30 October 2015

Interparliamentary Conference on Stability, Economic Coordination and Governance in the EU
Background notes

Chamber of Deputies of the Grand Duchy of Luxembourg
10 November 2015

Topic 3: Fair Tax Competition

The deepening of the Single Market and the establishment of the Economic and Monetary Union have increased cross-border activity of companies in the EU. In the meantime, Member States remained largely free to design their tax systems autonomously. This has lead to strong tax competition between Member States, which adapted their corporate tax rates in order to attract foreign direct investment.

The current mismatches between tax systems in the Economic and Monetary Union have allowed some multinational corporations to resort to tax planning in order to benefit from some EU Member States' tax specificities while fully respecting national, Single Market and international legislation. In some cases, this has increased the risk of tax avoidance through aggressive tax planning taking advantage of the technicalities of one or several tax systems.

The shifting of profits by some multinational corporations to jurisdictions allowing for more competitive tax rates raises interrogations on the fair contribution of mobile corporate groups to state budgets in times of fiscal consolidation and of higher tax burden on labour, which tends to be less mobile than capital.

Against this background, the Luxembourg Presidency has undertaken steps on improving fairness of tax competition. This commitment has led to significant progress on the transparency of tax rulings, a well-established practice in 26 Member States, which allows taxpayers to gain certainty on the enforcement of national and international provisions to their specific tax situation.

On 6 October 2015, under Luxembourg Presidency, the ECOFIN Council reached an agreement in record time on the Directive on the exchange of information on advance cross-border tax rulings, an initiative included in the March European Commission's Tax Transparency Package.

While the expectations of some stake-holders regarding the scope, the role of the European Commission, retroactive effects and the entry into force could not be met, in spite of intensive negotiations, the Directive strikes a workable compromise between the variety of views of Member States and delivers far-reaching improvements. It will require Member States to exchange information mandatorily and automatically on advance cross-border tax rulings, as well as advance pricing arrangements. The European Commission will be able to develop a secure central directory, available to all Member States, where the information exchanged would be stored.

Thanks to the adoption of this instrument increasing transparency on tax rulings and pricing arrangements, it has been established that as soon as one Member State issues an advance tax ruling or transfer pricing arrangement, any other Member State affected will be in a position to monitor the situation and the possible impact on its tax revenue, which will contribute to more fairness in corporate tax competition.

On 26 October 2015, the TAXE Special Committee of the European Parliament adopted the report on tax rulings and other measures similar in nature or effect, whose draft version calls "to eliminate mismatches – and refrain from creating further mismatches – between tax systems and harmful tax measures which create the conditions for massive tax avoidance by [multinational corporations] and tax base erosion within the internal market" and provides for recommendations. The TAXE report is the basis for the report with recommendations to the European Commission on bringing transparency, coordination and convergence to Corporate Tax policies in the Union, whose adoption is scheduled in the ECON Committee of the European Parliament later this year.

Significant progress has not only been made at the EU level but also at global level. On 8 October 2015, the OECD Base Erosion and Profit Shifting (BEPS) final package of measures was endorsed by the G20 Finance Ministers.

In his capacity as President of the ECOFIN Council, Luxembourg's Finance Minister, Mr Pierre Gramegna, welcomed the adoption of the BEPS rules and insisted on the importance of ensuring its global, coherent implementation within the spirit of ensuring a "level playing field".

Following the presentation to Finance Ministers, BEPS results will be delivered to G20 leaders on 15-16 November in Antalya. The focus will shift to putting in place an inclusive framework for monitoring BEPS and supporting implementation of the measures. The multilateral instrument capable of incorporating the tax treaty-related BEPS measures into the existing network of bilateral treaties will be open for signature by all interested countries in 2016.

Some points for discussion:

- How to strike the right balance between EU jurisdictions' freedom to design their tax systems and guaranteeing a fair taxation of profit in the Single Market?

- How could fairer tax competition in the EU be instrumental for investment and growth in the Single Market?

- Considering that the Treaty explicitly excludes tax harmonisation, which further institutional room for manoeuvre remains for improvement of tax competition and coordination, while guaranteeing the free movement of capital and freedom of establishment in the Single Market?

- Which steps should European and global policy-makers take to reach a wider "level playing field" and prevent further profit shifting?

- How to guarantee a more homogenous implementation at national level of tax legislation agreed at EU and global level?