

Opinion Statement FC 10/2018 on the European Commission Platform for Tax Good Governance Discussion Questionnaire on Tax Competition and Competitiveness

Prepared by the CFE Fiscal Committee

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This CFE Opinion Statement sets out CFE's views on tax competition and competitiveness. It was submitted to the EU Platform for Tax Good Governance in December 2018. CFE representatives at the Platform for Tax Governance are Piergiorgio Valente, President of CFE and Stella Raventós, Chair of the CFE Fiscal Committee.

CFE Tax Advisers Europe is a Brussels-based umbrella association uniting 30 European national tax institutes and associations of tax advisers from 24 European countries. Founded in 1959, CFE represents more than 200,000 tax advisers. CFE Tax Advisers Europe is part of the European Union Transparency Register no. 3543183647 - 05. For further information regarding this opinion statement please contact Stella Raventós, Chair of the CFE Fiscal Committee or Aleksandar Ivanovski, Tax Policy Manager at info@taxadviserseurope.org

This Opinion Statement responds to the European Commission Platform for Tax Good Governance discussion questions, setting out CFE's views on matters related to tax competition and competitiveness in general.

What and who defines a competitive tax system?

At a time of immense change in the international tax framework, CFE believes that tax policy tools and instruments should be utilised to promote competitive tax systems that help generate economic growth and prosperity for society. We accept, however, that competitiveness of tax systems is a relative concept in an international context. Fiscal policies to a large extent remain a prerogative of each country, involving difficult choices which allow jurisdictions to exercise their tax sovereignty in a way that produces the best outcomes for their societies. Hence, CFE acknowledges the fiscal sovereignty of Member States and their liberty to design competitive tax policies fit for their social and economic systems, to the extent these are compliant with EU law and OECD BEPS commitments, i.e.:

- primary EU law (fundamental freedoms and state aid rules);
- secondary EU law that concerns harmonized areas of taxation (VAT, the DAC administrative framework¹ and the corporate tax directives that affect the functioning of the Single Market)
- the OECD BEPS Action Plan and the related recommendations and guidance.

The CFE concurs that tax policy and administration directly affect the pillars that define a competitive tax system.² As such, stable institutions and a predictable environment for doing business, tax good governance standards, absence of corruption or undue influence of judicial and administrative decisions, macroeconomic considerations such as the economic impact of tax reforms, as well as a dynamic market all play a role in defining a competitive tax system. The competition factors that play a significant role in this framework include tax rates, the availability of double taxation relief in practice and the taxable base, all of which have had significant impact on cross-border investment decisions to the extent that countries

¹ The EU legislative framework for administrative cooperation:

- Directive 2011/16 - removal of banking secrecy, exchanges on request and spontaneous exchanges; AEOI on five non-financial categories (employment income, director's fees, pensions, life insurance products and property – income and ownership)
- DAC 2 (Dir 2014/107) – AEOI on financial account information: interests, dividends, account balances info etc.
- DAC3 (Dir 2015/2376) – automatic exchange of as of January 2018 of advance cross-border rulings (confirmatory rulings) and transfer-pricing rulings (advance pricing agreements): using a central directory of rulings
- DAC 4 (Dir 2016/881) – Country by Country Reporting on certain financial information: revenues, profits, taxes (paid and accrued), accumulate earnings, number of employees and certain assets
- DAC5 (Directive 2011/16) – Access to UBO registers by tax administrations
- DAC6 – mandatory disclosure rules on reportable cross-border arrangements

² World Economic Forum, *Global Competitiveness Report* (2011)

have had to compete for both investment and the related taxable revenue. Similarly, technological developments and the ability of economies to adapt to innovative business models, as well as sufficient focus on research and development related expenditure bear significance in the discussion on the competitiveness of a tax system.

The CFE believes that tax systems should contribute to an environment which is business friendly and attracts investment. Private sector investment creates growth and jobs, whilst the current state of the economy calls for tax policies that give priority to an investment-friendly environment. Ideally, tax policy decisions would as little as possible distort the investment forms and choices, in the longer-term interests of the EU internal market. In CFE's view, in absence of harmonizing legislation, the investment decisions could be driven by fiscal factors and Member States should retain their powers to influence such decisions to the extent these decisions take into account EU's criteria for tax good governance and the commitments made in the OECD BEPS process.

Simpler and more coherent tax rules throughout the EU would also contribute to a more competitive tax system, making the EU Single Market a more dynamic and business-friendly environment. This approach is in line with the finding of the European Commission Taxation Paper that "At the domestic level, the key aspects to consider are the simplification of tax rules and tax compliance and the features of process generating the tax law". As such, coordinated measures among EU Member States' rules would prevent mismatches among national legislations, which is an element to consider for a competitive tax environment, taking the interest of the Single Market as whole.³

Does a competitive tax system rely on a level playing field?

From CFE's perspective, tax policy, the implementation of tax laws and tax administration need to ensure there is a level playing field in the Single Market. Competition arising from jurisdictions putting in place harmful or aggressive tax measures affect markets and consumers across the board. It is not only a matter of EU Member States following primary and secondary EU law, but all Inclusive Framework jurisdictions (in the case of BEPS initiatives) implementing and adhering to agreed initiatives. If this is not the case, issues of competitiveness arise.

In the absence of a requirement for 'substantial economic presence', certain tax regimes could be perceived as harmful, as indicated by the EU's Code of Conduct for Business Taxation, which was established in 1997 as a commitment of the EU Member States towards a tax environment that ensures a level-playing field in the EU Single Market.⁴

³ European Commission Taxation Working Paper 67 of 2017, 'Tax Uncertainty: Economic Evidence & Policy Responses', page 24

⁴ Resolution of the Council of the EU of 1 December 1997 on a Code of Conduct for business taxation, acknowledging the positive effects of fair competition and the need to consolidate the competitiveness of the European Union and the Member States at international level, whilst noting that tax competition may also lead to tax measures with harmful effects, the need for a Code of Conduct for business taxation designed to curb

The results of the work of the Code of Conduct group are significant, helping not only to improve competitiveness in the EU Single Market, but also in ensuring that national tax systems remain competitive on fair terms. Similarly, the role played by the Code of Conduct process in establishing fair tax competition involving third countries (non-EU states) is significant too.⁵

Apart from the Code of Conduct process, to ensure a level-playing field in the Single Market, the Commission is also relying on its powers to scrutinise national tax practices against the EU State Aid rules⁶. In doing so, CFE believes that DG Competition should refrain as much as possible from introducing retroactive standards that could affect both tax certainty and the competitiveness of the EU Single Market.

Efficient tax systems demand a delicate balance between ensuring certainty of the laws and their application but also promoting tax policies that are fit for purpose in a particular context. However, if that balance is not reached, it will lead to tax uncertainty and undermine the tax system as a whole. For instance, the retroactive introduction of certain fiscal State aid compliance criteria, in our view would have such unintended consequences. Accordingly, the achievement of a desired balance should be based on two main pillars: Clarity of tax legislation and tax administration practice, and absence of retrospective legislation.

On balance, CFE believes that a level-playing field is indeed a very important consideration in the tax competitiveness debate, affecting markets and consumers across the board. Additionally, CFE believes that the EU should follow initiatives agreed to at international level, provided that the other OECD Inclusive Framework partners do the same. Issues of competitiveness and competition clearly arise where this is not the case.

In CFE's view, Member States should otherwise be free to make their sovereign choices in designing and implementing tax policy choices. Such practices however should not be based on harmful tax measures that are a clear manifestation of 'ring-fencing' and hence unduly distort the level playing field in the Single Market.

harmful tax measures, and emphasizing that the Code of Conduct is a political commitment and does not affect the Member States' rights and obligations or the respective spheres of competence of the Member States and the Community resulting from the Treaty, Preamble of the Council Resolution of 1 December 1997

⁵ Dr Tom O'Shea, *Ensuring Fair Taxation: 20 Years of the EU's Code of Conduct Group*, Tax Notes International, November 2018, page 717

⁶ Article 107(1) of the Treaty on the Functioning of the European Union: "Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market."

How to improve tax competitiveness?

Reducing complexity and distortions

Reducing complexities and distortions in the tax system is crucial to improving tax competitiveness. It requires simplicity and clarity of legislation, by introducing simple and easy to understand tax laws which ultimately work well in practice. In this respect, legislation should set clear general principles, which seek to prevent misinterpretation of the rules by both taxpayers and tax administrations.

At EU and international level, coordination should be pursued in order to avoid mismatches and loopholes that create opportunities for double interpretations. The established standards should also provide for best practices within the legislative process. In particular, all stakeholders should be given the opportunity to meaningfully engage with legislators prior to the implementation of legislation.

Stakeholder consultations prior to the enactment of legislation is a very positive feature of the legislative process in some Member States, all of which contributes to reducing the 'red-tape' perception and hence the complexity of a tax system. Stakeholder consultation should be of adequate duration, and allow for input on all aspects of the proposed measure rather than on narrow standalone issues. Feedback documentation summarising consideration given to responses to the consultation would facilitate a transparent and meaningful process.

Improving taxpayers' rights

Given the importance of this topic for stability and predictability in a competitive tax environment, CFE has long advocated for binding EU rules for protection of taxpayers. A fundamental right of tax certainty is therefore suggested, which is promulgated in the Model Taxpayer Charter, an initiative of three international tax professional organisations, CFE, AOTCA and STEP.⁷ It was compiled in 2013 and updated in 2016, to take into account interim developments. The compilation of the Model followed an extensive survey on the status of taxpayers' protection in 41 jurisdictions. It reflects the views of its authors' organisations on how to ensure taxpayers' position in the system, stimulate their trust, boost compliance and form competitive tax systems.

CFE has fully endorsed the EU's approach and views expressed by the European Commission⁸ that a Code or Charter on Taxpayers' Rights can enhance the efficiency and effectiveness of tax systems and can also increase the tax morale of the European citizens.⁹

⁷ CFE, AOTCA, STEP, A Model Taxpayer Charter, 2016 (second edition)

⁸ European Commission, Guidelines for a European Taxpayers' Code (2016), available at https://ec.europa.eu/taxation_customs/sites/taxation/files/guidelines_for_a_model_for_a_european_taxpayers_code_en.pdf

⁹ For CFE's detailed view on the matter, please refer to the Opinion Statement CFE 1/2018 on the Importance of Taxpayers Rights, Codes and Charters on Tax Good Governance, available at

R&D & SME incentives

In respect of boosting productivity through well-designed Research & Development tax policies, CFE is supportive of such policies to the extent those are compliant with the Code of Conduct Group recommendations of 2014 and the OECD BEPS Action 5 recommendations on patent boxes and the (modified) nexus approach.

Similarly, any incentives, regardless of the form or character, need to be compliant with primary EU law provisions that prohibit State aid in order to avoid distortions of the level-playing field in the Single Market.

Additionally, although tax policy decisions should as little as possible distort the operation of the Single Market and level-playing field, CFE also believes there is merit in policy initiatives aimed at assisting start-ups and SMEs. This is particularly so in the context of a rapidly changing tax environment where the complexity and costs of tax compliance can hinder competition.

Tax administration

CFE supports modernisation of tax administrations to reduce compliance burden and costs for businesses. Tax systems are intrinsically complex and tax advisers make complex tax systems work. Tax administrations should be efficient, accessible and transparent. Efficient tax administration is an important pillar of the competitiveness index and is becoming more challenging for taxpayers and tax administrations alike, particularly in the context of the increased compliance required by initiatives such as Country-by-Country reporting, the anti-money laundering directives, and the EU DAC6 mandatory disclosure rules for intermediaries.

As acknowledged by the European Commission Working Paper on Tax Certainty, companies are now paying much closer attention to tax risk (i.e., the risk of being considered non-compliant when audited) than they did in the past.¹⁰ Still, tax inspections and audits may also give rise to uncertainty with a stricter enforcement of tax rules. To that end, CFE strongly supports the tax administration modernisation and digitalisation projects to the extent these contribute to simplified tax compliance.

CFE has long advocated for the establishment of binding instruments that set out clear and equally applicable rights and obligations for taxpayers vis-a-vis tax administrations, throughout the EU. Increasingly, taxpayers in different EU Member States are facing equal tax obligations but are not treated equally by tax administrations in terms of their rights in different Member States.¹¹

<https://taxadviserseurope.org/blog/portfolio-items/opinion-statement-the-importance-of-taxpayers-rights-codes-and-charters-on-tax-good-governance/>

¹⁰ European Commission Taxation Working Paper 67 of 2017, 'Tax Uncertainty: Economic Evidence & Policy Responses', page 8

¹¹ Model Taxpayers' Charter (*supra*, at footnote 5)

As a means of providing advance certainty for taxpayers by tax administration, CFE is supportive of any programmes that establish such protection for taxpayers. We support both cooperative compliance programmes and tax ruling practices that comply with the OECD and the EU tax good governance standards and primary EU law rules.¹² Equally, cooperative compliance was recently endorsed by the IMF/OECD, on the basis that “cooperative compliance programs could reduce uncertainty for low risk companies, assist tax administrations to better focus their resources and promote a culture of greater trust”.¹³

In the same vein, where tax administrations provide tax rulings and Advance Pricing Agreements (APAs) these have proved to be an effective tool for the prevention of tax-related disputes, especially with respect to transfer pricing issues. They provide the taxpayer with advance knowledge of the tax treatment of particular transactions and therefore allow certainty for taxpayers in planning for the future, and also prevent the risk of subsequent disputes. The CFE calls upon the European Commission to consider harmonising measures that would outline an EU framework of tax rulings. All Member States should be required to establish simple and effective procedures for the conclusion of bilateral/multilateral APAs and/or confirmative tax rulings.¹⁴

Such a coordination of national procedures would benefit investment and competitiveness by providing clarity and a more predictable tax environment, as well as simplifying the rules applicable in the EU Single Market.

Tax Competition and Social Welfare

When considering the ‘pros and cons’ of tax competition and how it affects particular countries, it needs to be specified whether the matter under scrutiny concerns tax competition between EU Member States or tax competition between the EU Single Market and the rest of the world. As discussed *supra*, CFE acknowledges the fiscal sovereignty of Member States and their liberty to design tax policies fit for their social and economic systems, to the extent these are compliant with primary EU law (fundamental freedoms and State aid rules) and the secondary EU law that concerns harmonised areas of taxation (VAT, the DAC framework and the corporate tax directives that affect the functioning of the Single Market).

¹² For example, in spite of the challenges, the cooperative compliance programme of the Dutch tax administration has changed the relationship between the tax services and the companies from “adversarial ‘them and us’ relationship, to a stronger one characterised by cooperation”, see Dennis De Widt, *Dutch Horizontal Monitoring: The Handicap of a Head Start*. Umeå Universitet, 2017. See also Lotta Björklund Larsen et al. “Nordic Experiences of Co-Operative Compliance Programmes: Comparisons and Recommendations.” (2018) and OECD, *Co-operative Compliance: A Framework: From Enhanced Relationship to Co-operative Compliance*, 2013, available at: <http://www.oecd.org/tax/administration/co-operative-compliance.htm>.

¹³ IMF/OECD Report for the G20 Finance Ministers March (2017)

¹⁴ The first multilateral European Advance Pricing Agreement (APA) was concluded on 8 April 2004 by *Airbus Industrie* and the tax administrations of France, Germany, the United Kingdom and Spain. More on the benefits of the tax rulings: Carlo Romano, *Advance tax rulings and principles of law: towards a European tax rulings system?*. Vol. 4. IBFD, 2002.

In CFE's view, the absence of certain tax competition could lead to excessive taxation. Similarly, the longer-term tax competition within the framework elaborated *supra* would not necessarily lead to lower public revenues. Such policies of course need to be carefully balanced in order to protect the social welfare in each of the EU Member States whilst maintaining taxable revenues. Under no circumstances should tax competition be harmful to the extent it adversely affects the supply of public goods.

Conversely, tax policy choices between Member States (and within Member States) should be able to support quality healthcare, security, public safety, education and infrastructure, as basic pillars of the social model underpinning the European Union.

Is it good tax policy to keep reducing rates/ reducing cross-border barriers?

Admittedly, tax competition over mobile and easily shifted profit has resulted in downward trends in statutory tax rates, offset by broadening of the tax base, which enables countries to maintain their marginal tax rates on capital.¹⁵ These trends have been modified to a certain extent. While the declining trend in the average OECD corporate tax rate has gained renewed momentum in recent years, corporate tax rate reductions are less pronounced than before the financial crisis, with most countries engaging in a "race to the average", rather than a 'race to the bottom'.¹⁶ However, the interaction between expanding tax bases and tax rates must also be taken into account. This is particularly so if one considers that if a tax base is widened this can increase compliance issues and lead to instances of double taxation. In those cases, if the issue is not covered under double taxation treaties it poses a significant problem.

From our perspective, the competitiveness of tax systems cannot be assessed only by reference to tax rates or tax incentives but rather as an equilibrium of investment and growth-friendly tax policies that support the social goals of each Member State and the EU Single Market as a whole. CFE welcomes coordinated measures that reduce cross-border tax barriers on doing business and compliance burdens, through the introduction of instruments such as the Mini One-Stop-Shop (MOSS) (soon to become OSS). We also welcome any measures that ensure clear guidance and that are fit for purpose to allow taxpayers to do business in a simple, efficient and coherent manner throughout the EU.

Conclusion

Tax competition and competitiveness is a question of balance in tax policy in general. It is not only a matter of EU Member States following primary and secondary EU law, but all Inclusive Framework jurisdictions (in the case of BEPS initiatives) implementing and adhering

¹⁵ Michael Devereux, Rachel Griffith, and Alexander Klemm "Corporate income tax reforms and international tax competition." *Economic policy* 17.35 (2002) pages 449-495.

¹⁶ According to the OECD, the average corporate income tax rate across the OECD has dropped from 32.5% in 2000 to 23.9% in 2018. OECD (2018), *Tax Policy Reforms 2018: OECD and Selected Partner Economies*, OECD Publishing, Paris, <https://doi.org/10.1787/9789264304468-en>

to agreed initiatives. If this is not the case, issues of competitiveness arise. The EU is at the forefront of providing equilibrium in this respect.

Notwithstanding the above observations, CFE would also like to emphasise that it is not only the process of achieving harmony in tax competition and competitiveness which may, ultimately, boost economic growth and benefit EU citizens. It is also a question of balancing other policy areas from safety through to judicial systems, transport policy and a properly functioning financial market, to name but a few. Achieving economic growth which will benefit EU citizens can only be achieved if the system is balanced across these complex and interrelated areas.