regimes in cross-border situations. Till today these attempts seem insufficient. This led the OECD to draft a detailed action plan on Base Erosion and Profit Shifting⁶ in 2013. Also the European Union keeps its end up. On 16 December 2014, the European Commission⁷ announced its Work Programme for 2015 (‘A New Start’). One of the new initiatives is an ‘Action Plan on efforts to combat tax evasion and tax fraud, including a Communication on a renewed approach for corporate income taxation in the Single Market in the light of global developments’. This Action Plan intends, starting from the work already done on base erosion and profit sharing at OECD and G20 levels, to include measures at EU level in order to move to a system on the basis of which the country where profits are generated is also the country of taxation, including in the digital economy. The Communication aims at stabilizing corporate income tax bases in the EU for a fair taxation environment, including re-launching work towards a Common Corporate Consolidated Tax Base.

The European Commission clearly still strongly counts on the introduction of a CCCTB. This form of harmonization will always generate winners and losers

among the countries concerned. The Commission’s impact assessment shows that, in general, the smaller Member States lose and the large Member States win tax base.⁸ Hence, it is not surprising that especially the losing countries are not convinced about the system. An important objection is related to the way in which the group’s aggregated tax base is divided among the Member States in which group companies are subject to tax. This attribution occurs on the basis of an ‘apportionment formula’, which contains three apportionment criteria of *equal weight*: capital, labour and turnover, i.e., fixed assets, personnel/wages and sales. These fixed criteria (especially the asset factor) do not always reflect economic reality. If they want to collect the same tax revenue, loser States will therefore have to increase the tax burden on industry not opting for the CCCTB or on any other tax base, such as labour, or will have to raise their tax rate, which is not attractive from a policy competition point of view.⁹ Moreover, even some winner States like Germany, made reservations regarding the consolidation regime itself and regarding its optional character. In light of the *one stop shop* idea on which CCCTB is also based, numerous Member States have serious doubts on the ability of the tax administrations of some Member States to implement and enforce the application of CCCTB correctly.

In light of the foregoing, the question arises whether the introduction of a single European Corporate Income Tax (EUCIT) should (again) be investigated. This proposal goes far beyond the CCCTB because it involves not only the harmonization of the tax base, but also that of the tax rate. EUCIT can be conceived as a compulsory scheme only applicable for large multinationals and operating alongside national rules applicable to local companies. It can also be conceived as a more general scheme applicable to all companies. Under this model, the tax could be levied at the European level and a part or all of the revenue could go directly to the EU (see later).

The introduction of EUCIT has many advantages: first, it will simplify the realization (at least at the European level) of the action points included in the OECD Action plan on BEPS.¹⁰ Furthermore, EUCIT prevents Member States from using corporate income tax as a lever for harmful tax competition. The aforementioned ‘race to the bottom’ will stop and the

³ B. Genser, *Capital Taxation in an Enlarged EU: The Case for Tax Coordination in: Capital taxation after EU Enlargement*, Proceedings of Österreichische Nationalbank Workshops, nr. 6, p. 105 (2005).

⁴ Taxation trends in the European Union. Data for the EU Member States, Iceland and Norway, European Union (Eurostat Statistical books, ed. 2014) http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2014/report.pdf.

⁵ Structures of the taxation systems in the European Union 1970–1997 Eurostat, 8 (2000), http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/structures2000_en.pdf.

⁶ <http://www.oecd.org/ctp/BEPSActionPlan.pdf>.

⁷ European Commission Com (2014) 910 final 16 Dec. 2014.

⁸ Commission Staff Working Document. Impact Assessment, Brussels, 16 Mar. 2011 SEC (2011) 315 final http://ec.europa.eu/taxation_customs/resources/documents/taxation/company_tax/common_tax_base/com_sec_2011_315_impact_assesment_en.pdf.

⁹ B.J.M. Terra & P.J. Wattel, *European Tax Law*, 801 (Kluwer L. Intl. 2012).

¹⁰ Reference may be made to the fifteen action points as listed in the OECD (2013) Action Plan on Base Erosion and Profit Shifting, OECD Publishing, 40 p. (<http://www.oecd.org/ctp/BEPSActionPlan.pdf>).

fiscal capacity of corporate income tax will be restored.¹¹ Moreover, EUCIT can (wholly or partly) qualify as a new direct source of 'own resources' for the EU, replacing other income of the EU that rather qualify as national contributions of the Member States.¹² The system of 'own resources' enables the EU to finance its policies. In 2012, total EU revenue amounted to EUR 139.5 billion. Successive reforms have determined the system's current configuration, which relies on three key streams of revenue:¹³

- (1) The traditional own resources (mainly customs duties) representing 12% of total revenue in 2012, Member States retain 25% of the amounts as collection costs.
- (2) A resource based on Value Added Tax (VAT), accounted for 11% of total revenue in 2012.
- (3) A resource related to Member States' Gross National Income (GNI). This budget balancing element represented around 71% of total revenue in 2012.

Next to the aforementioned resources, there are other resources, which are not classified as own resources, namely taxes on EU staff salaries, contributions from non-EU countries to certain programmes, and fines on companies for breaching competition law. In 2012, these resources qualified as 'other revenue' accounted for 6.2% of the total (EUR 8.6 billion).

By phasing out the national contributions, the introduction of EUCIT could be organized in such a way that it would be (at least) a budgetary-neutral operation for the Member States and the EU. According to a recent study of the European Parliamentary Research Service,¹⁴ one of the major shortcomings of the current system is that it does not follow the provisions of the Treaties. Whilst these provisions (Article 311 TFEU) provide the Union with financial autonomy, most¹⁵ EU revenue depends on resources that are perceived as national

contributions. In the aforementioned study, some new possible own resources are mentioned. Next to revenues from the EU Emission Trading System (ETS), charges related to air transport and energy/carbon taxes, the EU Corporate Income Tax (EUCIT) is mentioned.¹⁶ In the study, author argues that '*an own resource assigning part of corporate income taxation proceeds to the EU, or EUCIT, would have a much broader scope than a CCCTB*'. But he immediately points out that '*due to the high political sensitivity of the corporate income taxation area, the Commission does not appear to consider the EUCIT a feasible option for the near future*'. In 2001, the Center of Economic Policy Studies specified as one of the disadvantages of EUCIT that it is politically difficult to achieve, especially in the short term: '*Instead of a short-term policy goal, EUCIT may be better thought of as a possible long-term solution to European corporate income taxation.*'

In the context of the political deal for the 2014–2020 Multiannual Financial Framework (MFF), the European Parliament obtained agreement from the Council that a high-level group (HLG) be set up to prepare a possible revision of the system.¹⁷ Diverse options are possible going from a simple financing system by which the entire budget is financed with a GNI resource on the one extreme, to a regime by which one or more new genuine own resources are created eliminating or reforming some of the existing resources, on the other extreme. The review of the system has to comply with four guiding principles: (1) simplicity; (2) transparency; (3) equity; and (4) democratic accountability.

To the extent that the need for actual financial autonomy of the European institutions in the sense of the EU treaty and the Treaty on the Functioning of the EU is deemed more important, the more important it becomes to evolve to a regime in which the national contributions are phased out and new genuine own resources are introduced.

On 17 December 2014, the HLG issued its first assessment report.¹⁸ It summarizes the key features of the current system and of recent reform attempts. Moreover, it deals with the methodological approach that will guide the activities of HLG and stresses that the viability of reform recommendations will depend not only on the economic soundness of the proposals but also on the careful consideration of the institutional and political aspects of the reform process.

With a view to its further work, the HLG has raised numerous questions in its report. In light of this editorial, two of these questions are very relevant: (1) Within the context of existing EU policies, and in

¹¹ On the economic advantages of this system, see i.a. T. Molenaar & I.T. Van Den Bergh, *Introducing a European Union Corporate Income Tax on the basis of an Enhanced Cooperation Agreement*, Forfaitair 10–15 (2011/219); A. Van der Horst, L. Bettendor & H. Rojas-Romagosa, *Will corporate tax consolidation improve efficiency in the EU?* CPB Neth. Bureau Econ. Policy Analysis, 78–80 (2007).

¹² On EUCIT, see: Commission Working Staff Paper, *Financing the EU Budget: report on the operation of the own resources system*, 27 Oct. 2010 (COM(2011) 510 final. SEC(2011) 876 final/2). On the economic advantages of this system see i.a. T. Molenaar & I.T. Van den Bergh, *Introducing a European Union Corporate Income Tax on the basis of an Enhanced Cooperation Agreement*, Forfaitair, 10–15 (2011/219); A. Van der Horst, L. Bettendor & H. Rojas-Romagosa, *Will corporate tax consolidation improve efficiency in the EU?* CPB Neth. Bureau Econ. Policy Analysis, 78–80 (2007).

¹³ European Parliament Research Service, *How the EU Budget Is Financed. The 'Own Resources' System and the Debate on Its Reform*, In-depth analysis, 30 (June 2014).

¹⁴ Alessandro D'Alfonso, European Parliament Research Service, *How the EU budget is financed. The 'own resource' system and the debate on its reform*, In-depth analysis, 1 (June 2014).

¹⁵ For the year 2013: 83% (cf. First assessment report, High-Level Group on own resources, 13 (17 Dec. 2014) (http://ec.europa.eu/budget/library/biblio/documents/multiannual_framework/HLGOR_1stassessment2014final_en.pdf).

¹⁶ Alessandro D'Alfonso, European Parliament Research Service, *How the EU budget is financed. The "own resources" system and the debate on its reform*, In-depth analysis, 25 (June 2014).

¹⁷ Joint declaration of December 2013 attached to the agreed 2014–2020 Multiannual Financial Framework.

¹⁸ http://ec.europa.eu/budget/library/biblio/documents/multiannual_framework/HLGOR_1stassessment2014final_en.pdf.

particular the Single Market, what are the resources most solidly justified to become an own resource? And (2) in the current economic context, what are the resources best suited to become an own resource and why? Under what conditions?

Hopefully, the HLG includes EUCIT in its assessment. The HLG will present the final outcome of its analysis in 2016.