DIRECT TAXATION: PERSONAL AND COMPANY TAXATION

The field of direct taxation is not directly governed by European Union rules. Nevertheless, a number of directives and the case law of the Court of Justice of the European Union (CJEU) establish harmonised standards for taxation of companies and private individuals. Moreover, actions have been taken to prevent tax evasion and double taxation.

LEGAL BASIS

The EU Treaty makes no explicit provision for legislative competences in the area of direct taxation. Legislation on the taxation of companies has usually been based on Article 115 of the Treaty on the Functioning of the European Union (TFEU), which authorises the Union to adopt directives on the approximation of laws, regulations or administrative provisions of the Member States which directly affect the internal market; these require unanimity and the consultation procedure.

Article 65 TFEU (free movement of capital) allows Member States to distinguish between taxpayers who are not in the same situation with regard to their place of residence or with regard to the place where their capital is invested. However, in 1995, the CJEU ruled (in Case C-279/93) that Article 45 TFEU is directly applicable in the field of taxation and social security: that article stipulates that freedom of movement for workers entails 'the abolition of any discrimination based on nationality [...] as regards employment, remuneration and other conditions of work and employment'. Articles 110-113 TFEU require Member States to enter into negotiations on the abolition of double taxation within the EU. Article 55 TFEU forbids discrimination between the nationals of Member States as regards participation in the capital of companies. Most of the arrangements in the field of direct taxation, however, lie outside the framework of EU law. An extensive network of bilateral tax treaties involving both Member States and third countries covers the taxation of cross-border income flows.

OBJECTIVES

Two specific objectives are the prevention of tax evasion and the elimination of double taxation. In general terms, a degree of harmonisation of company taxation is justified in order to prevent distortions of competition (in particular in connection with investment decisions), to prevent 'tax competition' and to reduce the scope for manipulative accounting.

RESULTS

A. Company taxation

Proposals to harmonise corporation tax have been under discussion for several decades (1962: Neumark report; 1970: Van den Tempel report; 1975: proposal for a directive on the alignment of tax rates between 45% and 55%). In 1980, the Commission stated that the attempt at harmonisation was probably doomed to failure (COM(80)0139), and concentrated on measures to complete the internal market: in the 'Guidelines on corporation tax' of 1990 (SEC(90)0601), three proposals were adopted, namely the Merger Directive (90/434/EEC — now 2009/133/EC), the Parent Companies and Subsidiaries Directive (90/435/EEC — now 2011/96/EU), and the Arbitration Procedure Convention (90/436/EEC). The fate of the 1991 proposal for a directive on a common system of taxation applicable to interest and royalty payments made between parent companies and subsidiaries in different Member States illustrates the often protracted nature of the negotiations with the Member States: despite being revised and receiving a favourable opinion from Parliament, the Commission withdrew it as a result of the failure to reach agreement in the Council. A new version appeared in 1998 as part of the 'Monti package' and was subsequently adopted as Directive 2003/49/EC.

In 1996, the Commission launched a new approach to taxation. In the field of company taxation, the main result was the Code of Conduct for Business Taxation, adopted as a Council resolution in 1998. The Council also established a Code of Conduct Group (known as the 'Primarolo Group') to examine cases of unfair business taxation. In 2001, the Commission prepared 'an analytical study of company taxation in the European Community' (SEC(2001)1681). The accompanying Commission communication (COM(2001)0582) noted that the main problem faced by companies was that they had to adapt to different national regulations in the internal market. In 2004, a working group was set up, and the results of its work were incorporated into a Commission proposal. The proposed 'common consolidated corporate tax base' (CCCTB) would mean that companies benefit from a system with a central contact point to which they could submit their tax refund claims. They would also be able to consolidate all their profits and losses made in the EU. Member States would retain full responsibility for setting their own rates of corporate tax. In April 2012, the European Parliament adopted its legislative resolution on this proposal. In June 2015, to give fresh impetus to the negotiations in the Council, the Commission came up with a strategy for re-launching the CCCTB proposal in 2016. The Commission opted for a two-step process, separating the common base and consolidation elements, with two interconnected legislative proposals: on a common corporate tax base (CCTB) and on a common consolidated corporate tax base (CCCTB). While it would call for the introduction of the CCCTB to be compulsory, there would be provisions for phasing it in. The revamped proposal, adjusted to take account of work by the Organisation for Economic Co-operation and Development (OECD), could also address tax avoidance by closing regulatory gaps between the national systems and thus putting a stop to common tax avoidance arrangements.

In September 2023, the Commission adopted a proposal entitled 'Business in Europe: Framework for Income Taxation (or BEFIT)', which will provide a single corporate tax rulebook for the EU, based on apportionment and a common tax base. The proposal will replace the pending proposal for a CCCTB. It will reduce compliance costs for businesses that operate in more than one Member State and make it easier for national tax authorities to determine which taxes are due. After being adopted by the Council, the proposal should come into force on 1 July 2028. Also in September 2023, the Commission published two other proposals for Council directives: one on transfer pricing and one for a head office tax system for small and medium-sized enterprises. After being adopted by the Council, these two proposals should enter into force in January 2026.

B. Fair taxation, tax transparency and measures to combat tax avoidance and harmful tax competition

In the course of the 2008 financial crisis, attention turned to combating tax avoidance and to the equitable taxation of companies. Increased transparency is seen as one of the ways of achieving this, as evidenced in the Tax Transparency Package of March 2015, which included the Council Directive on the automatic exchange of information on tax rulings between Member States (Directive (EU) 2015/2376) and the communication on tax transparency to fight tax evasion and avoidance. In 2015, the Commission adopted an action plan for a fair and efficient corporate tax system in the European Union, with provisions for reforming the corporate tax framework in order to combat tax abuses, ensure sustainable revenue and support an improved environment for business in the internal market. In January 2016, the Commission proposed a package of measures to combat tax avoidance, which included a proposal for a Council directive to combat tax avoidance practices with an immediate impact on the functioning of the internal market (adopted in July 2016). In April 2016, the Commission proposed an amendment to Directive 2013/34/EU as regards disclosure of income tax information by certain undertakings and branches. The proposal requires multinational enterprises to disclose publicly certain parts of the information submitted to the tax authorities. In June 2017, the Commission proposed new transparency rules for intermediaries (e.g. consulting firms, banks, lawyers, tax advisers) that design or sell potentially harmful tax schemes, following a request for a legislative proposal in Parliament's resolution (TAXE 2). This proposal was then adopted by the Council in May 2018. In December 2017, the Council published the first ever EU list of non-cooperative jurisdictions. The list is updated on a regular basis.

The transition to a digital economy has led to a growing disconnect between where value is created and where tax is paid. Discussions on modernising international corporate taxation started a decade ago in the G20, and have been supported by the OECD. On 8 October 2021, members of the OECD/G20 Inclusive Framework on BEPS (base erosion and profit shifting) agreed on the Two-Pillar solution, which is an approach to addressing the tax challenges arising from the digitalisation of the economy. The Two-Pillar solution will ensure that largest and most profitable multinational enterprises will be subject to a minimum tax rate of 15% and re-allocate profits to countries worldwide in the following way:

Pillar 1 is the place of taxation where value is created and where customers are located, regardless of a physical presence in the country. For this, the Commission proposed on 22 December 2021 'the next generation of EU own resources', which includes an own resource equivalent to 15% of the share of the residual profits of in-scope companies, which are to be reallocated to EU Member States. The proposals do not include extensive details, not least because the OECD is still working on practical implementation aspects of the pillar design. Very recently, however, in October 2023, the OECD published the Multilateral Convention (MLC) to Implement Amount A of Pillar 1. This reflects the current consensus achieved among members of the Inclusive Framework (IF). Pillar 1 needs to be signed and will only enter into force when at least 30 jurisdictions accounting for a critical mass of in-scope multinationals ratify the MLC.

Pillar 2 is a global 15% minimum tax, and for this the Commission published a proposal for a Council directive concerning a global minimum level of taxation for multinational groups on 22 December 2021.

Commissioner Paolo Gentiloni commented that the draft proposals are 'fully consistent with the final version of the OECD's model rules which set out the details for the application of the new framework. That means no gold plating; no departure from the international agreement [...]'.

The EU adopted its Pillar 2 Directive at the end of 2022 and Member States are obliged to implement the rules by 31 December 2023. The adoption of the directive means that minimum tax rules have become part of EU law.

C. Personal taxation

1. Income tax

The taxation of individuals who work in, or draw a pension from, one Member State but live or have dependent relatives in another has always been a contentious issue. With bilateral agreements, double taxation can generally be avoided, but this has not resolved issues such as the application of different forms of tax relief available in the country of residence to income in the country of employment. In order to ensure equal treatment between residents and non-residents, the Commission put forward a proposal for a directive on the harmonisation of income tax provisions with respect to freedom of movement (COM(1979)0737), on the basis of which taxation in the country of residence would have been the rule. Following its rejection by the Council, this proposal was withdrawn, and the Commission merely issued a recommendation on the principles that should apply to the tax treatment of non-residents' income. In addition, proceedings were brought against some Member States for discrimination against non-national employees. In 1993, the CJEU ruled (in Case C-112/91) that a Member State cannot treat non-nationals from another Member State less favourably in terms of the collection of direct taxes than it does its own nationals (see Case C-279/93). In general, integration in the field of personal direct taxation can be said to have been furthered more by CJEU rulings than by legislative proposals. In October 2017, the Council adopted a directive (Directive (EU) 2017/1852) aiming to improve existing double taxation dispute resolution mechanisms in the EU.

2. Taxation of bank and other interest paid to non-residents

In principle, taxpayers are required to declare income from interest. In practice, the free movement of capital and banking secrecy have offered scope for tax evasion. Some Member States impose a withholding tax on interest income. In 1989, the Commission proposed the introduction of a common system of withholding tax on interest income, levied at the rate of 15%. This proposal was then withdrawn and replaced by a new one to ensure minimum effective taxation of savings income in the form of interest payments (with a tax rate of 20%). Following lengthy negotiations, a compromise was reached, and Council Directive 2003/48/EC on the taxation of interest income was adopted. It has since been replaced by the more far-reaching Directive 2014/107/EU, which, together with Directive 2011/16/EU, provides for comprehensive exchanges of information between tax authorities.

ROLE OF THE EUROPEAN PARLIAMENT

On tax proposals, Parliament's role is generally confined to the consultation procedure. Its resolutions have broadly supported all Commission proposals in the fields of both company and personal direct taxation, while advocating a widening of their scope. In addition, Parliament's role is to encourage the Commission to submit new legislative proposals for fairer, greener and more efficient taxation.

In its former 'annual tax reports' (the first of which was adopted in February 2012), Parliament dealt with issues of double taxation and combating aggressive tax policy, and advocated for a common approach to effectively tackling tax fraud and tax avoidance, as well as to providing an improved framework for the correct functioning of the single market.

As a follow-up to the work of the temporary Special Committees on Tax Rulings and Other Measures Similar in Nature or Effect, Parliament adopted two resolutions (TAXE and TAXE 2).

In 2016, following the 'Panama Papers' leak, Parliament established a Committee of Inquiry (PANA Committee) to investigate alleged contraventions and maladministration in the application of EU law in relation to money laundering, tax avoidance and tax evasion. In October 2017, the PANA Committee adopted its final inquiry report. In December 2017, Parliament adopted a recommendation to the Council and Commission following the work of the Committee of Inquiry.

With a somewhat expanded mandate, the Special Committee on Financial Crimes, Tax Evasion and Tax Avoidance (TAX3) was established by Parliament in March 2018. Following the work of the TAX3 Committee, Parliament adopted a resolution in March 2019.

Parliament's Subcommittee on Tax Matters (FISC) is a subcommittee of the Committee on Economic and Monetary Affairs (ECON). It was set up in September 2020 to continue Parliament's fight against tax avoidance begun in the previous parliamentary term. Its objectives are to promote fair taxation at the national, EU and global level. In the light of forthcoming challenges in promoting a sustainable economic recovery in line with the Green Deal, it also wants to contribute to a more simple, efficient and sustainable EU tax policy. Examples of Parliament resolutions prepared at (sub-) committee level are:

— Resolution of 15 February 2022 on national tax reforms, which, inter alia, welcomes the historic agreement reached by OECD/G20 on the reform of the international tax system with the aim of ensuring a fairer distribution of profits and taxing rights among countries with respect to the largest multinational companies (partial reallocation of taxing rights to countries where value is created and establishment of a global minimum effective taxation of 15%).

— Resolution of 21 October 2021 entitled 'Pandora Papers: implications for the efforts to combat money laundering, tax evasion and tax avoidance', which calls on the EU to close loopholes that currently allow tax avoidance, money laundering and tax evasion on a massive scale. It also called for legal action to be taken by the Commission against EU countries that do not properly implement current EU legislation in this field.

— Resolution of 7 October 2021 on reforming the EU policy on harmful tax practices, which, among other things, calls for a revision of the criteria, governance and scope of the Code of Conduct for Business Taxation (which, according to the resolution, has been the Union's primary instrument to prevent harmful tax competition since 1997). It also states that revision of the Code of Conduct should be conducted using a democratic, transparent and accountable process involving a group of experts from civil society, the Commission and Parliament.

For more information on this topic, please see the website of the Subcommittee on Tax Matters (FISC).

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