EUTAXGOV

EU Tax Governance

The EU's Role in the Global Governance of Direct Taxes

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1. The EU and direct taxes

Traditionally, states have been reluctant to give up competences to set tax policy to a supranational level. Nevertheless, over time the EU has succeeded in establishing some common tax policies across its Member States. While the harmonisation of the value added tax already took off in 1967, direct tax policy (i.e., personal and corporate income taxes) only started to be regulated in the 1990s (see Annex) and the degree of harmonisation today is still lower. EU directives on direct tax policy mainly regulate the taxation of cross-border flows (such as dividends, interest, and royalty), harmonize anti-avoidance rules, and implement administrative cooperation and dispute resolution procedures. As will be discussed further below, the EU also strives to implement common direct tax policies directed at third countries. However, important aspects such as tax rates and many aspects of the tax base remain unharmonized up to date.

This leaflet summarizes the role of the different EU institutions in taxation, situates the EU within the wider universe of global tax governance and discusses in detail the EU's policy towards third countries. Finally, it provides an overview over the main current challenges.

2. The role of different EU institutions in taxation

All four main institutions of the European Union - the European Commission, the Council of the European Union, the European Parliament, and the European Court of Justice - play a role in tax governance.

Within the European Commission, the Directorate-General for Taxation and Customs Union (DG TAXUD) is responsible for developing and implementing EU policies on taxation, such as Directives, and Recommendations, and is actively involved in global negotiations in other fora (such as the OECD).

The Council of the European Union has several committees involved in tax governance, including the Economic and Financial Affairs Council (ECOFIN) and the Code of Conduct Group on Business Taxation. The ECOFIN is responsible for adopting EU Directives and monitoring member states' fiscal policies. The Code of Conduct Group on Business Taxation is a group of experts from Member States' ministries of finance that assesses and monitors tax measures in member states that could potentially harm the single market.[1]

In the European Parliament, the Subcommittee on Tax Matters (FISC), which was established in 2020 as part of the Committee on Economic and Monetary Affairs (ECON), organizes hearings on tax governance issues, and provides input and recommendations to the ECON Committee and other EU institutions on issues such as the EU's approach to international tax negotiations. Previously, the Parliament used to create temporary committees on specific issues, such as the Special Committee on Tax Rulings and Other Measures Similar in Nature or Effect (TAXE) or the PANA Committee of Inquiry, following the Panama Papers Leaks.

Finally, the European Court of Justice (ECJ) is responsible for interpreting EU tax laws, settling disputes between member states and between member states and the EU institutions. In the last decade, the ECJ has played an important role in tax governance, as the EU Commission has litigated against laws and administrative practices of several member states under the EU State Aid rules.[2]

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[1] Nouwen, "The European Code of Conduct Group Becomes Increasingly Important in the Fight Against Tax Avoidance: More Openness and Transparency Is Necessary."

[2] European Commission, "State Aid - Tax Rulings"; Eden and Byrnes, "Transfer Pricing and State Aid"; Peters, "Tax Policy Convergence and EU Fiscal State Aid Control: In Search of Rationality."

3. The triple role of the EU in Global Tax Governance

Global tax governance consists in the “set of institutions governing issues of taxation that involve cross border transactions or have other international implications”.[3] There is a multitude of organizations that make up global tax governance, among them the OECD, United Nations, regional tax organizations (such as ATAF and CIAT), World Bank, IMF – and, of course, the European Union. All organizations fulfil slightly different roles: Some focus on developing policy standards, while others mainly provide technical assistance, or facilitate an exchange of practices among countries. In the development of standards, the OECD and the so-called BEPS Inclusive Framework, which is located at the OECD, have taken a central role.

Within this institutional complex, the EU has taken up three functions:

- Input function: Pioneering policies and coordinating member states’ positions on the introduction of international standards;
- Ensuring a harmonized adoption of international standards among its member states;
- Using its market power to induce third states in adopting global standards

The input function:

Due to the (relatively) high degree of similarity of EU Member States’ tax systems and economic conditions, the EU is often a frontrunner in policy harmonization, and initiatives that are first tried in the EU serve as template for the development of standards with a more global reach. In addition, EU institutions are represented in international fora, such as the BEPS Inclusive Framework.

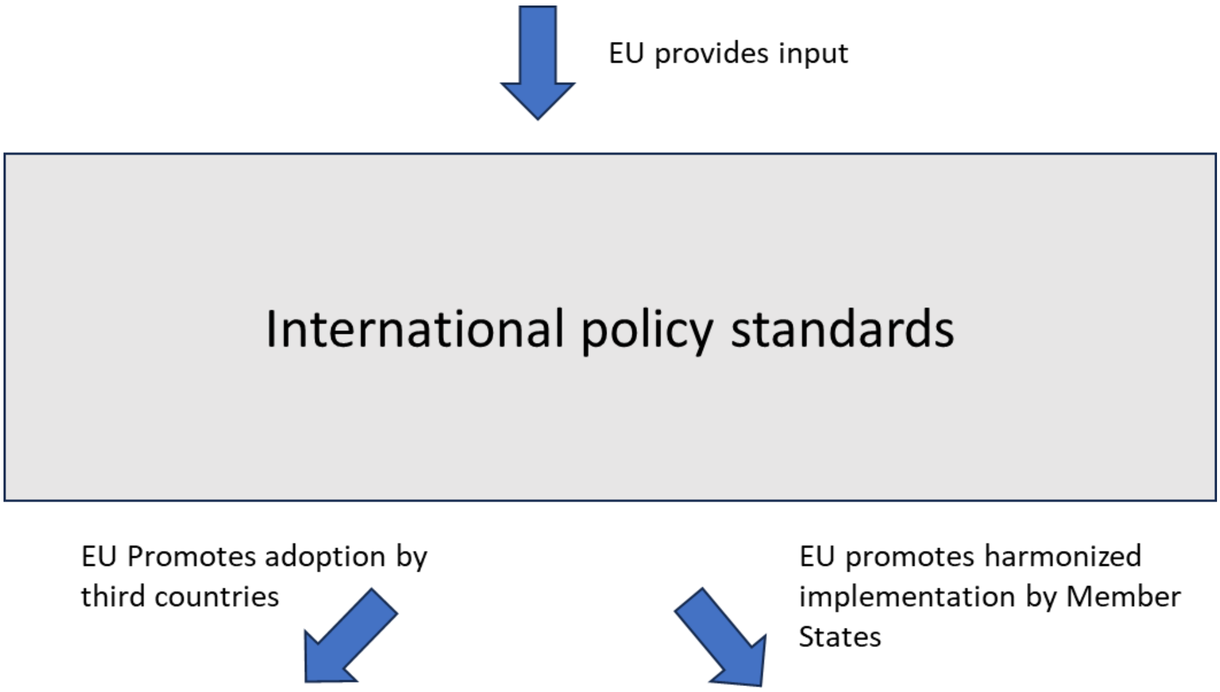
Harmonized adoption:

On the other hand, the EU also aims to ensure that global standards are transposed in a harmonized way within the Europe. By translating recommendations emanating from the OECD into Directives, it gives the former more binding character, which is backed up through the EU’s infringement procedures. Examples are the Anti-Tax Avoidance Directives (ATAD I & II), which transpose parts of the recommendations of the BEPS Project, and the Directives on Administrative Cooperation, which adopt international standards on exchange of information. Sometimes, the aim to ensure harmonized adoption has resulted in controversies. When, for example, the EU Commission argued in State aid investigations that Member States had not correctly interpreted the arm’s-length-standard, the argument was rejected by the European Court of Justice on the basis that the OECD documents spelling out the arm’s-length-standard were not binding.

Using power of the common market to ensure adoption of international standards by third countries

Finally, the EU has started to apply pressure on third countries to comply with international standards developed by the OECD. This role is the most controversial. The main instrument used is the *Standard of Good Tax Governance,* which is introduced in trade agreements, and which underpins the EU list of non-cooperative jurisdictions. Good tax governance, in turn, is mainly defined as adherence to a set of OECD standards.

[3] Dietsch and Rixen, “Global Tax Governance: What It Is and Why It Matters.”



The triple role of the EU in global tax governance

4. The EU's role vis-à-vis third countries: a source of tension

The Standard of Good Tax Governance was first introduced in 2008 as a framework to promote fair and transparent taxation in non-EU countries.[4] Over time it has been further developed and today it consists in a set of criteria, such as the absence of harmful tax regimes (fair taxation), and the adoption of international standards against tax evasion and tax avoidance.

There are two main mechanisms for inducing EU-countries to comply with the Standard: First, a tax governance clause is routinely incorporated into trade agreements and strategic partnership agreements concluded by the EU.[5] Recent examples are the 2018 EU-Japan Strategic partnership agreement or the EU-Philippines Partnership and Cooperation Agreement currently under negotiation.

Second, it underpins the EU list of non-cooperative jurisdictions in tax matters. The list is based on a process of assessment and monitoring conducted by the EU's Code of Conduct Group on Business Taxation. The assessment process involves evaluating countries based on criteria of economic importance to the EU and the good tax governance criteria outlined above.[6] Countries that fail to meet the latter are added to the list. The list is regularly updated, and countries that make sufficient progress in addressing their harmful tax practices may be removed from the list.

The EU list of non-cooperative jurisdictions has several implications. For example, EU Member States are required to apply stricter scrutiny to transactions involving companies or individuals based in listed countries, which can make it more difficult for businesses to operate in those jurisdictions. The EU and its Member States may also impose specific sanctions on listed countries, such as restricting access to

[4] Mosquera Valderrama, "The EU Standard of Good Governance in Tax Matters for Third (Non-EU) Countries."
[5] Council of the European Union, "Council Conclusions on the 'EU Standard Provision on Good Governance in Tax Matters for Agreements with Third Countries' – Adoption."
[6] Council of the European Union, "COUNCIL CONCLUSIONS on the Criteria for and Process Leading to the Establishment of the EU List of Non-Cooperative Jurisdictions for Tax Purposes."

EU funding or imposing higher withholding taxes on payments made to companies based in those countries.[7]

The EU list has been shown to have triggered policy changes in some countries, according to some empirical studies.[8] However, it has also faced criticism from affected countries, civil society, academics, and Members of the European Parliament, leading to tensions.[9]

One of the main sources of tension arises from the fact that international standards of tax governance (such as those promulgated by the OECD) may not necessarily be endorsed by countries whose compliance is monitored by the EU. These countries may argue that the standards imposed by the EU do not align with their national interests or may impose undue burdens on their economies, leading to diplomatic tensions.[10] Some affected countries have questioned the criteria used by the EU for blacklisting or greylisting jurisdictions, and have raised concerns about the fairness and objectivity of the process.[11]

Critics of the EU list also question whether all EU Member States themselves comply with the standard of good tax governance. There have been concerns raised about the tax policies of certain EU Member States, which may technically comply with the standard, but could still have harmful effects on other countries.[12] This has led to accusations of inconsistency and hypocrisy, with some arguing that the EU should ensure compliance within its own member states before imposing standards on third countries.[13]

Furthermore, the EU's approach to listing non-cooperative jurisdictions has been criticized for a lack of transparency, arbitrariness, as well as politicization of the process.[14]

5. Challenges for the future role of the EU in global tax governance

In order to resolve tensions in its tax relations with third countries, the EU will need to strike a delicate balance between promoting its tax governance standards and respecting the sovereignty and interests of third countries. This may involve engaging in constructive dialogues, addressing concerns raised by affected countries, and ensuring transparency and fairness in the listing process. It may also require the EU to critically assess and improve its own tax policies and practices to maintain credibility and legitimacy in its role as a global tax governance actor.

Next to this, the EU also faces challenges in its internal relations. First, it needs to ensure commitment by Member States in the current projects of tax harmonization. That this cannot be granted was shown

[7] European Commission, "Questions and Answers on the EU List of Non-Cooperative Tax Jurisdictions."
[8] Oei, "World Tax Policy in the World Tax Polity? An Event History Analysis of OECD/G20 BEPS Inclusive Framework Membership"; Collin, "Does the Threat of Being Blacklisted Change Behavior? Regression Discontinuity Evidence from the EU's Tax Haven Listing Process."
[9] Mosquera Valderrama, "The EU Standard of Good Governance in Tax Matters for Third (Non-EU) Countries"; Fowler, "Will the EU Really Blacklist the United States?"
[10] Cartwright-Carroll, "'Black-Governed Countries Matter'. PM Tells UN The Bahamas Is the Victim of Unjust Measures."
[11] Cartwright-Carroll.
[12] Langerock, "Off the Hook: How the EU Is about to Whitewash the World's Worst Tax Havens."
[13] Koutsouva, "The European Union's List of Non-Cooperative Jurisdictions for Tax Purposes."
[14] IFC Review, "Is the EU Tax Blacklist More Political than Technical?"

in the process leasing to the adoption of the OECD's Global Minimum Tax Proposal in form of an EU Directive. The process took a long time since Hungary (and initially Poland) withheld their approval for reasons not related to tax policy.[15] This is striking since transposing Pillar 2 in form of a Directive may not have actually been necessary to ensure EU wide adoption, since the mechanism of the policy creates incentives for countries to implement it.[16] Therefore, the EU institutions need to carefully consider for which projects political energy should be used.

More ambitious projects of tax harmonization have been stalled, for example the introduction of a common consolidated EU-wide tax base for companies. Originally known as CCCTB proposal, this initiative was recently relaunched as BEFIT proposal.[17] However, as of now it does not seem to have garnered sufficient support from member states. As further harmonization in direct taxation is certainly an important aspect in European integration, progress on such matters may be crucial. A common tax base would be a significant step towards further integration.

Especially since the COVID-19 crisis, calls for deeper integration both in substance and process have been made. On the substance, the possibility of shifting taxing powers directly to the EU have been evoked.[18] On procedural aspects, there has been an ongoing debate about the modalities of decision-making on tax policies at EU law. Currently, EU tax laws need to be adopted by unanimity to safeguard the sovereignty of Member States in matters of direct taxation. However, in 2019 the EU Commission proposed a shift to qualified majority voting, which would effectively take away veto power from individual EU states.[19]

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[15] van Brederode, "From Impasse to Unanimity: Understanding Hungary's Position on Pillar 2."
[16] Mason, "A Wrench in the GLOBE's Diabolical Machinery."
[17] European Commission, "Business Taxation for the 21st Century."
[18] Le Cacheux, "Funding the EU Budget with a Genuine Own Resource: The Case for a European Tax"; Heitmüller, "Corporate Income Taxation and COVID-19 – Time to Think about a European Tax?"
[19] European Commission, "Towards a More Efficient and Democratic Decision Making in EU Tax Policy"; Mosquera Valderrama, "A New Wind Change in Direct Taxation."

See also

EUTAXGOV Blog: https://eutaxgov.weblog.leidenuniv.nl/
Website EU Commission: https://taxation-customs.ec.europa.eu/taxation-1_en
Website EU Council: https://www.consilium.europa.eu/en/topics/taxation/
Website EU Parliament : https://www.europarl.europa.eu/committees/en/fisc/home/highlights

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Annex: Milestones of EU Tax Governance

1990: Parent-Subsidiary Directive (recast in 2011)/ Merger Directive (recast in 2005)

1992: Ruding report

1997: Establishment of the Code of Conduct for business taxation

1999: Primarolo report

2003: Interest and Royalty Directive

2003: Savings Directive

2009: Communication on Promoting Good Governance in Tax Matters

2011: Directive on Administrative Cooperation (DAC) 1

2011: CCCTB Proposal (relaunched in 2016)

2016: Anti-Tax Avoidance Directive (ATAD) I

2017: ATAD II

2017: First list of non-cooperative jurisdictions published

2020: FISC Subcommittee in European Parliament established

2021: Communication on Business Taxation for the 21st Century

2022: Proposal for Unshell directive

2022: Directive on Minimum Corporate Taxation