EU Parliament – FISC Subcommittee on Tax Matters

Hearing of 26.1.2021 – "The Impact of Brexit on the Level-Playing Field in the Area of Taxation"

Panel I - The post-Brexit fight against tax evasion and avoidance. The UK, its overseas territories and crown dependencies

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Distinguished Members of the European Parliament and of the FISC Subcommittee,

Ladies and gentlemen,

I am very grateful for the invitation and honoured to present my views in this hearing at such an important time of the history of European relations. As a European, I regret the departure of the United Kingdom from the European Union. As a lawyer, I respect the will of the British people.

The focus of my presentation is on the fight against tax avoidance and evasion. For this purpose, I shall mostly analyse selected rules of the EU-UK Trade Agreement. However, I will also take into account the impact of the UK Withdrawal Agreement and EU law on the relations of the EU with the UK, its overseas territories and crown dependencies.

Article FINPROV.1 indicates that the EU-UK Agreement does not apply to the crown dependencies, Gibraltar and the UK overseas territories for the issues falling within the scope of my presentation. I shall therefore separately address such issues.

From a policy perspective, the signature of the EU-UK Trade Agreement is desirable due to the strong economic and trade ties. However, the enforcement of the agreement may be problematic in practice, especially on tax matters, due to the specific wording of its clauses and the absence of their direct effect, which reflects the purely international law nature of the agreement. The clause COMPROV.13, contained in Part One, Title II confirms this on matters of interpretation.

A limited number of clauses with direct effect are otherwise applicable to tax matters in the EU-UK relations, such as Art. 10 of the Ireland/Northern Ireland Protocol to the UK Withdrawal Agreement, which applies full State aid scrutiny.

Moreover, some clauses of the EU-UK Free Trade Agreement, such as the one contained in Article SSC.67 on the protection of individual rights, have a quasi-direct effect. However, even in such case legal remedies will be granted in accordance with domestic legal orders.

In the absence of clauses with direct effect on taxation, the enforcement of the EU-UK Free Trade Agreement will be in practice very problematic, except when the Parties decide to abide by the Agreement. It is submitted that divergent interpretation on tax matters might lead to endless disputes, not subject to dispute settlement under Article 5.3 of the EU-UK Free Trade Agreement.

Taking into account the WTO experience of disputes between the EU and the US on tax and subsidies, this is all very discouraging and might create problems when securing fair tax competition and fighting against tax avoidance and evasion in the relations with the UK.

Moreover, the EU-UK Trade Agreement creates less legal constraints than EU law and related measures do. A good example is the notion of subsidy under Article 3.4 of the EU-UK Free Trade Agreement, which requires "material effect [of a subsidy] on trade or investment". This is more specific than the one contained in the CETA, which essentially reflects WTO law. Moreover, this concept of subsidy is much narrower than that of measures that "distort or threaten to distort competition" under Article 107 TFEU and Article 23 (1) (iii) of the 1972 EU-Switzerland Free Trade Agreement.

Unlike in the UK Withdrawal Agreement, EU law is totally irrelevant for the interpretation and application of the EU-UK Free Trade Agreement, which does not aim at sharing parts of the EU Internal Market with the UK. Therefore, the latter agreement does not share the dynamic nature of EU law and the interpretation of its clauses does not require a *de facto* consistency with CJEU interpretation of the corresponding EU law provisions.

Another example can show the reasons why the UK may enjoy a competitive tax advantage over the EU and its Member States, but also over other countries, such as Canada and Switzerland, that have accepted more stringent conditions in their Free Trade Agreements with the EU.

The CJEU Gibraltar judgment on tax state aids shows that *de facto* selectivity prevents EU Member States from shaping tax systems in a way that allows the systematic exploitation of cross-border tax disparities. By contrast, Art. 5.1 of the EU-UK Free Trade Agreement only refers to good tax governance as established in the framework of international tax coordination conducted under the auspices of the OECD. This is not the same and may allow the UK to do what EU Member States (and Switzerland) are in fact not allowed to. This applies even more to UK crown dependencies and overseas territories, which fall out of the scope of the Free Trade Agreement.

An unfortunate conceptual and terminological mismatch in the EU-UK Free Trade Agreement may create further problems. The English version of Art. 3.1 (2) (b) refers to measures that fight "fraud or evasion". In the tax technical terminology this is a false friend for the French "*evasion et fraude fiscale*", and should have been instead worded in English as "avoidance and evasion". The latter, correct, wording is used in Article SERVIN.5.41 and in footnote 69 to the safeguard clause of Article EXC.2 of Title XII on Trade. Such footnote reserves the right of the Parties to apply measures that secure the "equitable or effective" imposition or collection of direct taxes, and is contained at page 234 of the Agreement.

This right is actually the key to approach the protection of the interest of the EU and its Member States in case the UK introduces measures that can foster aggressive tax planning, i.e. a harmful exploitation of cross-border tax disparities, and sparkle up a race to the bottom.

When approaching tax avoidance and evasion, the EU and its Member States must protect free movement of capital under Article 63 TFEU ff., which prevent discriminatory measures that disproportionately counter such phenomena. However, Article EXC.2 of the EU-UK Trade Agreement may justify the adoption of measures that secure effective taxation.

Since EU Member States have a more limited leeway to introduce preferential tax regimes than the UK, they should pursue the establishment of a minimum effective corporate tax rate that prevents the race to the bottom across the EU and also applies to relations with third countries.

This is in substance the so-called Pillar 2 of the OECD BEPS 2.0 Project, and, in particular, the so-called Franco-German proposal, also known as GLOBE. Should the OECD fail to achieve consensus on the introduction of this mechanism at the global level, the EU and its Member States could consider this as an effective way to prevent that harmful tax competition involving the UK may undermine the effectiveness in the imposition or collection of direct taxes within the Internal Market.

Such grounds are in line with the rule of reason to preserve the balanced allocation of taxing powers, which the CJEU acknowledges as justification to restrict the exercise of fundamental freedoms.

This secures compliance with primary EU law without requiring the countering of the actual abusive practices. Moreover, it achieves an effective approach to tax avoidance schemes involving the UK, its crown dependencies and overseas territories. Also, it secures a fair and transparent framework for tax competition in the post-Brexit scenario despite the absence of specific provisions with direct effect that achieve this goal in the EU-UK Free Trade Agreement.

I thank you for your attention and am available to answer the queries that may arise in the framework of the discussion with the members of the Fisc Subcommittee on Tax Matters.