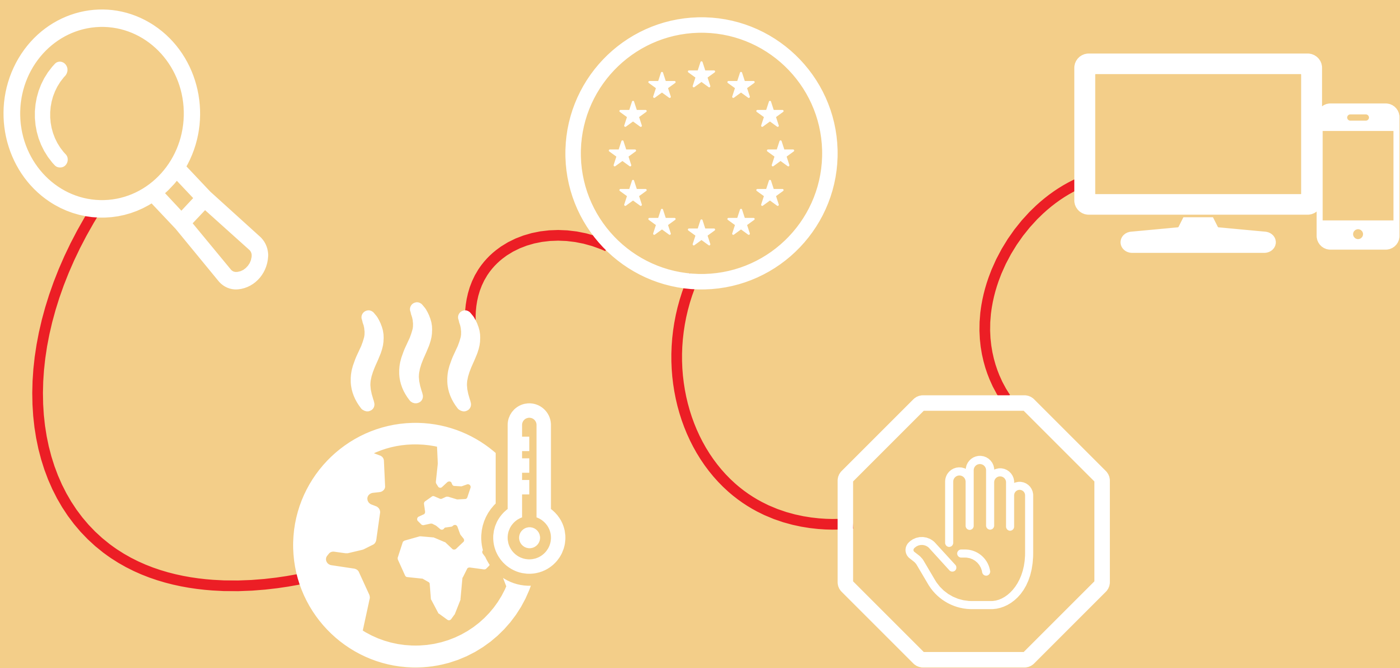
S&D

Tax justice to foster post-pandemic recovery

An S&D Roadmap



Content

Introduction

The COVID-19 pandemic breakout caused both a health and socio-economic crisis that caught the world and its leaders by surprise. As part of national responses, Member States granted tax facilities to companies and citizens. Now that the lockdown measures start being lifted, a crucial phase of the pandemic is about to debut: the recovery. The recovery should be based on a just taxation system, and it is also an opportunity to close tax loopholes and continue the fight against tax evasion and tax avoidance.

On 27 May 2020, the European Commission, following calls by the European Parliament and some EU Member States, proposed a European Recovery Plan together with a new recovery instrument, called Next Generation EU, which aim at providing resources for needed spending, reforms and investments.

That welcomed step requires the mobilisation of all possible resources, including taxes, at both national and European levels, towards a framework that fosters social and environmental sustainability.

Taxation will indeed have a crucial role in the recovery phase that is slowly starting, and must go hand-in-hand with other EU related instruments:

- It provides funding to public coffers to finance public services and investments;
- It ensures corporates which are rightfully supported during the pandemic can contribute to the recovery;
- It can have a behavioural effect that can speed up the transition towards a more sustainable economy and advance the EU Green New Deal implementation;
- It could provide for new EU own resources to allow for common projects and financing of EU priorities;
- It has a redistribution effect that can mitigate on-the-rise inequality induced by the pandemic; vulnerable people being particularly hit.

This crisis linked to the pandemic revealed once again that public services and publicly managed economic buffers are at the heart of our socio-economic resilience. The recovery phase should ensure that the EU is better prepared and equipped to guarantee its robustness, including through relevant tax reforms and coordination.

Such reforms should prevent social fragmentation in society, fight income and wealth inequality, increase transparency and allow for sustainable growth, both in environmental and socio-economic dimensions.

It should be of utmost priority for both the EU and its Member States to:

I. Halt tax competition

The recovery phase ahead of us should allow the EU to overcome the sanitary, economic and social impacts of the COVID-19 pandemic. For this to happen, the EU and its Member States will need to mobilise all resources. The recovery phase should be a phase of solidarity where cooperation will prevent any form of harmful competition. By working together and setting common ground, EU countries will prevent tax evasion and tax avoidance and restore fair competition between large and small companies, between highly globalised and digitalised firms and local businesses. Halting tax competition starts with:

- A minimum effective tax rate of 18% that could consist of a set of defensive and fair competition measures - such as an income inclusion rule, a switch-over rule, an undertaxed payments rule and a subject-to-tax rule. A first and fast step towards the establishment of a minimum effective tax rate could be to establish such a minimum rate to passive income such as interest and royalties, particularly subject to tax avoidance strategies;

- A minimal harmonisation of tax rules to simplify the administrative obligations of companies operating across the EU and to stop tax avoidance strategies exploiting differences between European legislations. A decisive step to achieve such harmonisation would be the adoption of a Common Consolidated Corporate Tax Base;

- A fairer taxation of highly digitalised companies and tech giants. The digitalisation of the economy is great progress, however it has also allowed large multinationals to easily and artificially shift profits to lower tax jurisdictions, including tax havens. A global reform is necessary to ensure all firms pay a fair share of tax where value is created and where profits are made. A crucial step towards a fairer taxation of the digitalised economy would require a strong and united EU position on the on-going global tax negotiations. The EU should pave the way with its own EU solution should no global deal be reached by the end of 2020.

II. Design a progressive environmental taxation package

Fighting climate change and achieving the Paris Agreement objectives will require colossal investments. It is therefore crucial that our tax systems adapt to this new reality to ensure the collection of extra and needed revenues and to incentivise virtuous sustainable behaviour. It is equality essential that environment-friendly tax policies participate to the needed tax shift alleviating taxes on income generated by labour. An environmental taxation package could encompass:

- A Carbon Border Adjustment Mechanism, WTO compliant that would restore fair competition between firms wherever they operate from and that would prevent both carbon leakage and reduce carbon emissions. The nature of such a mechanism that should consider the potential economic impact on different sectors, could take different forms, including being part of the EU Emissions Trading System;
- A tax on non-recycled plastics that could help achieve the European Strategy for Plastics in a Circular Economy;
- A taxation of energy that is in line with the Green Deal and Paris Agreement objectives, via a revision of the Energy Tax Directive. The revision should set ambitious targets while being accompanied by compensatory measures for the poorest households and paying attention to the particular situation of remote regions, in view of fighting against energy poverty. Such a revision would also be the first step in allowing for a kerosene tax that would tax aviation fuel at an EU minimum rate and repeal an unfair tax exemption for the aviation sector which should contribute its fair share once the progress of recovery allows for it;
- The introduction of an EU advertising tax aiming at offsetting negative externalities resulting from excessive consumption of non-sustainable goods or appliances that do not respect EU standards, for example in terms of energy products’ labelling, consumption and/or energy efficiency. The elaboration of this new concept could start through an assessment study performed by the Commission and would aim at promoting a more sustainable post-pandemic single market.

III. Develop new resources to support the recovery

Business as usual will not allow the EU and its Member States to cope with a crisis of this magnitude. The recovery phase will require the EU to be creative in bringing solutions that would allow us to overcome both the challenges brought by the pandemic and long term challenges such as climate change or the fight against income and wealth inequality.
The first step needed is for the Council and the Commission to explore and start designing new coordinated tax tools bringing additional resources, among which some could also become EU own resources such as:

- A Single Market Levy that would consist in a levy being applied on large companies who benefit the most from the possibilities offered by the Single Market. Such a levy would not disincentivise companies to operate cross border as revenues generated would allow the EU to further invest in needed services and infrastructure that also remove existing barriers;

- A European Framework to coordinate taxes on wealth and the transfer of wealth to fight tax avoidance, including a coordinated framework for inheritance taxes and a European progressive Net Wealth Tax. Both would allow for a fairer contribution from the wealthiest top 1% and address excessive accumulation of wealth that generates inequality. It would also prevent strategies to avoid paying taxes foreseen by similar schemes designed at the national level only. A progressive Net Wealth Tax, coordinated at the European level, could generate high additional revenues with a very low tax rate being applied to a rather broad base (the wealth of the top 1% representing about 22,5% of the EU total wealth)* ;

- A temporary excess profit tax that would be coordinated at European level and would consist in a higher tax rate on excess corporate profits for large multinationals, above a certain percentage of annual return. Such a calculation should be made on a global or European annual return to prevent any profit shifting strategy. By targeting companies having a higher annual return, the extra revenues collected would not harm those companies that are struggling the most while making the companies that could perform well, notably during the pandemic crisis, contribute fairly;

- A real Financial Transaction Tax, implemented by the 27 Member States, would reduce unproductive and excessive trading and participate in inequality curbing.

* Landais C., Saez E., Zucman G. 'A progressive European wealth tax to fund the European COVID response' April 2020

IV. Condition public support to virtuous tax practices

In times of crisis, great leaders understand that sometimes they must do 'whatever it takes'. This 'whatever' can, however, be an opportunity to speed up needed reforms and ensure that more virtuous practices are implemented. That means that aid should be applied in a socially, ecologically and economically sound and responsible manner. While EU countries are supporting companies in various ways, from direct State Aid to different exemptions, it is crucial for the acceptance by all EU citizens of such financial aid that the supported entities are not engaging in any tax avoidance schemes.

To promote tax practices that not only are legal but also respect the spirit of the law and a level playing field between large corporations and SMEs, the EU and notably the Commission should:

- Require the disclosure of essential financial information, including public country-by-country reporting by multinationals and essential non-financial information;
- Require that firms applying for State Aid certify that they are not involved in any reportable tax arrangement or potential harmful tax practice under EU law (DAC VI[**]);
- Condition the allocation of State Aid to the absence or the formal commitment to rapidly close subsidiaries in listed tax havens within the EU blacklist, unless real and substantial economic activity of such entity is proven by the company requesting State Aid;
- Adjust the EU public procurement rules to easily allow public buyers and local governments to exclude companies registered in tax havens or not living up to essential transparency standards from public contracts.

** Council Directive (EU) 2018/822 amending Directive 2011/16/EU ("DAC 6") as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements,

V. Reinforce the fight against tax fraud and tax avoidance

The EU, with particular impulse from the European Parliament, achieved fundamental results in the fight against tax fraud and tax avoidance in the past years, notably through the establishment of the first EU blacklist of tax havens and the automating of tax information exchange. More can now be done to boost the efforts previously initiated, such as:

- A transparent revision of both criteria and countries being assessed in the context of the blacklisting exercise. A robust EU blacklist of tax havens should notably include all EU countries in its assessment, as well as criteria allowing for the identification of jurisdictions that deliberately favour profit shifting and artificially lower the effective tax rate of companies and wealthy individuals, such as minimum effective tax rates. Such a revision should encompass a revised list of strong and harmonised counter-measures against listed tax havens;

- The automatic exchange of information has already proven its efficiency to counter tax avoidance and recover revenues. It can be further completed, notably when it comes to revenues generated via platforms.
  Transparency should, however, also be understood as the release of information that would allow decision makers, investors, journalists, civil society and citizens in general to be able to assess the risks of tax avoidance on a large scale. The adoption of public country-by-country reporting remains a political priority for whoever aims at fostering corporate responsibility on tax;

- Some tax arrangements are already known as being harmful for the collection of taxes. Identifying dodgy tax schemes, including patent boxes,freeports or golden visas, and gradually banning their use would be a determinant step towards tax justice;

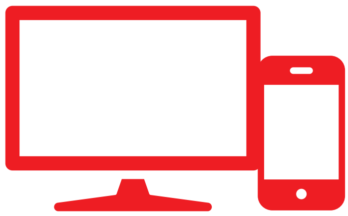
- Tax evasion is a predicate offence to money laundering and tools to enhance corporate transparency with a view to preventing money laundering, such as beneficial ownership registers, are important instruments to fight tax evasion as well. It is clear that a reform of the European Anti Money Laundering framework is urgently needed. We call for a fully harmonised framework for all EU Member States through a Regulation, a European centralised supervisory body with direct supervisory powers, as well as stronger cooperation between the national Financial Intelligence Units through a coordination and support mechanism and better instruments for judicial cooperation;

- The swift adoption of a definitive VAT system that would greatly limit the opportunities for cross border tax avoidance;

- The permanent and systematic integration of a tax analysis as part of a reformed and democratised European Semester process leading to regular accountable Country Specific Recommendations that would aim to ensure economic coherence across EU countries, as well as fairness and sustainability of EU tax systems. Such recommendations could ensure a fair balance between sources of revenues (labour, consumption, corporate, capital, etc.) and should also include innovative elements aiming at promoting the Green New Deal;

- A stronger regulation of the role of auditors, accountants and tax advisers so as to ensure they would not be facilitating certain harmful tax practices and dodgy arrangements; and instead become tax compliant facilitators.

In July 2020, the European Commission will present an ambitious package on fighting tax fraud and tax avoidance that will set some priorities for the years to come.



This package is more than timely, it is essential. 2020 could already be a year of success. No matter the outcome of the international tax negotiations led by the OECD, the EU should move forward and ensure a fairer taxation of digitalised large companies, while guaranteeing a minimum effective amount of tax is paid through a minimum effective tax rate. Also there also can be no further delay on making our tax system more fit for our environmental challenges, therefore the EU should adopt a second tax package focusing on environmental issues as from 2021. The European Parliament should support the European efforts aiming at restoring a fair tax system and it now has a permanent subcommittee on tax matters to remain active and propositional on tax justice.

The time is now. Nonetheless, any ambitious timeline would be set aside without a clear change of rules to decide on tax matters. The Conference on the Future of Europe is another opportunity to lift the unanimity rule on tax matters, which currently gives a de facto veto-right to each EU country, including Member States considered as EU tax havens. A first step could already be the activation of passerelle clauses for extending Qualified Majority Voting in files related to tax evasion and tax avoidance that are harming the functioning of the internal market. More democratic and accountable decisions on tax matters can only help the EU to deliver faster and participate fully in income and wealth inequality reduction.

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