

## Time for a Rethink?

The objective of this brief editorial is to seek more attention for and amplify the findings of a recent study, '*Removal of taxation-based obstacles and distortions in the Single Market in order to encourage cross border investment*' (the Single Market Study) by Jost Henrich Heckemeyer.<sup>1</sup> It has received very little attention thus far perhaps because it was published mid-summer, however, it deserves much more.

I found the study, about which there is more below, a welcome relief because it focuses on strengthening the competitiveness of the European Union. While the ambition to reduce tax obstacles to the functioning of the internal market has not disappeared, during the last decade much of the EU tax policy in the sphere of direct taxation, in particular company taxation, was driven by a dominant mantra: multinational enterprises (MNE) avoid tax, do not pay their fair share, countries engage in a race to the bottom and tax advisors are part of the problem. This mantra was carried by the various scandals, including LuxLeaks, Panama Papers and Paradise Papers; and the distinction between tax evasion and tax avoidance was hardly visible, if at all. Even though the tax gap caused by the informal economy<sup>2</sup> is a multitude of that resulting from tax avoidance by MNEs, most of the attention was and still is focused on them. While that is fully understandable from a political and a policy perspective – the legitimacy of the system is at stake – a point may indeed have been reached where rethinking would be welcome. Most of the recent EU anti-avoidance rulemaking for which consensus was readily achieved and European Commission activism regarding unlawful state aid indeed resulted in a significantly narrowed space and very much reduced appetite for tax avoidance on the part of governments and taxpayers. In addition, there is the overlay of BEPS measures not embodied in EU Directives, including the PPT. The result is tax

regulation of a complexity that is without precedent, and there is no end in sight. The proposal for an EU Pillar Two directive, while the entire OECD project may be on life support,<sup>3</sup> is still pending and the somewhat overreaching proposal for a directive to address misuse of shell entities is lurking in the background as is an initiative with respect to tax enablers.

While, as noted above, the concerns that have led to seemingly endless anti-avoidance tax regulations are understandable, the question is justified whether the point in time has arrived where we no longer see the forest for the trees. It is exactly this question that presents itself when one reads the Single Market Study. The background in the executive summary reminds us that the coexistence of twenty-seven different national tax systems in the EU means significant obstacles to cross-border business activity in the European Single Market and that this is contrary to the ambition set out in the Lisbon Strategy of establishing 'the most competitive and dynamic knowledge-based economy [ ... ] in the world'.<sup>4</sup> Some of the key findings in the report are as follows:

EU Member States have found it much easier to agree on curbing international tax planning than on reducing tax and administrative barriers in the Single Market. As a consequence, leeway for international tax planning has actually decreased significantly in recent years, but at the cost of a complexity explosion.<sup>5</sup>

Additionally:

While for the last ten years the fight against tax avoidance has been high on the European policy agenda, the avoidance of double taxation as well as the efficient implementation of EU law prohibiting

### Notes

<sup>1</sup> Study requested by the FISC Subcommittee of the European Parliament performed by the Policy Department for Economic, Scientific and Quality of Life Policies, Directorate-General for Internal Policies, PE 733.964 – Jul. 2022.

<sup>2</sup> See <https://www.imf.org/Publications/fandd/issues/2020/12/what-is-the-informal-economy-basics> (accessed 23 Sep. 2022). See also my Intertax editorial, *Digitalization in a Broader Tax Perspective*, Intertax 533–534 (2021), and literature referenced in that Editorial.

<sup>3</sup> See Mindy Herzfeldt, *Looking Past the Crumbling Pillars*, Tax Notes International (8 Aug. 2022).

<sup>4</sup> See *supra* n. 1, at 9.

<sup>5</sup> *Ibid.*

discrimination and restriction of cross border activity have been less of a concern to the legislator.<sup>6</sup>

Finally, the last citation from the Single Market Study:

Going forward, the EU must position itself in the global competition. The US tax policy has long been characterized by a greater awareness of the realities of international tax competition, providing also carrots and not only the stick for the investors. In contrast, the EU stands out globally with a high-speed strategy that almost exclusively centers on the fight against tax avoidance.<sup>7</sup>

Following a *tour d'horizon* of tax law integration in the EU as well as taxation-based obstacles and distortions in the single market, the study concludes with policy recommendations that include: (1) considering the wider context, i.e., the EU in global competition; (2) focusing on a harmonized corporate income tax; and (3) reducing compliance costs and double taxation risk through more efficient legislation, administration, and proceedings.

This author sincerely hopes that the study contributes to the EU policy makers take an appropriate amount of time and reflect on the current situation. As the study rightly notes, anti-avoidance measures have been adopted extremely rapidly. This has not only led to a patchwork

(that will only be made more complex upon the implementation of the proposed Pillar Two directive) of which effectiveness and efficiency have not been thoroughly examined, it may also affect the competitiveness of the EU in a world in which multilateralism retreats and fragmentation is on the rise.

As Professor Ana Paula Dourado noted in her recent editorial,<sup>8</sup> the signs of fragmentation are very evident. The inevitable scenario in the near and intermediate future is one of declining influence of the existing international institutions and multilateralism. Countries and their MNEs will have to factor in geopolitical risk and other uncertainties in organizing global value chains and thinking about resilience and competitiveness. In the context of Pillar Two, the question arises of whether it is truly in the interest of the EU Single Market to adopt the rather rigid template of the model rules at a point where adoption in certain other economically important regions in the world – and that includes the United States – is uncertain and, as the Single Market Study notes, competition may move to other tax fields.<sup>9</sup>

Stef van Weeghel

Professor of international tax law, University of Amsterdam.

Global Tax Policy Leader, PwC

Chair Board of Trustees, IBFD

Email: S.vanWeeghel@uva.nl.

## Notes

<sup>6</sup> *Ibid.*, at 10.

<sup>7</sup> *Ibid.*

<sup>8</sup> Ana Paula Dourado, *The World Split in Two and the Future of the International Tax System*, Intertax 482–483 (2022). See also *A New Age of Conflict*, The Economist (5 Mar. 2022).

<sup>9</sup> See *supra* n. 1, at 47.