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Corporate Tax Avoidance Crackdown, a Missed Opportunity for the EU Commission

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EuroPoint: In the aftermath of the Luxleaks scandal, the EU Commission is drafting legislation to crack down on corporate tax avoidance. The legislation is toothless and maintains a lack of transparency in tax dealings. This is a missed opportunity for the Commission to improve its low public trust rating.

Hundreds of years ago, friendly European powers were fighting all-out wars behind each other's backs over new overseas colonies. Pirates were at the forefront of those wars, yet pirates also served as convenient scapegoats.

Today, "friendly" EU states are engaged in a sour competition of offering multinationals lower and lower "sweetheart" tax deals. The man who encouraged a large amount of this corporate tax avoidance while serving as Finance Minister and later Prime Minister for the Grand Duchy of Luxembourg is Jean-Claude Juncker, today's EU Commission President.

Jean-Claude Juncker Passed a No-Confidence Vote in the EU Parliament Over his Role in Luxembourg's Tax Rulings

Starbucks Corporation maintains the narrative that it chose to base its regional headquarters in Amsterdam due to the city's rich history with coffee. That is odd, since the company's largest market and profit share in the region is in the UK. In reality, Starbucks received a tax ruling from the Dutch government that allowed the company to pay less than 1% tax. After the scandal broke out, Starbucks did indeed relocate their regional headquarters to the UK.

The EU is investigating such deals offered to corporations from authorities in Luxembourg (Fiat and Amazon), Ireland (Apple), the Netherlands (Starbucks), and Belgium. No less than 548 tax avoidance schemes in Luxembourg – the so called "Luxleaks" – were uncovered and published by an international consortium of investigative journalists.

Semantics

The Single Market opened the door for corporations to exploit loopholes in supranational EU legislation and mismatches between national legislation. Most corporations take advantage of the Parent –Subsidiary Directive from 1990, originally designed to avoid double taxation for multinationals with parent companies in one country and subsidiaries in another. The directive allows a tax exemption for dividends transferred between a subsidiary and its parent company in different member states. Through cross border "hybrid loan arrangements," what is defined as a debt in one country is defined as equity by another and therefore treated as a tax-deductible expense.

Accounting firms such as PricewaterhouseCoopers, Ernst&Young, Deloitte, or KPMG negotiated favorable "tax rulings" between their corporate clients and certain EU governments - assurances given in advance by tax authorities on how the tax will be calculated.

Yet a tax ruling by one state erodes the taxing rights and revenues of another state. In addition, such rulings create unfair competition between multinationals and small businesses that have to pay their full share of taxes.

The extent of tax avoidance is unknown, and the losses are impossible to calculate. To hide their tax rulings, member states invoke "sovereignty" in the tax area and "escape clauses" on grounds of protecting commercial secrecy and public policy.

Commission Fights Back, Not Hard Enough

The EU closed the hybrid loans loophole in July 2014 with an amendment to the Parent-Subsidiary Directive. In January 2015, the Council adopted an anti-abuse clause that allows member states to disregard artificial tax arrangements and hence tax corporations where the economic activity "of substance" is taking place.

The Commission is currently working on a Tax Transparency Package designed to ban governments from invoking "escape clauses." The law would mandate the 28 national tax authorities to share details on tax rulings amongst each other on a quarterly basis.

Yet the Tax Transparency Package does not go far enough. Tax rulings will not be made public. While this is a logical move given the complex approval process the legislation has to go through, it will be a missed political opportunity for the EU Commission.

This legislation comes at a time when fringe Eurosceptic parties capitalize over the financial crisis, the rich 1%, corporate abuses, and lack of transparency. The EU Commission faces a choice between giving Eurosceptics more arguments, or making tax rulings public and thus siding with the 99% in the public perception.

Trust in EU institutions is already low, at 37%. Trust in national governments is even lower, at 29%. Will citizens trust tax authorities to act righteously, given that this package does not even stipulate any penalties?

Voters will likely turn their trust to media outlets and the kind of investigative journalism that uncovered the tax rulings in the first place. Let's not forget that the Commission only started working on this package in reaction to the Luxleaks. Why not capitalize on it, mandate governments to make tax rulings public, and earn the trust of voters? How many similar legislative opportunities of this scale will the EU Commission have in the future?

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