The impact of national tax reforms on the EU economy

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The European Parliament adopted by 469 votes to 94, with 137 abstentions, a resolution 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)

Members considered that tax policy fragmentation creates various obstacles for citizens and companies in the single market, particularly small and medium-sized enterprises (SMEs), including legal uncertainty, red tape, the risk of double taxation and difficulties claiming tax refunds.

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%. Some Member States have developed schemes that would tax profits made in an international context at a lower rate than the national nominal rate, thus putting SMEs at a competitive disadvantage.

The resolution 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 reiterated that taxing profits in the country where the economic activities take place will allow governments to offer a level playing field for their SMEs. They highlighted the need to tax corporations using a fair and effective formula for the allocation of taxing rights between countries and called on Members States to swiftly agree on an **ambitious proposal for a European corporate tax rulebook**.

The resolution also 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

Parliament welcomed 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. It considered that both of these mechanisms need to be further improved.

Parliament 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.

The Commission and the Member States are called on to work together and ensure the transposition into EU law of the OECD/G20 Inclusive Framework agreement which suggests that multinational enterprises be subject to a 15 % effective tax rate.

(3) Recommendations and areas for reform

The resolution 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. The debt equity bias might incentivise companies to take on too much debt.

Given that debt equity bias varies considerably between the Member States, Members consider that a common European approach would be preferable in order to avoid distortions within the single market.

Members also look forward to: (i) a Commission proposal which should aim to ensure a more consistent determination of **tax residence** within the single market and (ii) a legislative initiative proposal for the introduction of a common, standardised, EU-wide system for the reduction of **withholding tax at source**.

Competing marginal effective tax rates

The resolution 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.

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