The impact of national tax reforms on the EU economy

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The Economic and Monetary Affairs Committee adopted an own-initiative report by Markus FERBER (EPP, DE) on the impact of national tax reforms on the EU economy.

Although tax policy is largely the responsibility of the Member States, the single market requires **harmonisation and coordination** in tax policy-making in order to increase the integration of the single market and prevent base erosion.

(1) Impact on small and medium-sized enterprises (SMEs)

While the costs of compliance with tax obligations are estimated for large multinational companies to be around 2% of taxes paid, for SMEs this is estimated around 30%. Furthermore, the profits of multinational enterprises tend to be taxed less than those of equivalent domestic enterprises.

The report pointed out that **differences in national tax regimes** can act as barriers to SMEs trying to operate across borders, as SMEs have fewer resources than multinationals to devote to tax compliance and optimisation.

Members considered that **harmonisation of the tax base**, such as the common corporate tax base, could reduce compliance costs for SMEs operating in more than one Member State. They reiterate that taxing profits in the country where the economic activities take place would enable governments to offer a level playing field to their SMEs.

Members also stressed the need to tax companies using a fair and effective formula for allocating taxing rights between countries, taking into account factors such as the workforce and the existence of tangible assets. They called on Member States to rapidly agree on an ambitious proposal for a European corporate tax code.

The report noted that many Member States and the EU have introduced dedicated regimes that favour SMEs. Members considered that such special treatment, if utilised extensively, while generally positive, could risk introducing further distortions and further possibilities of aggressive tax planning, and could further increase the overall complexity of the system. Member States are urged to **design tax benefits for SMEs** in a way that is consistent with the overall tax regime and does not encourage SMEs to stay small.

(2) Harmonisation and coordination of tax policies

Members pointed out that the EU has developed coordination mechanisms such as peer review procedures within the Code of Conduct Group (CoC) and country-specific recommendations in the context of the European Semester. They considered that both of these mechanisms need to be further improved.

The report noted the limits of the current decision-making process in the Council to meet legislative needs when it comes to promoting coordination between Member States and tackling harmful tax practices. It called for the **full potential of the TFEU Treaty to be explored**. It also stressed that the ideal level of coordination of tax policies to ensure maximum impact is the international arena, through the G20/OECD, recalling that EU tax proposals based on international agreements have always been more likely to be adopted by the Council.

(3) Recommendations and areas for reform

The report stressed that in areas of high importance for the functioning of the single market, such as taxation and the capital markets union, more harmonisation is warranted either through better Member State coordination or EU action. The reforms should focus on the following key areas:

Debt equity bias

Members deplored the debt equity bias in corporate taxation that allows for generous tax deductions on interest payments, while equity financing costs cannot be deducted in a similar manner, making debt financing relatively more attractive than equity financing. They recalled that these incentives can be reduced either by allowing a further deduction of equity financing costs or by reducing the possibilities for interest deductions. They look forward to the Commission's proposal for a debt equity bias reduction allowance.

Competing marginal effective tax rates

The report noted that the marginal effective tax rate can be a key factor for companies making investment decisions. Given the considerable differences in marginal effective tax rates between Member States, Members called on Commission to investigate whether some Member States distort competition by artificially lowering their marginal effective tax rates, for example through accelerated depreciation schedules or by adjusting the tax deductibility of certain items, and to communicate its results to Parliament.

Tax incentives for research and development

While stressing that tax incentives for research and development comes with obvious benefits to society and the economy, Members are concerned that certain types of tax incentives, such as patent or intellectual property tax regimes, do little to increase spending on research and development and may in fact distort the single market by encouraging profit-shifting and aggressive tax planning.

Members called on the Commission to propose guidelines on tax incentives that are not distortive for the single market. They stressed that further harmonisation regarding tax incentives for research and development spending may be warranted.

EU taxation scoreboard

Noting the Commission’s ongoing work on an EU tax scoreboard, Members stressed that the scoreboard should contribute to the fight against harmful tax competition and take into account the considerable public revenue losses imposed by national tax policies that are facilitating tax avoidance. The tax scoreboard should be built as an instrument to help Member States perform sound and robust reforms on tax matters.