ERT

Expert Paper

Principles for a competitive Europe in the field of taxation

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Introduction

The European Round Table for Industry (ERT) strongly supports fair tax competition and shares the objective of fighting tax fraud and evasion. European tax policies should stimulate investment, innovation, growth and the creation of high-skilled jobs, thus preserving and strengthening the global competitiveness of European companies. Paying taxes is one of our contributions to society. It is also important to keep the broader perspective: European companies generate growth, create jobs, drive forward technological change and innovation and foster prosperity for citizens and society.

1. Recovery through growth

The massive shock of the COVID-19 pandemic in combination with measures taken to contain it has plunged the European economy into the deepest recession since the Second World War. Despite the extraordinary efforts of national governments and the EU Institutions to support businesses, the European economy faces unprecedented consequences. The immediate response to the social and economic challenges resulting from the COVID-19 crisis is key to put Europe back on a sustainable growth path.

ERT therefore strongly and publicly supported the European Commission's recovery plan, "Next Generation EU" (NGEU),[1] aiming at sustainable, long-term economic growth, based on a green transition and a digital transformation to overcome the crisis. High investment is needed to empower European companies to be a major engine of economic recovery, prosperity, sustainable growth and the creation of jobs.

ERT strongly believes that economic recovery will only be stable and sustainable in case it is financed in a balanced way. EU institutions may be looking into new ways of raising revenues, but it is necessary to consider that the whole private sector's contribution to the economic recovery is essential to revitalise the European economy, and it should therefore not be disincentivised.

ERT supports stable, transparent, efficient, fair and predictable tax regimes that incentivise innovation, long-term investment, job creation and economic growth. All proposals on the taxation system in the EU should be based on a sound economic analysis of the consequences of such reforms and adopted with proper impact assessments. Tax should be paid once. Double taxation on the same activity by different jurisdictions as well as additional paperwork should be avoided.

An indiscriminate introduction of additional taxes and levies could place an additional financial and administrative burden on companies, possibly chilling private sector investment over the years to come. The entirety of the planned tax measures[2] could have potentially a detrimental effect on the overarching political objective to foster private investments and to empower the European industry to be the major engine of sustainable economic growth. On the other hand, measures (such as R&D tax incentives) that directly and immediately stimulate investment in infrastructure and jobs can also have a significant multiplier effect.

This is why we encourage the European Commission and the EU Member States to work towards creating more efficient, fair and predictable tax systems and to ease the administrative burden on companies. Also, a renewed focus on removing existing tax obstacles to intra-European economic activities could allow the European Union to accelerate post-pandemic growth.

Finally, ensuring efficient compliance processes, including through tax administration making increased use of digital technologies, would provide an additional boost to competitiveness in the EU.

1 ERT, 10 June 2020, public statement on "European industrial leaders support the Next Generation EU recovery plan": https://ert.eu/documents/european-industrial-leaders-support-the-next-generation-eu-recovery-plan/.

2 To help finance the economic recovery in the EU, new own resources are being considered to complement Member States' contributions to the EU budget. The interinstitutional agreement on budgetary matters between Parliament, Council and Commission includes a detailed roadmap for the introduction of new own resources, on top of the contribution based on plastic waste, by 2026.

The Commission intends to put forward proposals by June 2021 on sources of revenue including:

- a carbon border adjustment mechanism
- a digital levy
- an own resource based on the EU emissions trading system

Furthermore, the Commission has announced it intends to propose new sources of revenue, during the course of its mandate until 2024 such as:

- a Financial Transaction Tax
- a new common corporate tax base
- a financial contribution linked to the corporate sector

2. Principles for reform

ERT very much supports the Commission's desire to 'build back better'. An important pillar to that objective is a tax regime that supports not only growth but also technological innovation and research. Accelerated depreciation allowances, 'above the line' tax credits, direct grants and incentives across the EU would not only support investment in infrastructure and jobs but help establish the EU as a robust and sustainable hub for innovation and support both start-ups and long-term investment projects which otherwise are not helped by simple tax deductions on profits.

Overall, ERT wishes to encourage the Commission to improve the competitiveness of the EU fiscal system and work towards the following policy targets:

- **Efficient and predictable tax systems**
  Business needs simple, efficient, predictable and stable tax regimes that incentivise long-term investment. Laws must be applied consistently, creating a level playing field for all. ERT supports the Base Erosion and Profit Shifting (BEPS) principle that tax is paid where value is created. Tax should be paid once, avoiding double taxation on the same activity by different jurisdictions as well as additional paperwork.

- **Improving tax administration**
  Business encourages the EU to focus on improving tax administration. The EU should avoid imposing undue administrative burdens on its companies in comparison to other jurisdictions but rather focus on removing administrative obstacles. If the EU considers that new tax measures are needed to keep up with changes in the economy, then these measures must go in sync with drastic changes to existing rules, such as the anti-abuse rules, dispute resolution, and other measures to protect and improve the fiscal climate in the EU.

- **Supporting innovation**
  Aspects of the tax system that encourage and reward technological innovation, such as accelerated capital depreciation allowances, and 'above the line' payable tax credits for R&D, can help grow the European economy and build a robust and sustainable base for the future. ERT encourages the Commission to come up with policy initiatives towards providing R&D incentives including a tax credit.

  To ensure the competitiveness of the EU fiscal system, a new set of rules on R&D tax incentives should be designed for a large scope of innovations (e.g. digital technology, artificial intelligence, etc.). A comprehensive tax credit system for more research and development in Europe would thus be a first important step towards becoming a leading and competitive innovation location.

  Such a comprehensive European approach to R&D incentives, which takes into account that the EU Member States have different economic structures, would encourage innovation, promote European start-ups and, as a result, foster growth in Europe overall.

- **Efficient tax policy development and governance**
  ERT wishes to encourage the Commission to coordinate tax policy development and take maximum advantage of the expertise and governance available at DG TAXUD. Tax rules need to be conceived, impact assessed and designed appropriately and aligned. Especially considering the specific expertise required, as well as the requirement of consensus and unanimity, it is not helpful for multiple tax rules to be proposed by various parts of the European Commission. As always, business is very willing to participate in the necessary assessments and share considerations to work with the Commission experts in developing efficient and predictable tax systems.

3. Tax efficiency and digitalisation

Any tax measures have the potential to add huge complexity for taxpayers fulfilling reporting and compliance requirements. Hence, it is crucial that the European Commission ensures that any new tax measures improve ease of administration for both taxpayers and tax administrations.

Ensuring efficient compliance processes provides an additional boost to competitiveness in the EU. Digital technology can be a useful tool to reduce the administrative burden of EU companies. However, it needs a well-coordinated approach in the EU to ensure that EU companies can benefit from these advancements.

Observations:

- Many tax administrations, as well as businesses, are undergoing a global revolution in tax compliance as they seek to digitalise their processes to enhance efficiency and effectiveness. This is creating interesting dynamics where complex business systems and processes need to adapt to information and communications technology systems designed by the public sector.

- The use of modern technology plays an important role to safeguard revenues and gain efficiencies for both tax administrations and businesses. However, it will only help achieve the desired efficiency gains if the use of modern technology is embedded in a broader regulatory and administrative compliance strategy for the maximum benefit of all stakeholders.

- Whilst digitalisation has the potential to reduce the administrative burden on companies while increasing the effectiveness of tax administration controls, this potential will not be fully realised with the current level of diversity of approaches among jurisdictions and law enforcement agencies and without a consistent legal, administrative and technological global framework.

- 'Continuous transaction controls' (CTCs) are an example of systems that enable law enforcement agencies such as tax administrations, to harvest data associated with business activities that are relevant to the exercise of their function. Such data is obtained directly from business transaction processing and/or data management systems, in real-time or near-real-time. It is important to address the risks and substantive costs to companies – engendering broader economic implications – due to a lack of coordination among the governments issuing such continuous transaction control platforms.

Recommendations:

- The use of technology has a positive impact on trade. It also advances the common goal of reducing tax burdens on business while also facilitating tax collection by countries. It is essential to develop a set of Practice Principles to promote consistency and compatibility of CTC processes across national borders, and different parts of every country's public sector that wish to adopt CTCs.

- It is recommended, given the increasing trend of transaction-based reporting using technology, to address this topic, to promote harmonisation of practices and approaches to reduce tax burdens on business and increase the efficiency of digitalisation for tax administrations.

- Another example of more efficiency by the means of digitalisation is the Standard Audit File for Tax (SAF-T). This is an international standard for the electronic exchange of reliable accounting data from organisations to a national tax authority or external auditors. The objective is to enable businesses and accounting software to create a SAF-T, containing reliable transaction data from systems that cover a specific period and which is easily readable by its standardisation of layout and format.

- SAF-T advances efficient and effective audits by internal and external auditors and by revenue bodies. It also enables companies to better automate digital processes such as tax declarations, promotes better archiving measures for companies and leads to fewer tax inquiries. Once fully implemented across Europe, SAF-T is likely to reduce the cost to the company and the tax authorities (with one standard reporting file instead of multiple local filings, each in its format).

4. Specific tax measures under development by the European Commission

4.1. Digital levy

- Digitalisation encompasses any economic activity involving the movement of information, services and products. Differentiating between digitised and non-digitised business models for tax purposes is practically impossible.

- Any policy initiative on the digital economy must be globally aligned at OECD level with principles of international taxation to avoid any undue burden on companies and consumers. The OECD Inclusive Framework addresses the tax challenges arising from the digitalisation of the economy and prevents uncoordinated unilateral tax measures.

- If a digital levy were to be applied on turnover, it would break with the international convention of taxing company profits, instead of revenue. More than profit taxation, turnover taxation risks significant economic double taxation, not just with other similar sorts of taxation, but also with regular corporate taxation as well as consumption taxes. Adding such additional forms of taxation inevitably leads to additional administrative burdens for both the taxpayer and tax authorities.

- A digital equalisation levy would lead to an elaborate introduction of an additional tax system within the already complex international tax environment and lead to high uncertainty for all its stakeholders. A common framework for any emerging proposals must be ensured to gain legal certainty around multilateral tax initiatives.

4.2. A new common consolidated corporate tax base (CCCTB)

- A new Common Consolidated Corporate Tax Base (CCCTB) should refocus on dealing with obstacles to developing and accessing the European market. It should aim to encourage European companies to expand into new markets within the EU by allowing consolidation of profits and losses they make in the different Member States.

- A CCCTB could simplify tax management for European companies currently dealing with 27 different corporate tax systems, through the introduction of a one-stop-shop, thus reducing compliance costs. Amongst other, the one-stop-shop would have companies file one single tax return in their headquarter country. At the same time, legal certainty for European companies will increase.

- The introduction of a Common Corporate Tax Base (CCTB) without the benefits of consolidation and a one-stop-shop, delivered via improved elements of the proposed CCCTB, would not achieve the desired EU tax policy goals. Any two-step approach is likely to further disadvantage EU businesses in the first phase and, in the end, may not lead to the second step in regulation by Member States (i.e. allowing consolidation) or even postpone it to an indefinite future. Without full consolidation, the CCTB would entail too many inherent disadvantages that would outweigh the potential benefits from a common tax base.

- Significant adjustments are required to make the CCTB a realistic framework for companies wishing to invest in Europe, especially while other major economies are currently finding ways to make their fiscal regimes more attractive for investments. The CCTB should include the principles of consolidation and the one-stop-shop from the outset.

- Work currently ongoing at the OECD dealing with the tax challenges of the digitalisation of the economy could provide helpful indications for adjustments. Simplification in determining a common tax base would be achieved if there was a single accounting base for legal entities as it is the case for group financial reporting of listed entities (e.g. IFRS). Immediate elimination of double taxation shall also be granted in case of a tax reassessment in one Member State.

4.3. A financial transaction tax (FTT)

Putting in place an EU-wide financial transaction tax risks increasing the cost of raising finance for investment in the EU and would put an additional burden on the 'trading place EU'. An FTT would impact strongly on the real economy since a large part would be passed on as transactional costs and thus be borne by companies in the course of their operations including:

- An increase in transaction costs due to the FTT may lower market liquidity for equity, corporate bonds and commodities especially if derivatives and/or corporate bonds are in the scope of the tax and may therefore minimise the frequency of financial transactions.

- An increase in the cost of hedging financial risks (e.g. interest rates, commodity prices, exchange rates) incurred by MNEs as part of their operational activities if derivatives fall under the scope of the tax. The same would apply for cash management.

- In a context of increased prudential requirements which lead companies to use markets more to fund, such a tax would have many negative effects, particularly concerning their financing costs and the need to finance their long-term investments.

- The tax would also increase the costs for the management of company-owned pension funds, thus reducing the payable rent for employees, the same would apply for and employee share programs.

4.4. A carbon border adjustment mechanism (CBAM)[3]

- Reducing greenhouse gas emissions requires a global level playing field for European companies, in a particular industry, ideally via harmonised carbon pricing at least at the G20 level. However, in the absence of a global carbon price, measures that complement existing carbon leakage prevention instruments, such as a Carbon Border Adjustment Mechanism (CBAM) or alternative instruments are required to ensure that non-EU producers bear the same carbon costs.

- Carbon Border Adjustment Measures could become part of the mix of relevant instruments, under certain conditions, and after a pilot phase, following an extensive analysis of sector specificities/value chains, its impact on European exports and a full assessment of potential trade risks. Implementation pathways of such measures vary between sectors and can be effective under certain conditions:

  - Provide a predictable and gradual transition from the current carbon leakage protection measures (i.e. ensuring complementarity with EU ETS) to avoid price instability until the new measures have proven their effectiveness.

  - Ensure competitiveness of both European imports and exports.

  - Impose a carbon price on imports as close as possible to the real embedded cost for European producers to ensure WTO compliance, taking into account free allocations and compensation for indirect costs.

  - Follow a sectoral approach and detail the complex implementation mechanisms for all sectors and products in scope only after a pilot phase in some primary products, followed by extensive analysis and consultation.

  - Conduct a thorough analysis and evaluation of its potential implications across the value chain and its impact, also indirect, on all economic sectors, beyond the products and sectors directly targeted.

  - A well-designed Carbon Border Adjustment Mechanism could be a suitable tool for those sectors where it can be implemented pragmatically for emissions-intensive and/or trade-exposed sectors (e.g. cement, steel, refining, engineered wood, glass), notwithstanding the potential risk of trade retaliation, or exports viability.

  - Such mechanisms can help EU-based manufacturing to compete fairly on European and international markets with non-EU products that do not have equivalent carbon costs. Furthermore, for some sectors, they form an essential policy tool to build the 'low-carbon business case' in the long run and secure continued investments in low carbon technologies across European assets.

3 The messages are based on the ERT flagship paper "Making the most of Europe's climate leadership" which was released on 10 December 2020: https://ert.eu/documents/climate-leadership/. ERT Members voice their support for EU climate goals and share ideas to empower the transition.

The European Round Table for Industry (ERT) is a forum that brings together around 60 Chief Executives and Chairs of leading multinational companies of European parentage, covering a wide range of industrial and technological sectors. ERT strives for a strong, open and competitive Europe, with the EU and its Single Market as a driver for inclusive growth and sustainable prosperity. Companies of ERT Members have combined revenues exceeding €2 trillion, providing direct jobs to around 5 million people worldwide - of which half are in Europe - and sustaining millions of indirect jobs. They invest more than €60 billion annually in R&D, largely in Europe.

This paper was developed in the Working Group on Finance & Tax of the European Round Table for Industry.

More info and previous papers on: https://ert.eu/focus-areas/finance-and-taxation/

Contact: Philippe Adriaenssens (philippe.adriaenssens@ert.eu)

+32 2 534 31 00
contact@ert.eu
www.ert.eu
@ert_eu

Boulevard Brand Whitlocklaan 165
1200 Brussels, Belgium