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Editorial

State of tax affairs in the European Union

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Ireland assumed the role of Presidency of the European Union on 1 January 2004. For my part that means that as Presidency of the ECOFIN Council I have to take charge of the varied and often pressing agendas of all matters pertaining to economic and financial dossiers. This agenda is very broad; however, I will concentrate my thoughts in this editorial to matters of taxation. Before reflecting on the '*State of Tax Affairs in the EU*' I think that it is important to briefly set out the programme of work that Ireland set itself in the field of taxation.

Direct Taxation

In the direct taxation area, the Irish Presidency is working with other Member States to resolve outstanding issues in key direct tax matters. The EU set itself a target of mid 2004 for the satisfactory conclusion of the necessary arrangements with certain third countries in relation to the EU Taxation of Savings Directive. We hope to be in a position by the end of our tenure as Presidency to report to the Council that all the remaining obstacles have been removed so that all Member States will be in a position to apply the provisions of the Taxation of Savings Directive from 1 January 2005 as was previously agreed by Council. As readers of this journal will, no doubt, be aware, the taxation of savings Directive is a complex dossier and has been the subject of prolonged and often difficult negotiations over the last decade and a half. The Presidency is supporting the Commission in its ongoing negotiations with the third countries on this important tax dossier.

Ireland has long been an advocate of addressing specific obstacles to the functioning of the single market. In this regard, we are hopeful that we can make substantial progress on the proposal to amend the Mergers Directive during our six months. That proposal is designed to modernise and update the original Mergers Directive, which had been previously agreed during an earlier Irish Presidency.

Another area of work that we are focusing our resources on is the proposal to amend the 2003 Interest and Royalties Directive. That Directive eliminates withholding taxes on cross-border interest and royalty payments between associated companies and branches in different Member States. The proposal amends the Directive to ensure that interest and royalty payments are subject to tax once in a Member State and enlarges the list of companies that can benefit from the Directive.

Finally in the area of direct taxation, as Presidency we will of course continue to play our part in the ongoing work of the Code of Conduct Group. That Group is currently involved in the analysis of both the rollback of existing identified harmful corporate tax measures, as well as monitoring 'standstill', i.e. the non-introduction of any new potentially harmful measures by the Member States. Going forward, this Group will also have to take cognisance of the regimes of the ten Accession States which will become members on 1 May 2004.

Indirect Taxation

With regard to indirect taxation, the Irish Presidency is currently progressing four dossiers, two in relation to VAT and two in the area of excises.

The first VAT item concerns a proposal from the European Commission for a Council Directive changing the place of supply rules for services for VAT purposes. The proposal, if adopted, shifts the place of taxation in most cases from where the supplier is established or has a fixed place of business (which is the current position) to the place where the business customer is located. The present arrangements are administratively complex and may lead to distortions of competition and double or non-taxation of international supplies of services. It is hoped that we can make progress on this issue during our six months and achieve a more rational system of taxation.

The second VAT item relates to VAT reduced rates – this is not a new issue. Consideration of this issue resumed at ECOFIN in January following discussions during the Italian Presidency on a European Commission proposal presented in July 2003. Agreement was not possible on the Commission proposal which sought substantial changes to VAT rating structures. The Irish Presidency is continuing to facilitate further discussion on the matter at working group level with a view to further discussion at ECOFIN later on during our presidency.

On 1 May 2004, we will welcome 10 new countries as full participating members of the EU. In order to be in a position to do that much work has been under way for some time now both by the Accession States and also by the existing 15 Member States. For instance, we are currently progressing an amending directive to the Taxation of Energy Products Directive agreed last year and which is intended to provide for certain transitional derogations (from applying the EU minimum tax rates) for the Accession States. The intention is to have this proposal agreed by the 1 May, 2004 accession deadline.

The Presidency is also advancing discussions on a proposal for a Council Regulation on Excise Administrative Cooperation. This proposal is intended to combine the general principles and specific provisions for administrative cooperation in the excise area and also to develop the existing provisions so that they are adequate for the present excise context.

Significant progress has been made to date and the Presidency is also prepared to look at any additional proposals that may emerge from the Commission between now and the end of June.

Debate on Corporate Taxation

Turning now to the issue of the 'state' of the debate in the European Union, I believe that when it comes to matters of taxation, we always have, at ECOFIN, a vibrant and often vigorous debate, as it should be.

One subject on which there has been much debate in recent years is the area of corporate taxation. The European Commission has issued Communications in the area over the last number of years and there have been a number of important conferences discussing such matters. In their 2001 Communication, the Commission set out its twin track approach of (i) the identification of targeted solutions to specific problems and (ii) the longer term approach of a longer-term proposal for a common consolidated corporate tax base for companies for their EU-wide activities. I heartily endorse the approach of identifying targeted solutions to specific problems. As I indicated earlier, this is an area that the Irish Presidency has been and will continue to be a committed active proponent seeking to ensure that the internal market is enhanced for the good of all EU members. While I welcome the Commission view that they are not suggesting any harmonisation of rates, Ireland does not support the longer term objective of a common consolidated corporate tax base. A common consolidated corporate tax base goes beyond the idea of 'co-ordination' of EU policy in the direct tax area and is not necessary in order to tackle obstacles within the internal market. It is debatable as to whether the proposals would contribute to the simplification of the tax system and there would also be particular difficulties in attempting to find a mechanism by which profits could be allocated between the different countries on a rational, economic and fair basis. Moreover, if there is to be a single tax base, there could be a serious loss of flexibility for a Member State in the manner in which it could operate its tax system. I accept that views on this issue differ considerably among Member States and I am sure that this issue will continue to be a source of lively debate.

Role of Unanimity in Taxation Matters

An issue that has been to the fore during the last number of months is the role of unanimity in taxation matters. Some Member States have called for a move to qualified majority voting on certain taxation matters such as tackling fraud or addressing administrative taxation matters. Others, including Ireland, have argued for retention of unanimity for all taxation matters.

I believe that a debate on this matter is important, but often displays a lack of understanding by some of the importance of the retention of the fiscal policy tool at the level of the Member State. Ireland believes that, as a matter of principle, unanimity must be retained for all taxation matters. One of the key components of a State's expression of sovereignty is the right to determine the level of Government expenditure and the tax rates and structures required to support it. Taxation questions are, both historically and in the contemporary world, of profound sensitivity and touch very directly on the relationship of the citizen to the State. It is appropriate that the right to determine taxation issues continues to be held at national level.

Apart from differing choices about the level of overall taxation, the attitude as to what type of taxation is influenced by historic and cultural factors. Given Ireland's economic history and our poor level of economic prosperity for much of the early years of EU membership we have come to recognise the importance of low levels of direct taxation on employment and enterprise. That said, there is a general recognition of the need for high levels of taxation on products such as tobacco and alcohol and also on areas such as property transfer. Other countries have, for their own distinct reasons opted for a different taxation mix with higher rates of direct taxation often combined with low or no taxation on products such as alcohol. This I believe is the right of the Member State to choose whatever fiscal policy mix that is appropriate for their citizens and at the end of the day it will be a matter for the citizens to judge on the appropriateness and effectiveness of the domestic tax system. The Community as a whole has a very important role in ensuring that whatever system is pursued is fair and not harmful to other Member States.

Taxation is an issue which is close to the heart of every Finance Minister. In my stint as Irish Finance Minister since 1997, whenever the issue of taxation is on the ECOFIN Council agenda I have seen healthy debate at such Council meetings. I take heart from such debate, as I am firmly of the view that debate is a good sign. An exchange of views from various perspectives can only ensure a more rigorous assessment of proposals and more appropriate legislation for all is pursued. So in answer to the question as to the State of tax affairs in the European Union, I believe that they are very healthy and that Member States have shown a willingness to engage and strive to pursue the improvement of the functioning of the internal market.

Finally, it remains for me to acknowledge the imminent enlargement of the European Union on 1 May which will present opportunities and challenges for all. As President of the ECOFIN Council I would like to take this opportunity to welcome the Accession States to the European Union and look forward to the very many opportunities that enlargement provides both for the new and the existing members.