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Brussels, 9 July 1997

OPINION
of the
Economic and Social Committee
on
Taxation in the European Union
Report on the development of tax systems
SEC(96) 487 final and COM(96) 546 final



Memorized text

On 18 February 1997 the Commission decided to consult the Economic and Social Committee, under Article ... of the Treaty establishing the European Community, on

Taxation in the European Union - Report on the development of tax systems
(SEC(96) 487 final and COM(96) 546 final).

The Section for Economic, Financial and Monetary Questions, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 10 June 1997. The rapporteur was **Mr Geuenich**.

At its 347th plenary session of 9/10 July 1997 (meeting of 9 July 1997) the Economic and Social Committee adopted the following opinion by 93 votes to 27 with 19 abstentions:

1. Introduction

1.1 In its paper of 20 March 1996 entitled **Taxation in the European Union (SEC(96) 487 final)** the Commission presented a view of taxation policy, which in particular highlighted the major challenges facing the European Union: the need to create growth and employment, to stabilize fiscal systems and to realize the single market in all areas, including that of taxation.

1.2 At the informal Ecofin Council meeting in **Verona** on 13 April 1996, finance ministers welcomed the Commission paper and agreed on the need to take forward the consideration of these issues in a **High Level Group**, to be set up and coordinated by the Commission.

1.3 In its **Report on the development of tax systems of 22 October 1996 (COM(96) 546 final)** the Commission summarizes the views expressed by members of the High Level Group on the issues first raised by the Commission's Verona document and sets out its own assessment of these particular issues and its planned approach for the future.

1.4 In this opinion the Committee confines itself to discussion of **the two documents referred to above**. Where the Committee has already expressed a view on problems raised in these two documents, reference is made to the relevant opinions, in particular the **Opinion on Direct and indirect taxation** of 20 December 1995¹ and the **Opinion on a Common system of VAT - a Programme for the Single Market**².

1.5 In this opinion, as in the reference documents mentioned above, only taxes which are of Community-wide importance, where national structures, or changes to these, affect other Member States, are discussed. These comprise income and withholding tax, corporation tax, taxes on labour, consumer taxes, particularly VAT, as well as a tax on energy and products harmful to the environment.

2. Rising burden of tax on labour

2.1 Analysis in the Commission documents

2.1.1 There is so far little evidence that **fiscal erosion** is affecting **total revenue** from taxes and social levies. Over the last fifteen years their share of Community GDP has remained constant or risen slightly. However, whilst **labour has been increasingly heavily taxed**, the tax burden on the other factors of production has fallen overall.

2.1.2 One method for analysing the long-term trends in the structure of taxation is to calculate **implicit tax rates** (i.e. tax revenues divided by the tax base) for factors of production and consumption.

Between 1980 and 1994, the European average of the implicit tax rate on employed labour increased steadily from 34.7% to 40.5%. The same rate for the other factors of production (capital, self-employed labour, energy, natural resources) decreased from 44.1% to 35.2% (see graph below).

2.1.3 The implicit **rate for consumption** was broadly stable, rising slightly from 13.1% to 13.8%. Again there were large variations between individual Member States however. Those Member States which had the largest rises in the implicit tax rate on employed labour over this period were mainly those where the level of total taxation had increased most.

2.2 The Committee's recommendations

2.2.1 The Committee welcomes the Commission's approach of looking at the **tax system as a whole**, as discussing each major type of tax separately automatically implies far-reaching changes in the financing

structure both of the public sector and private households. The tax discussion should thus be **comprehensive**.

2.2.2 Mass unemployment is the EU's most intractable problem. All contributions to reducing this and the measures needed to do this thus have the highest priority. This is also one of the central themes of the **Commission's White Paper** on Growth, Competitiveness and Employment - The Challenges and Ways Forward into the 21st Century³. A way has therefore to be found of **financing a reduction of the burden of tax** on labour and reducing non-wage labour costs.

2.2.3 Public expenditure reductions are one way of financing a reduction of the burden of tax on labour, but are not on their own sufficient. Alternative sources of finance are indirect taxes (taxes on consumption), the introduction of minimum tax rates for energy products and **consideration of the possible** introduction of completely new types of tax such as, for example, a Tobin⁴ tax applicable to the international financial markets, the discussion of which has been initiated by well-known economists and financial experts.

2.2.4 Although the Member States have to assess themselves the extent to which tax instruments are needed for the achievement of national environment-policy objectives, there is however clearly an area in which **action at Community level** is needed. This is true of the **taxation of energy**, which has an important role to play here if the goal of stabilizing CO₂ emissions at the level of 1990 by 2000 is to be achieved.

The Committee welcomes the Commission's proposals on the taxation of energy products⁵.

2.2.5 The **approximation of European VAT rates** can also help reduce the direct taxation of labour. In Member States where indirect taxation rises as a result of tax approximation, the direct taxation of labour must at the same time be reduced. In this way overall tax revenue trends will remain unchanged and job creation will be encouraged. At the same time flanking measures will be provided to alleviate the effects on the lowest income groups of an increase in indirect taxation.

The Committee would refer in this context to its Opinion on a Common system of VAT - a programme for the single market⁶ and to its **Opinion on Direct and Indirect Taxation**⁷.

2.2.6 **To sum up**, the Committee points out that the above financing opportunities, as well as the measures discussed below for the taxation of income from capital would have different effects on overall tax revenues in the various Member States and would thus differ in the extent to which they offer ways of financing a **reduction of the burden of public levies on labour**. Each Member State must therefore adopt the financing measures best suited to it in the framework of the Commission's existing requirements.

3. Fiscal erosion through tax switching

3.1 Analysis in the Commission documents

3.1.1 In comparison with many other areas of European integration, tax policy is clearly lagging behind. **In tax policy terms Europe is a patchwork**. As a result of **erosion of fiscal bases**, especially the more mobile ones, professed attempts to defend tax sovereignty have in fact had the opposite effect, **a gradual real loss of tax sovereignty** for all the Member States. More and more Member States are poaching other Member States' taxpayers, particularly in the field of business.

3.1.2 In the case of direct taxes there are two main ways of reducing the effective tax burden:

First, **switching production and tax bases to low-tax countries**, in order to benefit from low taxation of factor income. This makes it attractive for a state to reduce business taxes, because the resulting loss of tax revenue will, in the medium term, be counter-balanced by new revenue from tax and social levies arising from additional employment.

Secondly, manipulating the cost of inputs into the final product in multinational corporations **via internal transfer prices** with the goal of transferring taxable income to low-tax countries: this kind of manipulation is possible because **inputs have no market value**. The internal transfer prices fixed are thus to a great extent outside the scope of the tax authorities' checks on abuses.

3.1.3 Even **indirect taxes**, which are harmonized to a much greater extent than direct taxes, are not immune to fiscal erosion. A particular threat to **VAT** is that because of the **country of destination principle** firms active in **two or more Member States** will be **registered** in the same number of countries (two or more) **for tax purposes**. In contrast to the taxation of the turnover of a firm operating in the Community **in a**

single location, there is **no EU tax authority** to cover such cases with an **overview** of the activities of a firm which could then be assessed at a single tax centre. In addition to this, there is the fact that, with the growth of cross-border services, new technologies are being used to switch taxable revenues to locations outside the net of the VAT system. Moreover, the differences between national rates of VAT offer more and more scope for tax avoidance. The reduction of checks on the cross-border movement of goods leads to substantial losses of VAT revenue for the budgets of the Member States and the EU itself.

3.1.4 The **black economy** also contributes to fiscal erosion. It should be borne in mind that there are always two sides to work in the black economy: the worker and his employer.

3.2 The Committee's recommendations

3.2.1 It is in the **vital interests** of the European Union, the internal market and EMU for tax dumping in Europe to be eliminated and prevented. Whilst **fair competition between tax systems**, aimed at creating favourable conditions for workers, employers and consumers is to be welcomed, **destructive competition**, benefiting few and hurting many, could undermine the whole EU:

- if **net contributors** to the EU budget are expected to pay ever heavier contributions while the tax revenues urgently needed to finance these are being undermined; and
- given that individual net contributors are estimated to be suffering annual losses of tax revenue of the order of ECU 25 to 30 bn as a result of tax dumping⁸.

3.2.2 It must not be an aim of EU tax policy to harmonize business taxes simply for the sake of it. Measures are needed however to ensure that tax dumping between the Member States does not threaten to undermine the EU.

The Committee does advocate the setting of **minimum standards for the rate of corporation tax** and minimum harmonization of the main criteria used in **determining the tax base**. For further details the Committee would refer to its Opinion on **Direct and Indirect Taxation**⁹.

3.2.3 The Committee feels that the same approach should be adopted as in dealing with **direct subsidies**, with due regard to the principle of subsidiarity. Direct subsidies continue to be the responsibility of the Member States, although the **Commission monitors compliance with the rules of competition**. Such monitoring is also needed in relation to taxation. The monitoring of tax support measures practised so far is not enough, as it extends only to **deviation from the general systems of the Member States**. This does **not** allow for the fact that, as things stand at present, **distortions of competition are arising from the very differences in individual tax systems**, which are in some cases even more serious than the distortions accentuated by specific tax incentives.

3.2.4 At present a Member State cannot on its own eliminate either all the tax obstacles or the individual causes of the fiscal erosion described. In this situation, the Committee feels, doing nothing is not an appropriate solution. The Commission must, whilst fully complying with the principle of subsidiarity, study and propose solutions to these problems, which the Member States cannot themselves solve by individual action.

3.2.5 The requirement for **unanimity in the Council** on tax decisions is clearly a barrier to progress on taxation and the requirements of the internal market. This is demonstrated by the large number of important Commission tax proposals currently blocked by the Council.

But the Committee feels that the Commission has the instruments at its disposal. Under **Article 101 of the EC Treaty** the Commission is in fact required to eliminate differences in the laws and regulations of the Member States which are distorting the conditions of competition in the common market. In such a case the matter is to be discussed by the Council of Ministers. Any decision is **in principle required to be unanimous**. But if no agreement is achieved a decision can then be taken by a **qualified majority at the proposal of the Commission**.

The Committee feels that the Commission should act as soon as possible under Article 101.

4. Tax fraud

4.1 Analysis in the Commission documents

The problem of tax fraud is particularly acute in relation to the taxation of **income from savings**. This is the **most mobile base of all**, and differences in taxation can cause serious distortions to capital allocation and flows. The **elimination of currency risks** and the reduction of tax rate differentials in **stage III of EMU** would lead to such differentials being even more extensively exploited than at present.

4.2 The Committee's recommendations

4.2.1 The further harmonization of the **internal market** progresses, the more clearly differences in **tax systems** are felt and the more relevant they become for the decisions of economic operators. The basic principle here is that minimum harmonization of taxes and tax bases is **needed most** where the tax base is at its **most mobile**, i.e. in relation to income from capital such as interest and dividends.

4.2.2 In order to rein back competition over taxes, to provide the resources needed for the creation of jobs and to ensure that the European Union is not at a disadvantage on the **international capital markets**, the Committee recommends the following measures, in implementing which **international constraints** must be considered:

4.2.2.1 Introduction of the concept of the **Community resident**: it is no longer acceptable on the one hand to abolish European internal frontiers and on the other to distinguish within the Member States between "residents" and "non-residents", as this implies the existence of frontiers.

4.2.2.2 Introduction of a European and international approach to the taxation of income from savings. In the context of such measures the existing differences between the Member States with regard to the taxation of income from savings (**withholding tax or compulsory notification**) must be respected, and it must be ensured that no one system is preferred at the expense of another. Member States in which taxes are raised on the basis of a notification requirement must have the assurance that income earned by their residents on savings in other Member States will be notified to them.

In the reverse case, Member States with a withholding tax must have a guarantee that income earned by their residents on savings in other Member States will either be subject to withholding tax or systematically notified.

4.2.2.3 This would mean that Member States could **choose** between a **withholding tax** and **systematic notification** of interest and dividends paid to the authorities of the Member State in which the saver is resident.

4.2.2.4 Within the EU **tax havens** situated in the territory of Member States would be abolished. The regularization of European "exclaves" outside the Union and exotic offshore centres should also be negotiated.

4.2.2.5 In view of the outflow of savings to non-Community countries, a solution based on that adopted by the EU should also be sought **in the framework of the OECD**, involving a withholding tax or the exchange of information.

4.2.3 The Committee agrees with the personal representatives of the finance ministers in regarding the intensification of **cooperation** between tax authorities in dealing with tax evasion and fraud in the internal market as a priority. This cooperation should not however be restricted to the exchange of experience on ways of stopping tax fraud; it should, rather, serve to improve **checks and official cooperation** between the tax authorities of the Member States. Here use should be made of the opportunity to carry out joint tax inspections in cases of cross-border economic activity.

4.2.4 By limiting tax fraud a contribution can be made to **financing a reduction of pressure on labour** in those states which are the source of savings and thus the basis for the taxation of interest.

4.2.5 The Committee refers for further details to its **Opinion on Direct and indirect taxation**¹⁰.

5. The Commission's future strategy

5.1 The Commission's view

5.1.1 On the basis of the discussions of the EU finance ministers' personal representatives the Commission has developed a **strategy for the future**.

5.1.2 The personal representatives stressed the need for **more coordination**. The **Commission** then proposed the establishment of a new permanent **Forum** to deal with strategic tax policy questions to enable

the Member States and the Commission to **exchange information and discuss tax questions**. This proposal was welcomed by the **Dublin European Council** in December 1996. Commissioner **Monti** chairs the Forum which brings together high-level representatives of the finance ministers of the Member States. With regard to tax competition, the Commission hopes that the work of the Forum may lead to initiatives in the following areas:

- securing broad agreement on what types of measures are **harmful in a Community context**;
- defining common standards across a range of areas (a "**code of good conduct**");
- introducing greater coordination of measures that are taken by the taxation authorities of Member States and designed to **prevent tax competition** from harming the common interest;
- reinforcing **cooperation between tax authorities** in the mutual fight against tax fraud and evasion.

5.1.3 The following questions are also to be discussed in the **forum**:

- the role, functioning and possible coordination of **double taxation treaties**;
- the simplification of the **tax environment for SMEs** and other businesses;
- the interaction of taxes and social security contributions, in particular for **cross-border workers**;
- and the taxation of international services and the impact of **new technologies**.

5.1.4 The Commission proposes complementing the work of the Forum with the discussion of forward-looking initiatives on the development of tax systems meeting the Community's needs and facilitating the smooth operation of the internal market.

5.2 The Committee's recommendations

5.2.1 The Committee endorses the **Commission's strategy for the future** and recommends that the Commission make use of **Article 101 of the EC Treaty** (see Appendix 1) so that strategies to block progress on EU-wide tax-policy coordination can be countered.

5.2.2 The Committee welcomes the initiatives announced by the future Luxembourg Presidency in the area of European tax policy, in the hope that progress will thus be made on solving the problems referred to in this opinion.

5.2.3 As an **appendix to this opinion** there follow a number of possible options for change to the EC Treaty aimed at **enlarging the scope for action** on European tax policy. The Committee stresses that the contents of the appendix are intended merely as a basis for discussion and not as binding recommendations.

Brussels, 9 July 1997.

The President
of the
Economic and Social Committee

The Secretary-General
of the
Economic and Social Committee

Tom Jenkins

Adriano Graziosi

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N.B.: Appendices overleaf.

APPENDIX 1**EC Treaty****Article 101**

(Treatment of rules distorting competition).

" Where the Commission finds that a difference between the provisions laid down by law, regulation or administrative action in Member States is distorting the conditions of competition in the common market and that the resultant distortion needs to be eliminated, it shall consult the Member States concerned.

If such consultation does not result in an agreement eliminating the distortion in question, the Council shall, on a proposal from the Commission, acting unanimously during the first stage and by a qualified majority thereafter, issue the necessary directives. The Commission and the Council may take any other appropriate measures provided for in this Treaty."

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APPENDIX 2

1) Article 7a

The internal market shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of this Treaty. Double taxation or the absence of taxation is incompatible with the internal market. Where no other state is responsible, taxation shall be the responsibility of the Member State of residence.

2) Article 73d

1. The provisions of Article 73b shall be without prejudice to the right of Member States:

- (a) to apply the relevant provisions of their tax law which provide for different tax treatment for 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; this shall not however give rise to any difference in the tax burden;
- (b) to take all requisite measures to prevent infringements of national law and regulations, in particular in the field of taxation and the prudential supervision of financial institutions, or to lay down procedures for the declaration of capital movements for purposes of administrative or statistical information, or to take measures which are justified on grounds of public policy or public security.

2. The provisions of this Chapter shall be without prejudice to the applicability of restrictions on the right of establishment which are compatible with this Treaty.

3. The measures and procedures referred to in paragraphs 1 and 2 shall not constitute a means of arbitrary discrimination or a disguised restriction on the free movement of capital and payments as defined in Article 73b.

3) Article 99

The Council shall, acting in accordance with the procedure referred to in Article 189b and after consulting the Economic and Social Committee, adopt the VAT provisions.

4) Article 100

5) Article 100a

1. The Council shall, acting in accordance with the procedure referred to in Article 189b and after consulting the Economic and Social Committee, adopt the measures for the approximation of the provisions laid down by law, regulation or administrative action in Member States which have as their object the establishment and functioning of the internal market.

2. In addition to the case referred to in the second half of the first sentence of Article 189b(3), the Council shall also act unanimously on taxes which are only partly destined for the Community budget and provisions relating to the free movement of persons and the rights and interests of employed persons, if at least two Member States so require; if an application to this effect is lodged, the Council shall also act unanimously in relation to any subsequent decisions (Article 189b(5) and (6)).

6) Article 130s

1. The Council, acting in accordance with the procedure referred to in Article 189c and after consulting the Economic and Social Committee, shall decide what action is to be taken by the Community in order to

achieve the objectives referred to in Article 130r.

2. By way of derogation from the decision-making procedures provided for in paragraph 1 and without prejudice to Article 100a, the Council, acting unanimously on a proposal from the Commission and after consulting the European Parliament and the Economic and Social Committee, shall adopt:

- provisions primarily of a fiscal nature, if at least two Member States so require, in relation to taxes only partly destined for the Community budget;
- measures concerning town and country planning, land use with the exception of waste management and measures of a general nature, and management of water resources;
- measures significantly affecting a Member State's choice between different energy sources and the general structure of its energy supply.

The Council may, under the conditions laid down in the preceding subparagraph, define those matters referred to in this paragraph on which decisions are to be taken by a qualified majority.

3. In other areas, general action programmes setting out priority objectives to be attained shall be adopted by the Council, acting in accordance with the procedure referred to in Article 189b and after consulting the Economic and Social Committee.

The Council, acting under the terms of paragraph 1 or paragraph 2 according to the case, shall adopt the measures necessary for the implementation of these programmes.

7) Article 220

Member States shall, so far as is necessary, enter into negotiations with each other with a view to securing for the benefit of their nationals:

- the protection of persons and the enjoyment and protection of rights under the same conditions as those accorded by each State to its own nationals;
- the simplification of formalities governing the reciprocal recognition and enforcement of judgments of courts or tribunals and of arbitration awards.

Without prejudice to measures adopted under Article 100a, the Member States may enter into agreements with each other on the practical implementation of the prohibition of double taxation (Article 7a); they shall inform the Commission of such measures and the Commission shall bring these to the attention of the other Member States.

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APPENDIX 3
to the opinion of the Economic and Social Committee
(Rule 47 of the Rules of Procedure)

The following amendments, which received at least one quarter of the votes cast, were defeated in the course of the Committee's debates:

The whole opinion

"1. Introduction

*1.1 Taxation is a very complex and involved subject. In this opinion, the ESC confines itself to discussion of **the documents SEC(96) 487 final and COM(96) 546 final**. It has, therefore, elected to address only the most important macro-economic tax issues; sectoral matters are dealt with only where they raise questions of more general significance.*

1.2 This document takes as its departure point the fact that unemployment in the EU is around 20 million and that this problem has exhibited a considerable degree of intransigence to all previous attempts to resolve it or even to alleviate its effects. It therefore approaches the subject of European taxation policy from the standpoint of how this can best be structured in order to contribute to the solution of what must be regarded as the most important and urgent problem facing the EU at the present time.

1.3 The long-term nature of this problem and the fact that the trend is showing little sign of improvement, underlines the need for radical thinking and a new approach rather than a repetition of the tired 'remedies' which have so signally failed to provide a solution to date.

*1.4 In this, the ESC is at one with the Commission which, referring to President Santer's Confidence Pact for Employment, said that **'This highlighted in particular the need to reverse the tendency of taxation systems to be detrimental to employment**, as part of a wide-ranging strategy to create more jobs in the Union.'*

*1.5 As the Commission document notes, the European Council in Florence also requested the Council 'to submit to it, before the European Council in Dublin, a report on the development of tax systems within the Union, **taking account of the need to create a tax environment that stimulates enterprise and the creation of jobs...**'*

1.6 &nb sp;In the final analysis, job creation depends on sustained economic growth and the surest way of achieving this is to reduce the twin burdens of excessive taxation and excessive regulation on the wealth-creating private sector of the economy. Unless this fundamental truth is recognized, other measures aimed at reducing unemployment will be ineffectual and Europe will be doomed to suffer the scourge of unemployment indefinitely.

2. The Commission documents

2.1 The Commission proposed a new and comprehensive view of taxation policy in its reflection document 'Taxation in the European Union' dated 20 March 1996. In particular, it highlighted the major challenges facing the Union; the need to create growth and employment, to stabilize fiscal systems and to fully realize the Single Market.

*2.1.1 At the informal ECOFIN Council Meeting in **Verona** on 13 April, Finance Ministers welcomed the Commission paper and agreed on the need to take forward consideration of these issues in a **High Level Group**, to be set up and coordinated by the Commission.*

2.1.2 *This High Level group met four times; the Council's Secretariat was also present at the meetings.*

2.2 *In its 'Report on the Development of Tax Systems' dated 22 October 1996 the Commission sets out its conclusions drawn from the four meetings of the Group on the issues raised by its Verona document, gives its own assessment of these issues and indicates what it sees as the way forward for the future.*

2.2.1 *The Commission emphasizes that any proposal for Community action in taxation must take full account of the principles of subsidiarity and proportionality. It does not seek harmonization of taxation systems for harmonization's sake.*

2.2.1.1 ***The High Level Group generally gave little support to minimum corporation tax rates or bases at this stage, even within the framework of the overall objective of ensuring some minimum degree of effective taxation within the Union.***

2.2.2 *It is felt that better cooperation at Community level requires the setting up of a permanent group where Member States and the Commission can share information on, and review, taxation policies. Such a group, chaired by the Commission, could be used to provide a strategic overview of taxation policies and of the work of the existing specialized committees. It would be tasked with helping to identify key initiatives, whether legislative or not, which could contribute to the realization of essential EU objectives while preserving the Member States' tax collecting capacities*

2.2.3 *Sharing information more closely on policies and measures in other Member States should enable the group to address the question of tax competition. To that effect, the Commission will take forward a number of initiatives directed at :*

- securing broad agreement on what types of measure are harmful in a Community context;*
- defining common standards across a range of areas (a 'code of good conduct');*
- introducing greater coordination of tax measures taken by the taxation authorities of Member States which are designed to prevent tax competition from harming the common interest; and,*
- reinforcing cooperation between tax authorities in the mutual fight against tax fraud evasion.*

2.2.4 *The group could also examine the major policy implications of certain specific issues, such as :*

- the role, functioning and possible coordination of double taxation treaties;*
- the simplification of the tax environment for SMEs and other businesses;*
- the interaction of taxes and social security contributions, in particular for cross-border workers; and,*
- the taxation of international services and the impact of new technologies.*

2.2.5 *There is also a need for further work on the interaction between taxation and shared Community goals, such as enterprise, employment and the environment.*

2.2.5.1 *The Commission document recognizes that **enterprise** is an essential force for the creation of growth, prosperity and employment within the Union. Creating an environment which enables enterprise to flourish is vitally important to maintain and enhance the Union's competitiveness world-wide. The Single Market is central to this; taxation is seen as one of the most important areas in which the Single Market has not been fully achieved. Tax systems must allow cross-border economic activity to develop within the Union; at the same time, they must ensure that neither double taxation nor tax evasion result.*

2.2.5.2 To promote **employment**, there is widespread agreement on the need to reverse the trend in taxation structures towards an increasing burden on labour compared to other tax bases. The Commission underlines that, in accordance with the principle of subsidiarity, Member States should have flexibility in choosing the method of reducing taxes on labour and the means of financing those reductions. For the longer term, the Commission believes that there are great benefits to be gained in coordinating tax measures and presenting them as part of a Community-wide effort to reduce unemployment. It also considers that it is crucial to persuade economic agents that tax structures will be geared towards promoting employment from now on. There is a need to create the right environment for job creation by reducing the tax burden overall, including for businesses.

2.2.5.3 For the **environment**, the Commission acknowledges the need to explore an increased use of energy and environmentally-related taxes but current practice shows that environmental objectives are often best achieved when taxation instruments are combined with other measures, used consistently to change behaviour. In deciding the choice of instruments, the effects on competitiveness, on employment and on the environment should be carefully assessed.

2.2.6 Given that SMEs are the dominant source of new jobs in the Union, taxation policies should also facilitate and sustain their employment creating capacity.

2.2.7 The Commission advocates the introduction of a minimum withholding tax along the lines of its 1989 proposal as a first step in the regularization of the taxation of income from savings.

2.2.8 Even in the absence of new legislation on taxation, an increasing number of cases is coming before the courts, both nationally and to the European Court of Justice. There is concern that, unless Court judgements are supplemented by other instruments, the development of Community tax systems risks being piecemeal.

2.2.9 Bearing in mind the analysis and the lines of action outlined above, the Commission considers that there is a pressing need to make progress, both with regard to individual issues and to the broad direction of tax policies.

3. General comments

3.1 The Committee agrees with the broad thrust of the Commission's proposals.

3.2 In many EU countries the taxes on labour are high, representing around 23.5% of GDP for the EU average. This figure is higher than in, for example, the USA (19.4%) or Japan (16.6%). Within the EU itself, there are large differences; figures range from 14% in Greece to 32% in Sweden.

3.2.1 It is disingenuous to pretend that increases in the taxes on labour, whether they are borne by the employer or the employee, are not inimical to the prospects for employment.

3.2.1.1 To the extent that they are levied on the employer, they increase the cost of employing labour and reduce the demand. By the same token, attempts to 'protect' employment by increasing the cost to employers of releasing workers (which is, in effect, another form of taxation on employment since the payments made by the employer are, in part, a substitution for payments which the State would otherwise have to make) have the effect of making employers more reluctant to engage workers in the first place.

3.2.1.2 Where taxes on labour fall on employees, they have the effect of reducing their net disposable income and, therefore, their purchasing power. They are also inflationary, in that they stimulate demands for higher wages to offset the reduction in the workers' standard of living; if the increased wages are not matched by a commensurate increase in productivity, this pushes up the employer's costs, reduces the competitiveness of the business and further undermines economic growth and the prospects for employment.

3.2.2 *The ESC therefore concludes that a reduction in the taxes on labour, whether levied on the employee or the employer, would make an important and positive contribution to reducing the current levels of unemployment in the EU.*

3.2.3 *This contribution would, however, be severely diminished if the reduction in taxes on labour were merely transferred to other forms of corporate taxation. A reduction in the overall burden of direct personal taxation and the taxation of enterprises is required in order to stimulate economic growth and create increased demand for labour.*

3.2.3.1 *In particular, the ESC is opposed to the introduction of new taxes on information technology, such as an Internet tax or a bit tax, or on financial services (a Tobin tax).*

3.2.3.2 *The former would be tantamount to a taxation on learning and would severely hamper attempts by the EU to catch up with the level of technological advancement already achieved by other leading nations; at a time when the governments of other countries are spending billions of dollars to promote computer literacy in their populations, it makes no sense for the EU to consider handicapping its own citizens by taxing the means of their knowledge acquisition.*

3.2.3.3 *A Tobin tax would risk damaging the competitiveness of the EU nations in the global financial markets and would drive many of these operations off-shore, with a consequent loss of jobs and international financial expertise.*

3.3 *There are various reasons for wishing to harmonize taxes, some good and some bad. A desire for uniformity just for its own sake is a **bad** reason. The ESC is therefore pleased to note that the Commission has no desire to harmonize for harmonization's sake and that it embraces the principles of subsidiarity and proportionality.*

3.3.1 *Whilst it accepts that the ultimate harmonization of taxes is a legitimate aim, and an inevitable concomitant of economic and monetary union, the ESC advocates a cautious approach. As long as individual Member States continue to exhibit different economic patterns and varying economic performance the governments of each individual state must have the freedom to adjust their fiscal policies to meet the budgetary requirements of their national economies. A strategy which is right for, say, Germany at any given moment may not be right for Portugal at the same time or, indeed, for Germany at some other time. It will require a much closer degree of convergence between national economies than that stipulated by the Maastricht Treaty before Member States can harmonize their tax rates and even that limited degree of convergence is still far from being achieved.*

3.3.2 *In any case, harmonization of tax rates is a pointless exercise without also harmonizing tax bases, structures, systems, rules and interpretation. Indeed, uniform rates without uniform application may increase distortions rather than reducing them.*

3.3.3 *In the context of the Single Market, differences in interpretation and application between various tax regimes and variations in the tax base constitute a much greater impediment to cross-border trade and the completion of the Single Market than rate differentials.*

3.3.3.1 *Tax differentials are perfectly compatible with free open markets. In the USA, Canada and Switzerland, companies and individuals are taxed both by the Federal governments and by the individual states, provinces and cantons at widely varying effective total rates.*

3.3.3.2 *Within the overall objective of reducing the burden of taxation, the ESC considers that a measure of harmonization would be beneficial and feels that efforts at harmonization should be concentrated on the removal of identified obstacles to the creation of a true Single Market, particularly in the fields of VAT and*

company taxation, reducing the compliance costs for tax-payers of all types of tax, protecting cross-border transactions from the effects of jurisdictional battles between revenue authorities and removing the discrimination against companies earning profits abroad which is caused by unrelieved imputation taxes. Once these measures had been achieved, it would be possible to obtain a much clearer view of the need and the scope for further levels of harmonization.

3.3.3.3 The ESC therefore endorses the Commission's proposals for the setting up of a permanent group to deal with the issues set out in the Commission document. It considers that the areas which offer the greatest scope for making substantial progress in the short term are the defining of common standards, achieving greater coordination of tax regimes, improved cooperation in the fight against tax fraud, the simplification of the tax environment and the working of double-taxation treaties. The ESC believes that, taken together, these issues constitute an agenda which could make real progress in bringing closer the realization of the Single Market.

3.4 The ESC endorses the High Level Group's refusal to propose the imposition of minimum corporation tax rates or bases at this stage. Any European tax policy cannot be conceived in isolation but must take account of world-wide policies and trends. Those who seek to impose minimum tax rates in the EU ignore this reality.

3.5 The ESC does not agree with the Commission's proposal for a minimum withholding tax on interest from savings. In its Opinion on 'Direct and Indirect Taxation'¹¹ the ESC stated that a European approach to this problem 'must respect the existing difference between the Member States as regards the taxing of income from savings (withholding tax or compulsory declaration) and should not prejudice one system to the detriment of the other.' It reiterates this position.

3.5.1 The introduction of a European standard withholding tax would result in an out-flow of capital to countries where the rates of taxation on these savings were lower and this movement could not be curtailed without the effective re-introduction of exchange controls, which would result in the marginalization of Europe in the global financial markets and would have the most seriously detrimental effect on the economic growth of the EU.

4. Conclusions

4.1 Government, in the conduct of its role in a modern economy well-developed public services, must prioritize expenditure and raise revenue. These actions inevitably place a re-distributive burden on the economy and include effects which are detrimental to encouraging faster economic growth. The ESC believes that efforts should be made to identify substantial and timely changes in areas where economic growth may be adversely affected by government actions, especially in taxation policies, without jeopardizing that level of social protection which is a hallmark of the European social model.

4.1.1 The ESC believes that, unless this can be achieved, the economic performance of the EU against its major world competitors, such as the USA, Japan and the emerging nations of the Pacific Rim, would continue to decline and that this decline would not only frustrate the desire to extend and improve the European social model but would imperil the maintenance of the levels of social protection which currently exist. It could also lead to further increases rather than a reduction in the level of European unemployment and the social tensions which this would create might well be greater than the fabric of European unity could withstand.

*4.1.2 The ESC does not, therefore, see any dangers arising from rate reductions per se provided that measures are taken to avoid the distortions created by unfair competition. In fact, experience in different tax regimes across the world demonstrates quite clearly that, paradoxically, the total tax **yield** increases as tax **rates** fall, particularly in respect of corporate tax and personal income tax, and that the maximum yield from these taxes is achieved at an effective rate of about 18%.*

4.1.3 The arguments for imposing minimum tax rates and withholding taxes within the EU ignore the fact that this would simply drive business away to the many prosperous and expanding countries not hampered by such restrictions. As a result, they would continue to expand and grow increasingly prosperous while the EU contracted and became progressively more impoverished in comparison with them.

4.2 The ESC feels that a progressive, market-led move towards converging tax rates and bases, taking into account the different revenue-raising requirements of individual Member States, is likely to be more effective than an imposed one. A certain harmonization of tax systems and structures is a desirable aim.

4.3 Reforms to the tax system should concentrate initially on avoiding unintentional distortions to company location decisions, facilitating cross-border mergers within the EU and reducing the administrative burdens on businesses of transfer pricing and jurisdictional disputes between revenue authorities.

4.4 Small and medium-sized enterprises should be supported by reduced rates of corporate tax on their profits, within specified profit limits.

4.5 Employment creation would be most effectively enhanced by reducing the overall tax burden and by controlling or reducing public expenditure.

4.6 The ESC accepts the Commission's proposition that environmental objectives are best achieved when taxation instruments are combined with other measures that are used consistently to change behaviour and it agrees with the Commission that, in deciding on the choice of instruments, the effects on competitiveness, on employment and on the environment should be carefully assessed.

4.7 The ESC accepts the need to reduce the burden of taxation on labour but agrees with the Commission that Member States should have flexibility in determining the extent and the method of such reductions as well as the means by which they should be financed.

4.8 The introduction of new taxes on information technology or international financial markets would be severely damaging and should not be contemplated at a European level.

4.9 The ESC recommends that existing bilateral double-taxation agreements should be replaced by a single European double-taxation agreement. It would not be essential for every Member State to subscribe to such an agreement for it to work and deliver considerable benefits to taxpayers in the participating nations although, obviously, it would be preferable for this agreement to encompass the whole of the EU.

4.10 The ESC shares the Commission's concern that the development of Community tax systems should not take place in a piecemeal fashion.

4.11 The ESC supports the proposal to set up a group to improve the cooperation between tax regimes, to share information on and review tax policies, to coordinate measures against tax evasion, to identify key initiatives and to study the way forward to a more closely integrated tax system.

4.12 The ESC agrees that European taxation policy should take account of the impact on enterprise, employment and the environment."

Result of the voting:

For: 37

Against: 84

Abstentions: 17

Point 2.2.3

In the second sentence delete the words: "... such as for example, an Internet Tax, a Tobin Tax applicable to the international financial markets or a bit tax".

Reason

The three types of tax mentioned (an internet tax, a bit tax, and a Tobin tax applicable to international financial markets) would all have an undesirable distorting effect and should not be contemplated. An internet tax would inhibit the ability of Europe to keep pace with technological developments in the telecommunications field: a bit tax would be a tax on new learning techniques and would disadvantage the development of computer literacy in Europe in comparison with the rest of the world: a Tobin type tax would encourage some international financial operations to move to locations outside the EU.

Result of the voting:

For: 44

Against 90

Abstentions: 9

Point 2.2.5

Add a new sentence at the end of the first paragraph:

"However, Member States which are required to reduce their VAT rates as a result of harmonization would not have this opportunity and would have to raise other taxes in order to make good the lost revenue."

Reason

The present text is unbalanced in that it does not take into account the problems of those Member States which would have to reduce some VAT rates.

Result of the voting:

For: 40

Against: 87

Abstentions: 16

Point 5.2.3

Delete point 5.2.3 and the Appendix 2.

Reason

It is too late to propose Treaty changes since the Intergovernmental Conference is now over. Such proposals are therefore now irrelevant.

This paragraph and the appendix extend the remit of the opinion outside the scope of the documents which are being examined. The appendix raises issues which could need to be considered more carefully against a wider remit.

Result of the voting:

For: 50

Against: 59

Abstentions: 22

- ¹ Opinion of the Economic and Social Committee of 20 December 1995, rapporteur **Mr Janssen**, OJ No. C 82 of 19 March 1996.
- ² Opinion adopted on 9 July 1997, rapporteur **Mr Walker**, CES 774/97.
- ³ Growth, competitiveness and employment - Commission White Paper (COM(93) 700 final).
- ⁴ **James Tobin**, A proposal for international monetary reform, The Eastern Economic Journal 4 (3-4), July/October 1978, pp. 153-159.
- ⁵ Proposal for a Council Directive on Restructuring the Community framework for the taxation of energy products (COM(97) 30 final - 97/0111 CNS).
- ⁶ See footnote 2.
- ⁷ See footnote 1.
- ⁸ Source: German federal finance ministry, quoted from press reports.
- ⁹ See footnote 1.
- ¹⁰ See footnote 1.
- ¹¹ Opinion of the Economic and Social Committee of 20 December 1995, rapporteur **Mr Janssen**, OJ No C 82 of 19 March 1996.

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CES 773/97 Appendix 1 D/NT/as .../...

CES 773/97 Appendix 2 D/NT/as .../...

CES 773/97 Appendix 3 D/NT/as .../...