The CCCTB is not the corporate tax reform the EU needs

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According to the Commission, the new CCCTB initiative is the most ambitious corporate tax reform ever proposed in the EU. However, despite the most noble intentions, the proposal presents a number of fundamental problems.

First of all, the CCCTB will add an extra layer of regulation to already established international frameworks to tackle tax avoidance, namely the OECD/G20 BEPS project and the EU Anti-Tax-Avoidance Directive (ATAD).

Secondly, the CCCTB undermines Member States' tax sovereignty. The fairness of their tax systems is a matter for which EU countries are pre-eminently responsible and accountable to their own people. Several countries will be hurt.

Thirdly, CCCTB will create new hurdles for enterprises as it may reduce the scope for business expansion. It is highly likely to increase internal costs and it will impose very large costs of transition into the new system.

Thus, we urge the European Parliament ECON committee to halt this corporate tax plan until more comprehensive impact studies have been released.

Introduction

On 25 October 2016, the European Commission announced a new package of corporate tax reforms. The package includes three separate legislative initiatives: a directive on a Common Consolidated Corporate Tax Base (CCCTB); a directive on Double Taxation Dispute Resolution Mechanisms in the EU; and a directive amending the so called Anti-Tax Avoidance Directive (ATAD) as regards hybrid mismatches with third countries (European Commission, 2016a).

With respect to the CCCTB directive, this is the second time the Commission has put forward this initiative. The Commission now wants to adopt a staged approach. Accordingly, the proposal has been split into two different directives, one covering a common corporate tax base (CCTB) and the other covering the CCCTB itself. By separating the establishment of a single set of rules to decide how a company's profit will be taxed from the consolidation directive, the Commission hopes to attract more consensus across Member States. However, the governments of Denmark, Ireland, Luxembourg, Malta, the Netherlands and Sweden have already filed formal objections stating that, like the 2011 proposal, this initiative does not meet the principle of subsidiarity.

In 2017, the EU average corporate tax rate equates to 21.51%, down from 27.95% in 2003. However, there is still substantial variance between Member States. Hungary reports the lowest corporate tax rate (9%), Belgium the highest (33.99%) (KPMG, 2017).

An EU-wide tax on profits is not needed to tackle tax avoidance

According to the Commission, the new CCCTB initiative is the most ambitious corporate tax reform ever proposed in the EU. The Commission claims that reforming corporate taxation in this direction will boost growth, jobs and investment all around the Union, and that it will help combat tax avoidance and provide a fairer EU-wide corporate tax system (European Commission, 2016b)

But there are important problems with the proposal. Firstly, as the Confederation of Netherlands [Dutch?] Industry and Employers (VNO-NCW, 2016) and the UK Parliament (House of Commons, 2016) report, the CCCTB will add an extra layer of regulation to already established international frameworks to tackle tax avoidance. Completed in 2015, the 15 action points developed in the context of the OECD/G20 Base Erosion and Profit Shifting (BEPS) project (OECD, 2015) have already introduced a comprehensive package of measures to monitor multinational enterprises (MNEs) corporate tax avoidance practices. Moreover, the Anti-Tax-Avoidance Directive (Council Directive (EU) 2016/1164) adopted on 12 July 2016 reflects the adoption of the BEPS scheme. Adding another EU-wide dimension to these already complex frameworks will put all European Member States at a disadvantage, especially in terms of tax competitiveness, and out of step with the international consensus (Deloitte, 2016).

Thus, the argument that the plan for a Europe-wide tax on profits is needed to tackle tax avoidance by brass-plate companies is a weak one. As a recent working paper by UNU-WIDER (Cobham and Janský, 2017) underscores, revenue losses related to tax avoidance have decreased sharply all around the world in terms of percentage of GDP since 1980. In OECD countries, these revenue losses are today close to 0%, down from 1% of GDP in 1980. Interestingly, this decline occurred in a period when corporate tax rates decreased sharply due to intense competition, whilst corporate tax revenue remained stable (Zuluaga, 2016).

The CCCTB would result in an unjustified transfer of taxing rights from small open economies to large closed ones. According to Ibec (2017) this would cost Ireland over €4 billion per annum in tax revenue (or over 7.7% of tax revenue).

A CCCTB undermines Member States' tax sovereignty

Secondly, the introduction of the proposal would require the merger of EU national legal systems and would amount to creating a new, EU-wide tax code for multinationals. This obviously undermines Member States' tax sovereignty whilst not solving the problems of transfer mispricing. As Murphy (2016) explains, the CCCTB directive is not a consolidation process in an accounting sense simply because this proposal is not based on consolidated accounts. Currently, the EU does not have a consistent accounting base and at highest level the International Financial Reporting Standards (IFRS) do not mandate the capital maintenance concept. This means that there are substantial differences in the recognition and valuation of key revenues and expenses by companies. With this in mind, it is likely that companies which operate in different Member States will incur double taxation, thus deterring investment and harming economic activity.

Whilst not directly affecting a country's corporate tax rate, all Member States will lose freedom with respect to how they define the tax base. A 2011 study by Ernst & Young (E&Y) concluded that substantial changes in country-by-country tax collections would occur (E&Y, 2011). Five countries would lose at least 5 percent of their revenues, including Denmark, the Netherlands, Ireland, Finland and Germany. Ten would gain revenues, with France, Greece, Latvia, Spain and the UK all gaining at least 2 percent. It was also found that the CCCTB system would redistribute, with Belgium, Spain and France seeing rising employment, and all the other remaining countries losing jobs. This system is also likely to rise the effective tax burden on firms, thus reducing their incentive to direct investment to its most productive uses. Adopting the CCCTB would have larger negative impacts on FDI, with seven countries experiencing FDI reductions of more than 4 percent. All of this will have important implications for how Member States raise taxes and conduct domestic policies. Thus, expect EU countries to raise or introduce new taxes to level off CCCTB-related losses.

CCCTB creates new problems for business

Thirdly, although a mandatory CCCTB may save enterprises time otherwise needed to scrutinise different rules of computing the corporate tax base, it is highly likely that a reduction in their administrative burden will be offset by an increase in internal costs due to compliance with more stringent regulation. A mandatory CCCTB will also change corporate behaviour, including where companies are set up. By requiring disclosure of sensitive information, the new directive will put EU businesses at a competitive disadvantage vis-à-vis non-EU MNEs not based in EU Member States but operating in the EU (Lithuanian Free Market Institute, 2015).

Only three EU countries (Belgium, France and Spain) will benefit in terms of GDP, FDI and employment change from the introduction of a mandatory CCCTB (E&Y 2011).

A CCCTB is also likely to discourage EU companies' growth (De Broe, 2017). By making the new rules mandatory for all groups with consolidated worldwide revenues greater than €750 million, European businesses will have an incentive not to exceed that threshold. Once that revenue is reached, companies will also lose their ability to access tax incentives such as patent or innovation boxes. As Ernst and Young (2017) warns, the costs of transitioning into the new system will be very large.

Following the introduction of the CCCTB, European businesses may see their liquidity position impaired in times of recession. This is because the introduction of an Allowance for Growth and Investment (AGI) results in additional tax relief if equity increases, but also in an increased tax assessment if equity decreases (Grilli, 2017). Moreover, as the Confederation of Netherlands Industry and Employers (VNO-NCW, 2016) explains, this means that the AGI actually serves as a penalty on making investments or distributing dividends. All of this will not increase the appeal of the investment and business climate within the EU.

Conclusion

As EPICENTER research already stressed in the past (EPICENTER 2014), European institutions should preserve the highest possible degree of tax competition between Member States. The regulation of Member States' tax base will negatively affect tax sovereignty and is likely to lead some EU countries to introduce new types of taxation. Businesses are also likely to be severely impacted by the introduction of this directive. Some of these new EU-wide rules will also collide with already established international frameworks to tackle tax avoidance. In short, CCCTB risks putting both Member States and EU companies at a disadvantage.

In light of all these technical questions, it is striking that the Commission has done neither a country-by-country assessment on the likely impact of CCCTB on Member States' corporate tax revenues nor a detailed study on businesses' response to this new regulation. The impact assessment published on 25 October 2016 is not enough (European Commission, 2016c). Thus, we urge the European Parliament ECON committee to halt this tax plan until more comprehensive impact studies have been released and properly scrutinised.

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