

# Harmonization of Taxation

## ■ RESOLUTION PASSED BY EUROPEAN PARLIAMENT

The European Parliament passed a resolution on 17 November 1983 on the harmonization of the systems of taxation in the European Community<sup>1</sup> (hereinafter "Resolution"). The detailed Resolution follows on from a Commission report<sup>2</sup> on the possible convergence of the tax systems of the EEC Member States and a report of the Parliamentary Committee on Economic and Monetary Affairs.<sup>3</sup> This note outlines and describes the principle proposals and comments contained in the Resolution.

### General propositions in the Resolution

The main thrust of the Resolution is to emphasize the disadvantages arising from the failure by Community institutions to take more effective steps towards harmonization of taxation in the Community. In general terms, the Parliament points out that such a position gives rise not only to discrimination and distortion but also causes inconsistency and ineffectiveness in the economic policy of the Community. The eradication of fiscal barriers to the free movement of goods, services, capital and persons for which the Parliament vigorously presses, would further, to a great extent, the establishment of the internal market envisaged by the Treaty of Rome. The Parliament calls for action by the Member States, and indeed all sectors concerned, to exercise their best efforts in order to contribute to this objective.

The Resolution makes reference to a number of specific points as regards the relationship between the harmonization of taxation in the Community and the four fundamental principles of free movement laid down by the Treaty. It also makes comment upon, what it considers, the necessity of harmonizing the tax burden upon undertakings operating in the Community in a manner which does not impair the competitive position of such enterprises vis-à-vis their non-European counterparts.

### Specific problems addressed by the Resolution

#### *Free movement and freedom of establishment of persons*

The European Parliament stresses the vital importance of taxation as a factor in the process towards European integration and particularly in the establishment of the internal market.

In order to bring about the abolition of fiscal barriers to the "free movement of persons, ideas, mail and workers in frontier areas",<sup>4</sup> the Parliament calls on the Council of Ministers to accept the new proposals for a Sixth<sup>5</sup> and Seventh<sup>6</sup> Directive on exemption from taxes at importation for goods contained in travellers' personal luggage. These proposals include a program for the gradual extension of exemptions better adapted to changes in the cost of living. It also proposed that exemption should be granted from "import duties"<sup>7</sup> throughout the Community to books, magazines and newspapers in the case where these are sent from one taxable person in one Member State to a private individual established in another Member State. The European Parliament also wishes the Council to adopt as soon as possible the Directive<sup>8</sup> regarding frontier workers. In addition, a Directive was called for to enable workers employed temporarily in another Member State to deduct contributions paid to a pension fund in their country of origin from the tax on individuals in the other Member State.

#### *Free movement of goods and services*

Under this head, the Resolution addresses, in particular, the problem of VAT harmonization and the harmonization of taxes other than turnover taxes which affect the consumption of alcoholic beverages and manufactured tobacco.

The Commission and the Council are entreated to complete the harmonization of the system of VAT as a first step towards the objective of fiscal neutrality. In this connection, the Parliament calls for the adoption of further measures on the standardization of the basis of assessment of VAT by:

- (a) the gradual reduction of the number of rates;
- (b) the gradual elimination of the derogations listed under Art. 28 of the Sixth Directive<sup>9</sup> on VAT;
- (c) the adoption of the Seventh Directive<sup>10</sup> on VAT concerning works of art and secondhand goods while assuring that the levy of VAT in this case does not have cumulative effects; and

1. Official Journal of the European Communities (hereinafter "O.J.") No. C 342 of 19 December 1983 at 73.

2. COM (80) 139 final.

3. Doc. 1-903(83).

4. O.J. No. C 342 of 19 December 1983 at Para. 6.

5. O.J. No. L 206 1982, already adopted.

6. Proposed Seventh Directive, O.J. No. C 114 of 1983.

7. The use of the term "import duties" in the English text does not appear compatible with the French or Dutch versions of the Resolution. As import duties have officially been abolished between the Member States, this term probably refers to taxation at importation such as VAT.

8. O.J. No. C 21 of 1980.

9. O.J. No. L 145 of 13 January 1977.

10. O.J. No. C 26 of 1978, as amended by O.J. No. C 136 of 1979.

(d) the adoption of the Tenth Directive<sup>11</sup> on the renting of tangible personal property.

The Parliament points out particularly that the varying number and range of rates applied is too high and causes distortion. It requests the Commission to make suitable proposals in order to move towards the introduction of a dual-rate system. Such a system would comprise "a reduced rate for essential foodstuffs and special cases and a standard rate for other products and services".<sup>12</sup>

In addition to these calls for action, the Parliament stresses the need to adopt the proposal for a Fourteenth Directive<sup>13</sup> on deferred payment of import duties which would not only aim at the simplification of administrative procedures but would be advantageous for businessmen and for the European economy as a whole.

The Resolution goes on<sup>14</sup> to discuss the Commission's approach to the harmonization of taxes other than turnover taxes affecting the consumption of manufactured tobacco. It points out that it is unacceptable for the Commission to harmonize the relationship between the *ad valorem* and *specific elements* of such taxes and calls on the Commission to adopt the alternative approach (preferred by the Parliament), involving the harmonization of the *ad valorem* element of the tax as a specific proportion of the retail selling price. However, on the subject of the tax systems currently applied to alcoholic beverages, the Parliament believes the Commission has adopted the correct approach in proposing the harmonization of structures before the harmonization of rates and it calls for work to be resumed immediately to further this objective.

It is pointed out that excise duties on mineral oils should be harmonized and that the proposal for a Directive was submitted as early as 1973.<sup>15</sup>

A general request is made in the Resolution to the Council and the Commission to prepare proposals for the harmonization or gradual abolition of the "various taxes other than VAT and excise duties affecting intra-Community trade in goods and services".<sup>16</sup>

### Free movement of capital

The main point which was emphasized under this head is the obstacle presented to the objective of free movement of capital by the difference existing in the tax systems applicable to capital transactions. This thwarted the goal of creating a European market for securities, a factor which was recognized as "vital" in the revival of investment throughout the

Community. In this connection, the Parliament asks that work on the proposed Directive of 30 April 1976<sup>17</sup> on indirect taxes on transactions involving securities should be continued and that a report should be prepared detailing the scope for the abolition of capital duty.

On a more general note, the Resolution draws attention to the number and variety of incentive schemes adopted by the Member States to encourage investment in securities and bonds. It calls for coordination at the European level of such schemes and for the harmonization of withholding taxes deductible from cross-frontier investment income by establishing a common system of imputation credits.

The Parliament makes certain proposals in relation to the manner in which such an imputation credit system should be operated.<sup>18</sup> In order to liberalize capital movements within the Community in the form of dividend payments, the Resolution specifies that an imputation credit should be made available to shareholders of a company to offset corporation tax deducted within that company's accounts. In addition, this imputation credit arising in one Member State should be available to shareholders in other Member States. No restriction on the amount of an imputation credit in the form of an advance corporation tax should be allowed in any Member State on the ground that the underlying corporation tax was paid in another Member State. It is, perhaps whimsically, suggested by the Parliament that these principles should apply in such a manner that there would be an "equitable" division of tax revenue between the Member States! It wants to ensure that, so far as possible, tax revenue should not accrue to third Member States through which the investment income flows. As a method of furthering the aim of liberalisation of capital movements, the Parliament considers<sup>19</sup> that the Community should seek to enter treaties for the avoidance of double taxation of investment income with non-member countries which have compatible tax systems, or at least seek some kind of coordination with such countries to achieve this effect.

11. O.J. No. C 116 of 1979.

12. O.J. No. C 342 of 19 December 1983 at Para. 10.

13. O.J. No. C 203 of 6 August 1982.

14. O.J. No. C 342 of 19 December 1983 at Para. 13.

15. O.J. No. C 92 of 31 October 1973.

16. O.J. No. C 342 of 19 December 1983 at Para. 16.

17. O.J. No. C 133 of April 1976.

18. O.J. No. C 342 of 19 December 1983 at Para. 22.

19. Id., at Para. 24.

## Tax burden on business

The Resolution continues to discuss and to propose the harmonization of the tax burden on undertakings which would have the aim of ensuring "fair conditions of competition between undertakings and increasing the competitiveness of European industry".<sup>20</sup> The variation in the rates of corporation tax, amounts of tax credits, and the different bases for assessing corporation tax were some of the factors noted as relevant. The view is also expressed in the Resolution that examination should be made of the following areas:

- (a) the effect of taxes on industrial and commercial profits in the case of individuals or partnerships which have not opted for corporation tax and the resultant distortion of competition;
- (b) the consequences and advisability or generalizing the wealth tax on companies in force in some Member States;
- (c) the advisability and effects of harmonizing or abolishing local taxes on undertakings which are currently in force in some Member States;
- (d) the economic impact of all taxes on business undertakings and the charge of VAT on transactions between registered traders.

Furthermore, it is thought that effort should be made to introduce a common system of imputation credits according to the principles described above with regard to free movement of capital. More effective action is required to combat tax evasion and fraud, and in this connection, the Parliament urges the Commission to report on the implementation of the Directive on mutual assistance by the competent authorities of the Member States<sup>21</sup> and to submit proposals on the practice of transfer pricing. The Resolution also makes mention of the large part played by parafiscal charges in the financing of expenditure on social security in some Member States and the fact that the burden of these charges has an adverse effect on the competitiveness of undertakings and particularly in labour-intensive industries. In this respect, the Commission is asked to examine the effect of the highly uneven burden of parafiscal charges in different Member States on the development of undertakings and the Community economy and to submit recommendations on the subject. The Council of Ministers is again called upon to adopt proposals for Directives and, in particular, those on the taxation of parent companies and subsidiaries in different Member States and a common tax system applicable to mergers,

hive-offs and the transfer of assets among companies in different Member States still pending.<sup>22</sup>

## Conclusion

The Resolution is a long and detailed one with the Parliament constantly stressing the need for harmonization in this field which is so important in making investment decisions and paramount to the competitiveness of undertakings in the Community. The Parliament does not, however, want to see piecemeal action taken in limited areas but instead it should form part of an "overall approach to the implementation of common policies"<sup>23</sup> in which tax is often a vital factor. It reiterates the need for action at the European level to avoid the risks of distortion of competition and inconsistency caused by Member States varying numbers of incentive schemes, rates of VAT, company tax, excise duties and other aspects of fiscal policy which are perhaps, as yet, not regarded as matters of common interest and therefore remain uncoordinated.

In general terms, although the Parliament has outlined several particular examples of where harmonization of the tax system should be applied, it seeks, throughout the Resolution, to emphasize that what is needed is an "ordered programme of successive stages, taking into account the positive or negative financial, economic and social consequences of harmonization for each Member State".<sup>24</sup> It commends the Commission on its comprehensive report on the harmonization of taxation in accordance with Arts. 95, 99 and 100 of the Treaty of Rome and urges action to be taken on these proposals. The Parliament regards the introduction of a scheme of financial incentives applicable to the Community's own revenue as greatly contributing to hasten the desired fiscal harmonization. It considers, however, that priority should be given to the harmonization of indirect taxes, VAT and excise duties and to company taxation.

20. *Id.*, at Para. 19.

21. O.J. No. L 331 of 1979 (VAT); O.J. No. L 336 of 1977 (Direct Taxes).

22. O.J. No. C 39 of January 1969.

23. O.J. No. C 342 of 19 December 1983 at Para. 29.

24. *Id.*, at Para. 37.