European Economic and Social Committee

ECO/363
Completing EMU/
Taxation

Brussels, 10 December 2014

OPINION

of the
European Economic and Social Committee
on
Completing EMU – The role of taxation policy
(Own-initiative opinion)

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On 27 February 2014 the European Economic and Social Committee, acting under Rule 29(2) of its Rules of Procedure, decided to draw up an own-initiative opinion on

Completing EMU – The role of taxation policy.

The Section for Economic and Monetary Union and Economic and Social Cohesion, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 18 November 2014.

At its 503rd plenary session, held on 10 and 11 December 2014 (meeting of 10 December 2014), the European Economic and Social Committee adopted the following opinion by 164 votes to 53 with 11 abstentions.

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1. Conclusions and recommendations

1.1 The slower recovery in Europe than in the rest of the world is symptomatic of a degree of dysfunction that a deeper economic and monetary union must address. This opinion supports the process of deepening EMU, particularly in the euro area, from the aspect of the role of taxation. Progress in coordinating direct taxation has been and will continue to be hard to achieve because it remains in the competence of Member States and is rooted in the fabric of how each Member State has chosen over the centuries to finance its perceived necessary government expenditures. Any change to taxation must result in a more globally competitive and sustainable tax regime.

1.2 In order to allow the proper functioning of Economic and Monetary Union, the new legislature must lay the foundations for and move gradually towards a fiscal union capable of overcoming the huge diversity of national rules which hinder real integration and the creation of a single market and furthermore towards an enhanced common budget for the euro area.

1.3 Together with the ECB monetary pillar, in the medium term there must effectively also be a "common budget pillar" ensuring macroeconomic stabilisation within the EMU, particularly in the event of "asymmetric shocks".

1.4 Correcting the shortcomings and loopholes in taxation policy entails taking more ambitious steps within the euro area with a view to reducing and standardising the range of different taxes, extending tax bases, aligning tax rates more closely, and strengthening cooperation and information exchange mechanisms in order to combat fraud and evasion.

1.5 The new legislature must cooperate closely with the OECD and G20 in seeking a speedy solution to the global problem of base erosion and profit shifting. The OECD has made good progress in introducing a global model for taxing corporations which seeks to capture tax where the economic substance is located. It should form the basis for corporate taxation in the EU.

1.6 In order to move towards a deeper fiscal union, it is essential to continue budgetary surveillance under the Two-pack and to swiftly introduce an own resource fund in the euro area to reverse macroeconomic imbalances[1].

1.7 The Committee fully supports the continuation of the European Semester process, which should be reviewed to ensure its effectiveness. The individual Country Specific Recommendations could be a tool in moving to common ground.

1.8 The meagre common budget of barely 1% of EU GDP must be increased, especially in the euro area. Commission President Juncker's political guidelines "A New Start for Europe" call for the budget to be oriented further towards jobs, growth and competitiveness. The EESC supports this approach and emphasises the need to use the review of the Multiannual Financial Framework at the end of 2016 to lay the foundations for an increased budget to fulfil the proper functioning of the monetary union.

1.9 The Commission should follow up on its Communication of March 2013 "Towards a Deep and Genuine Economic and Monetary Union"[2] and introduce a Convergence and Competitiveness Instrument directed at contractual arrangements for Member States to undertake reforms with a national and European benefit to address imbalances which could not be undertaken without financial assistance. This fund should develop into an own resource fiscal capacity capable of giving temporary assistance in combating regional shocks[3].

1.10 The euro area budget should help the monetary union to function better, give fiscal backing to achieve a full banking union, and to offset asymmetric shocks. These functions were lacking when the economic crisis struck, dramatically exacerbating inequalities that required fiscal measures.

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1 The system is nevertheless overly rigid and unwieldy, and incapable of rapidly ensuring the flexibility needed to tackle immediate economic circumstances and come up with a euro area policy mix, in a situation where the Member States no longer have sufficient room for manoeuvre to launch recovery plans for their economies. The consequence is to generate powerful financial instability.

2 COM(2013) 165 final.

3 EESC opinion on *CCI/Major economic policy reforms*, OJ C 271, 19.9.2013 p. 45.

1.11 The EESC is aware of the complexity of the issue, and proposes a raft of measures to be adopted gradually, in keeping with the objectives set out in the European treaties[4]:

Short-term (6 to 18 months):

- Create a "Common Consolidated Corporate Tax Base" in the EU[5], in line with the Committee's previous positions[6] and with a fairer setting of parameters than in the current Commission proposal[7] The progress achieved by the OECD will also have to be considered.

- Respond to global developments at OECD and G20 level on base erosion and profit shifting (BEPS) to ensure that tax regimes are transparent and do not give unfair tax concessions and urgently eliminate practices used in the Member States to grant selected corporations special tax privileges.

- Seek effective agreements in the euro area to extend the planned financial transaction tax beyond the eleven Member States which support it.

- Involve citizens in combating the black economy, tax evasion and tax fraud by encouraging the private sector to reinforce instruments such as service vouchers, forms of electronic payment that leave a trace and cooperation with the authorities to these ends.

- Improve administrative cooperation beyond the current VAT network and database, using enhanced cooperation, in four areas:

    i) Strengthen the Eurofisc platform[8] as an embryonic EU agency acting as a VAT clearing house and tackling tax fraud that is beginning to operate in the euro area, in order to complete the information chain for national treasuries, thus putting an end to "carousel fraud"[9].
    ii) Strengthen the 2011 Mutual Assistance Directive[10] as a legal basis throughout the EU, with some of its content, if necessary, taking the form of a regulation.

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4 See Articles 113 and 115 TFEU in particular.

5 See the ECO-relevant highlights from the *Political Guidelines for the next European Commission*, presented to the European Parliament by Jean-Claude Juncker. See also Juncker: *A New Start for Europe: My Agenda (...)*, p. 6.

6 EESC opinion on *CCCTB*, OJ C 24, 28.1.2012, p. 63.

7 COM(2011) 121 final.

8 www.eurofisc.eu.

9 Fictitious sales in the State of final consumption causing potentially unlimited losses for national treasuries.

10 Directive 2011/16/EU.

iii) The Committee urges the Commission to implement its proposal contained in the Action plan for Fighting Fiscal Fraud and Fiscal evasion to blacklist jurisdictions that act as tax havens, in disregard of good governance in tax matters and calls for common criteria to be established at EU level for identifying such jurisdictions so as to prevent this being applied unevenly. The Committee urges DG Competition to fully investigate any unfair tax agreements reached by MS and individual companies. The use and location of businesses in these territories should moreover be specifically mentioned in the Corporate Social Responsibility reports of companies quoted on stock exchanges.

iv) Set up a European body for tax simplification on the basis of previous experience in the Member States.

Medium-term (18 months to 5 years):

- On corporate taxation: In the spirit of the "monetary snake" of the 1980s and preparing the ground for a Treaty change, create a "tax snake" in the euro area consisting of effective minimum and maximum rates, so as to progressively harmonise them.

- Achieve specific fiscal capacity in the euro area[11], through income based on the previously mentioned tax on financial transactions and four others: consumption of non-renewable energies (limited to those that have registered price falls in recent years), a temporary levy on balance of payments surpluses of more than 6% of GDP[12], emission of joint bonds and a share of seigniorage income from issuing currency.

- Set up an authority in the euro area to coordinate the Member States in collecting these six taxes and in checking, inspecting and distributing revenue.

- Thereby establish an additional, federal budget in the euro area, providing for common unemployment insurance, cohesion policies and sustainable investment linked to the green economy.

- Amend the current fiscal decision-making model in the euro area, bringing in a qualified majority system. The Committee recognises that this would require a contentious treaty change.

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11 See EESC opinions on *Fiscal policy: growth and fiscal adjustments*, OJ C 248, 25.8.2011, p. 8 and on *Completing EMU - the next European legislature* and the *Blueprint for a deep and genuine economic and monetary union*, COM(2012) 777 final/2, point 3.

12 See EESC opinion on *Completing EMU - the next European legislature*.

2. EMU and its fiscal and taxation framework

2.1 Framework

2.1.1 The 28 EU Member States have set out on the path of integration, with stronger commitments and obligations within the euro area, guided by monetary union, now strengthened by an evolving banking union and the Intergovernmental Treaty on Stability, Coordination and Governance in the Economic and Monetary Union.

2.1.2 Taxation policy currently covers more than 600 distinct taxes. These provide the bulk of revenue, equivalent in total (taxes and social security contributions) to 39.4% of the Member States' GDP[13] and 40.4% in the euro area. There is a need to bring more coordination to the tax policies of Member States in the euro area to complement the single monetary policy of the ECB.

2.1.3 Making progress towards fiscal union, in the case of the euro area, would mean being able to rely on its own resources and make a start on effectively supporting important structural reforms in the economies in difficulty as well as to implement solidarity-based and redistribution policies which are essential to offset asymmetric shocks.

2.1.4 Compared to other advanced economies the EU, and the euro area in particular, has lower rates of growth (GDP) and employment. Most economic integration theories suggest models that comprise both monetary and fiscal union. The TFEU however imposes decision-making by unanimity in matters of taxation, making the adoption of legislation far more difficult.

2.1.5 The euro area's lack of macroeconomic efficiency can be attributed in part to the mismatch between fiscal policy, which is highly decentralised and within the ambit of the Member States, and monetary policy, which in the euro area countries is increasingly centralised under the authority of the ECB.

2.1.6 The ECB's limited powers prevent it from financing budget deficits by creating money. This might be positive for price stability and the value of the currency, but not for growth, employment and other objectives. There has been little progress in the EU towards fiscal union since monetary union. This makes it difficult to ensure mobility of labour and capital, and to respond to the crisis and asymmetric shocks.

2.2 Revenue and expenditure trends and problems

2.2.1 The minimal tax policy coordination applied to date is barely sufficient to prevent the distortion of competition between Member States and to mitigate the competitive race to the

13 2012 data published by Eurostat (92/2014) on 16 June 2014.

bottom which mainly affects nominal and effective rates of corporate and personal income taxes; this could have a positive impact if handled in a concerted way between the Member States. Unfortunately, for the moment this is a negative-sum game in which the winners are income on capital and highly mobile labour, with the great majority losing out.

2.2.2 Although fiscal integration requires a system of transfers and an authority, the EU budget is limited to 1% of GDP. Net transfers make up a minimal part of these resources, despite the objectives set out in the **Europe 2020 strategy** and the **Europe 2030 project**.

2.2.3 The roadmap towards a fully-fledged Economic and Monetary Union, drawn up in 2012[14], proposes moving in the medium term towards an economic, monetary and fiscal union, by means, among other things, of more specific initiatives, while in the short term it is planned to strengthen fiscal and economic governance (Six Pack, Fiscal Pact and Two Pack); the European Semester and its Recommendations; and lastly the Intergovernmental Treaty on Stability, Coordination and Governance in the EMU signed by 25 countries, outside the TFEU. The system is one-way, rigid and unwieldy, failing to provide the flexibility needed to tackle the immediate economic situation in a crisis situation and to introduce a euro area policy mix.

2.2.4 In fact, it is remarkable that so far only measures on the expenditure side have been launched while completely neglecting the revenue side of a fiscal union.

2.2.5 In addition to the absence of a fiscal supervisory authority, the troika acted in a politicised way, imposing austerity policies on countries which required aid, drawing criticism from the European Parliament[15] and the EESC for their lack of effectiveness and transparency.

2.2.6 The EESC supports the Commission President, Mr Juncker's, political guidelines "A New Start for Europe" that call for the EU to replace the "troika" with a more democratically legitimate and more accountable structure based around the EU institutions, with enhanced parliamentary control both at EU and national level.

2.2.7 Meanwhile, policies of fiscal devaluation pursued in some of the most vulnerable of the euro area countries resulted in damage to the European social model[16] rather than increased competitiveness, as the reduction of the burden on labour as a factor of production had scarcely any impact in terms of improved growth, employment and the debt situation, leading to unnecessary loss of tax income. In some Member States however, correcting some imbalances seems to begin to show beneficial effects.

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14 COM(2012) 777 final/2.

15 Alejandro Cercas, Report: PE528.091v02-00.

16 *Eurofound Yearbook*, 2013.

3. Comments

3.1 Relevance of the taxation of financial and digital services

3.1.1 The difficulty of making progress on integration in the field of taxation has been illustrated in two areas: financial transactions and transactions in the digital economy; the Commission must give a rapid response, in line with investigations by the Competition DG, the recommendations of the Commission Expert Group on Taxation of the Digital Economy[17] and the OECD's first proposals[18] for a coordinated international approach to combat tax avoidance by multinational enterprises, under the OECD/G20 Base Erosion and Profit Shifting Project (designed to create a single set of international tax rules to end the erosion of tax bases and the artificial shifting of profits to jurisdictions to avoid paying tax).

3.1.2 As the planned financial transaction tax applying to the whole EU has so far progressed no further than the February 2013 Directive on enhanced cooperation involving only 11 euro area countries[19], its application should be extended at least to the euro area (overcoming the lack of progress of the last months).

3.1.3 The EESC welcomes the proposal to amend the Directive on Taxation of savings income[20] to improve the quality of information and ensure more effective prevention of tax evasion.

3.2 Tax structures: bases, rates and exemptions

3.2.1 Every year the EU loses far more tax income than the United States or other countries where there is less of a black economy, tax or employment fraud and tax evasion[21]. In order to prevent dysfunctions such as tax havens, the extensive and complex tax structures require greater homogeneity, simplification and harmonisation between countries. The process should begin with the euro area, coordinated by the Commission and the Euro-group, using a European simplification body of the kind that already exists in some countries[22].

3.2.2 The EESC also believes that convergence of tax policies should be a priority in the framework of the European Semester (taking advantage of some Country Specific

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17 See the Report - On 22 October 2013, the Commission adopted a Decision setting up the Expert Group, which that same year defined the scope of its work and its Roadmap. Its opinion was published on 28 May 2014.

18 http://www.oecd.org/tax/beps-2014-deliverables.htm.

19 COM(2013) 71 final, 2013/0045 (CNS): Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia.

20 Taxation of Savings Income - European Commission.

21 Friedrich Schneider, "Shadow Economies and Corruption all over the World: Empirical Results for 1999 to 2003" , in: special issue of the *International Journal of Social Economics* (IJSE), Series 1, Vol. 35, No. 9, 2008.

22 For example The Office of Tax Simplification, HM Treasury, part of the Government of the United Kingdom.

Recommendations), since this is the forum for coordinating economic policy efforts between the Member States in order to achieve the Europe 2020 objectives too, with the help of the other policies.

3.2.3 The EESC calls for a fairer and more effective system, with tax reform and harmonisation geared towards transparency, broadening the tax base and prevention of aggressive tax avoidance, thus enabling rates of tax to fall and the burden to be redistributed.

3.2.4 The EESC recommends limiting the system of exemptions, depending on the nature of each tax by means of rigorous economic and social cost-benefit analyses, in line with the international principle of tax expenditures, which has been consolidated since 1968, and considering that during the last five crisis years tax-benefit systems were able to contain a considerable part of the increase in market inequality in most EU Member States, according to Commission studies[23].

3.2.5 The EESC urges the EU to take a more active part, through euro area representatives, in discussions on coordinating its harmonisation and simplification work with the OECD[24], the IMF[25] and the G-20[26], beginning with transfer prices, fraud and the black economy and, above all, problems of fairness in the distribution of the burden of taxation.

3.2.6 The EESC considers that the BEPS (Base Erosion and Profit Shifting) action plan[27] will be essential to combating tax evasion and aggressive tax planning at global level. It therefore encourages the G20, the OECD and all the Member States to develop it, creating an embryonic EU agency acting as a VAT clearing house and tackling tax fraud, in order to eradicate the problem of "carousel fraud"[28] in intra-Community transactions, which is more damaging than the black economy itself.

3.2.7 Lastly, given that tax exemptions and reliefs result in effective tax rates that are far lower than the nominal ones, they should be coordinated with European objectives on employment, productive investment, business competitiveness and social inclusion, as well as with the Union policies which shape the European social model.

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23 European Commission Research note 02/2013 "The effect of tax-benefit changes on income distribution in EU countries since the beginning of the economic crisis".

24 OECD project on Base Erosion and Profit Shifting (BEPS).

25 Role of the IMF in international taxation.

26 https://www.g20.org/sites/default/files/g20_resources/library/Saint_Petersburg_Declaration_ENG.pdf.

27 Centre for Tax Policy and Administration - OECD.

28 Fictitious sales in the State of final consumption causing potentially unlimited losses for national treasuries.

3.3 **Taxation of companies**

3.3.1 The EESC calls for priority to be given to harmonisation of company taxes to progress towards a coherent budgetary and **fiscal** union[29] so that SMEs do not pay the highest effective tax rates. The EESC also considers highly reprehensible the practice of some Member States of granting special, unpublicised tax reliefs to selected multinational corporations; in this connection it calls on the European Commission to do everything possible to eliminate such practices. This state of affairs leads to a distortion of competition that is incompatible with the whole purpose of the single market.

3.3.1.1 One of the first and most important levers should focus on creating a "common consolidated tax base". This position was officially put forward by the Committee in 2006[30] and confirmed subsequently[31]. As long ago as 1992 the **Ruding Report** pointed to the need for common rules to define the tax base **starting with minimum and maximum rates**.

3.3.1.2 In the spirit of the "monetary snake" designed to resist currency fluctuations before the introduction of the euro, the Committee suggests that the authorities responsible are encouraged to cooperate establishing a ceiling and a floor for corporate tax. Exemptions which are less conducive to increasing employment or productivity should also be eliminated in a coordinated way.

3.3.2 The EESC welcomes the proposal for a directive on parent companies and subsidiaries in different Member States, one of 34 measures included in the *Action Plan to strengthen the fight against tax fraud and tax evasion*[32] presented by the Commission at the end of 2012. It would however prefer this to be implemented by means of a regulation.

3.3.3 Regarding intra-EU trade in goods and services, there has been more progress on the harmonisation of VAT, where the harmonisation of tax bases has improved but there are still major differences in rates of tax.

3.3.4 Finally, in view of their strategic character, the EESC recommends that priority be given to tax incentives for research and development[33].

3.3.5 Care should be taken to ensure that any measures envisaged do not harm the competitiveness of European companies.

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29 See EESC declaration *An action plan for Europe*, adopted at the plenary session of 29 and 30 April 2014. See also EESC opinion *Smart fiscal policy consolidation strategies — challenges of identifying growth drivers for Europe*, OJ C 248, 25.8.2011, p. 8.

30 EESC opinion on *Creation of a common consolidated corporate tax base in the EU*, OJ C 88, 11.4.2006, p. 48.

31 EESC opinion on *Common Consolidated Corporate Tax Base*, OJ C 24, 28.1.2012, p. 63.

32 COM(2012) 722 final.

33 Placing taxation at the service of research and development.

3.4 Taxation of persons and households

3.4.1 Natural persons are subject to both direct and indirect taxation. It has to be borne in mind that indirect taxes are regressive by nature and especially upward harmonisation of indirect taxation is regressive and can have a drastic effect on the lowest-income sectors of the population without countervailing income supplements.

3.4.2 Harmonisation of the direct taxation of natural persons is limited to specific cases and the tax burden has ceased to converge.

3.4.3 At least in the euro area, the number of chapters in personal income tax law and the cost of social security contributions should be revised in order to prevent social dumping, make the "tax wedge" on labour more uniform and thus facilitate its mobility[34]. The progressive nature of such taxation should be extended to income from capital and the wealth by which it is generated, once again making property, inheritance and gift taxes an instrument of control. Furthermore these kinds of taxes have less dampening effect on demand than taxes on labour.

3.4.4 The need to place more emphasis on investment rather than consumption makes it important to harmonise and set up *convergence snakes* for the taxation of income on savings[35] and dividends received by natural persons and cross-border pension benefits.

3.4.5 The EESC supports the search by the Commission for ways to make tax structures more growth-friendly, and to look at the role that taxation can play in meeting consolidation needs in the context of broadening tax bases like housing taxation. So the recommendations made by the European Commission to Member States in the European Semester were to make further use of recurrent taxes on property, for the purpose of consolidation or as part of a tax shift away from labour[36].

3.4.6 The EESC also proposes that additional measures be adopted to harmonise environmental taxes, taking the Commission's 2030 Framework for Climate and Energy Policies as a starting point.

3.4.7 The public will help to combat the serious problem of tax and labour fraud if there are incentives to do so. Instruments like the service voucher or tax exemptions and relief for other personal support services, which combine the objectives of promoting social welfare and bringing the black economy into the open, should be strengthened.

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34 Eurogroup, statement 8 July 2014, *Structural reform agenda - thematic discussions on growth and jobs - Reduction of the tax wedge*.

35 http://europa.eu/legislation_summaries/taxation/l31050_en.htm.

36 European Commission (2014), *Tax reforms in EU Member States, page 112*.

3.4.8 In order to combat the informal economy, the EESC proposes that tax incentives be introduced for the use of forms of payment, such as cards and mobile phones, which leave a trace and encourage financial and digital inclusion, by means of harmonised tax reliefs or exemptions for individuals and companies who reduce their use of cash.

3.4.9 Similarly, public cooperation could be stepped up by means of economic incentives for detecting possibly fraudulent transactions, modelled on what is normal practice in the US.

3.5 Territorial taxation (regions, States and EU)

3.5.1 The great diversity of taxation encourages fraud, corruption and the black economy. The EESC calls on the Member States of the euro area to take on greater powers in the four major areas of taxation: direct taxation of natural and legal persons (including taxation of capital income and property as well as other wealth related taxes), and indirect taxation in the form of VAT and special taxes.

3.5.2 Making progress on fiscal governance inevitably means a gradual hand-over of sovereignty by the Member States. In this way, tax collection could continue to be predominantly a matter for States, with checks, inspections and distribution of revenue being handled between the Union and the States. To this end, the EESC proposes the establishment of an EU tax authority, beginning with the euro area.

3.5.3 In keeping with the principle of subsidiarity, local taxes must be respected, but the EESC recommends launching a campaign of simplification by reducing, grouping and standardising many existing taxes.

3.6 External dimension and link with public policies

3.6.1 A supranational fiscal policy[37] would be an effective instrument for achieving the aims of the Treaties, particularly cohesion and sustainability policies.

3.6.2 The EESC calls for the establishment of an additional federal budget, at least in the euro area, which could collect taxes and gradually take on those policies which can be better implemented in common: unemployment insurance linked to active labour market policies[38], research and development, defence, a common mechanism to compensate for the debt interest burden[39], etc.

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37 Stefan Collignon, *Taking European integration seriously*.

38 See EESC opinions on *Completing EMU - the next European legislature* and on *For a social dimension of European Economic and Monetary*, OJ C 271, 19.9.2013, p.1.

39 See EESC opinion on *Restarting growth*, OJ C 143, 22.5.2012, p.10.

3.6.3 Lastly, the EESC strongly supports the initiatives taken by the OECD and G-20 in the field of international tax cooperation and to combat tax fraud, and urges that automatic exchange of tax information become the international standard.

Brussels, 10 December2014

The President
of the
European Economic and Social Committee

Henri Malosse

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N.B.: Appendix overleaf.

APPENDIX
to the
OPINION
of the European Economic and Social Committee

The following amendment, which received at least a quarter of the votes cast, was rejected during the discussions (Rule 54(3) of the Rules of Procedure):

Point 1.4

Amend as follows:

> *Correcting the shortcomings and loopholes in taxation policy entails taking more ambitious steps within the euro area with a view to reducing and standardising the range of different taxes, extending tax bases, aligning tax rates more closely, and strengthening cooperation and information exchange mechanisms in order to combat fraud and evasion.* <u>*At the same time, it should be borne in mind that the overall tax burden in the euro area should not exceed the tax burden in neighbouring countries.*</u>

Reason

Since the opinion includes proposals for new taxes, it is important that the overall tax burden in the euro area not exceed the tax burden in neighbouring countries – otherwise this (high tax burden) may adversely affect the euro area, prompting more businesses to relocate and workers to emigrate.

Result of the vote:

For:	80
Against:	129
Abstentions:	17

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