tax justice network

Europeanising Company Taxation - Regarding National Tax Policy Autonomy
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In this article the authors suggest the introduction of a common consolidated corporate tax base (CCCTB) and a minimum tax rate in the EU, to eliminate transfer pricing concerns and the problems stemming from tax competition.

The authors point out that it is counterproductive to insist on preserving sovereignty in tax matters, because in an open economy sovereign nations compete with each other on tax rates, and this "tax competition" removes or curbs their abilities to design autonomous tax policies:

> "Precisely the principles of nationally separate taxation, which preserve countries' formal sovereignity to design their own tax systems, lead to a restriction of their actual capacity to achieve the objectives of distributive fairness and efficiency. Precisely the fact of their formally unlimited tax sovereignity leads to a limitation of their de facto policy autonomy."

The problem, the authors explain, is related to fundamental principles of international tax law which, they summarise,

> ". . . as a general rule is based on the legal form and not on the economic substance of a subsidiary or other place of business. Little more than a mailbox in a low tax country is required in order to assign profits to the country or route them through in a tax efficient way. Empirical evidence suggests that companies make use of these opportunities to a considerate extent."

This contributes to the "transfer pricing" problem, and the authors analyze the problems of the prevalent "separate entity" accounting method and the arm's-length principle. Items such as "knowledge and experience" are very difficult to price correctly at arm's length, and it is easy for multinationals to manipulate transfer prices so that profits are reported in low tax countries and losses in high tax countries; and corporation taxes are reduced overall.

To recover autonomy on organising socially just and efficient tax systems, the authors argue that states should not simply adapt individually to the global tax environment, but should operate collectively, at a European level. To achieve this, it is necessary to harmonise certain aspects of European tax policy. Specifically, the authors propose two steps.

The first step is to introduce in the EU a mandatory common consolidated corporate tax base (CCCTB) with formulary apportionment, as a solution to the problem of tax competition. This way, states would no longer compete with each other on tax rates. This would potentially raises another problem, however, that if tax competition is eliminated on this way, states will start to compete with each on other factors, particularly mobile factors. This, in turn, can be addressed by a second step: agreeing on a common tax rate, or at least a minimum tax rate:

> With a common consolidated tax base plus formula apportionment, tax competition is no longer only about shifting profits on the books, but rather – in so far as no minimum tax rate is set – real investments. Companies and countries can compete on the factors which are part of the apportionment formula. It is conceivable that, because a CCCTB limits the possibility of shifting paper profits, it reinforces the competition for real investment. The significance of this competition for member states depends, among others, on the weighing of mobile and immobile factors in the formula. The more mobile the factors in the formula, the more susceptible the system is to tax competition between member states.

The authors discuss the benefits of the CCCTB in the EU, compulsory for all legal forms across the EU, and with a minimum tax rate.

> We have already explained why formula apportionment which is primarily based on microeconomic factors will not curb locational competition, even if it leads to a more transparent form of competition in comparison with the status quo of tax competition based on shifting paper profits. That is why the CCCTB with formula apportionment must be accompanied by a minimum tax rate if tax competition is not merely to be pushed onto other factors
> ……….
> Our proposal for an exemplary minimum tax rate is based on the assumption that the common European tax base is as broad as the current average national tax bases. This rate, inclusive of local business taxes, should be 30%.

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