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CORPORATE INCOME TAX IN EU COUNTRIES COMPARATIVE ANALYSIS[1]

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Abstract. *If the EU aspires to become the "most competitive economy in the world" by 2010, as agreed by EU leaders in Lisbon in 2000, corporate tax reform should become a priority on the political agenda. The jungle of EU member state tax system hinders competitiveness of European industry, big and small, through high compliance costs, double taxation and protectionist regulations. A more harmonized tax system should improve fairness, efficiency, simplicity and transparency for operators.*

Key words: *Corporate income tax, Tax reform, European Union*

INTRODUCTION

All member states in the EU and most other countries in the world tax company profit. This is a matter of some controversy. It goes without saying that corporations fulfil an important economic role and, as only individuals and not companies can bear taxes, the taxes that companies do pay will be passed on in the form of higher prices or lower payments for inputs (labour, capital, etc.). The question can therefore be asked why states tax them. The justifications for corporate taxes are manifold. Corporate taxes can be seen as *benefit taxe*s, i.e. corporations pay for the public services they use as a company (e.g. infrastructure). Another argument in favour of taxing corporations is that it would otherwise create incentives for individuals to accumulate income in corporations in order to avoid paying tax. Corporate taxation has also been defended as a *rent ta*x. The aim is then to capture the economic benefits that the owner of fixed factors earns (1). A corporate tax is levied on the "taxable profits" of a company, i.e. the difference between the revenues of a company and its expenses, as ascertained through the company accounts. There are, however, significant differences between countries in the way taxable profits are calculated and the level of corporate taxation.

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Tax harmonisation is one of the main outstanding issues for a well functioning Single Market. After years of substantial neglect by the member states and deadlock in the EU Council, they started to discuss corporate tax matters on a multilateral basis and to meet regularly to evaluate their respective tax systems. In the meantime, progress has also been realised on two separate, but not unrelated dossiers, the decision to move to International Accounting Standards (IAS) for all EU listed corporations, and the agreement on the European Company Statute (ECS). By 2005, all EU listed corporations should move to IAS as the accounting standard, thereby creating a single European standard. The agreement on the European Company (known by its Latin name of *Societas Europaea* and abbreviated SE) will allow a single incorporation for EU firms, reducing the cost and burden of having to comply with different company law regimes. Combined, these three elements could radically ease the way of doing business in Europe, but they are interdependent, and failure to achieve progress on one may make the other two much less attractive.

Probably the most uncertain element at this stage is corporate taxation. Member state tax systems are widely heterogeneous, and a more common European tax system will only be possible as a result of comprehensive European tax reform. So far, EU initiatives in the area of corporate taxation are limited to eliminating harmful tax regimes in the member states. The concept of an EU corporate tax system is beginning to take shape, but the thinking is still in a very preliminary phase. Broadly speaking, experts see two possibilities: Home State Taxation (HST) or Optional Common Base Taxation (CBT). Both proposals would allow companies to compute their EU profits under a single set of rules (rather than under 15 different rules as at present) and to apportion those profits EU-wide to be taxed in the individual member states. But both HST and CBT require agreement by the member states on the definition of a group of companies and a uniform formula to apportion profits, which raises a number of complex questions. This will most likely not be in place for the entry into force of the European Company Statute in 2004, but it should not hinder all those concerned to start preparations as soon as possible. The benefits of more tax coordination are clear.

THE CORPORATE TAX IN THE EU - CURRENT SITUATION

The EU's member states retain full control over the formulation and implementation of corporate tax policy. Tax policy in general has been regarded as a basic prerogative of national sovereignty and thus not the object of any Community competence (some indirect taxes, such as VAT, fall within Community competence and have thus been the subject of EU legislation). There are thus 15 different tax systems in the EU.

Over the last two decades, nominal corporate rates have decreased in the EU, and the practice of multiple tax rates is disappearing. Nevertheless, there continue to be wide differences between the rates. For example, in 2001 tax rates varied between 10% (Ireland) and 39% (Belgium). See Table 1 below.

The various methods member states apply to calculate taxable profits differ in many respects, both for domestic and foreign income. Differences in the calculation of domestic income may be due to, among other things, different accounting systems, different treatment of dividends received from other companies, different treatment of capital gains or losses and different treatment of depreciation This is partly captured by calculating the

effective tax rates a company faces in a particular member state. Effective tax rates are generally lower than the nominal rates (see Table 2). Moreover, the divergence between the countries is lower when measuring effective rates as compared to nominal rates. Nevertheless, the difference between effective and nominal rates has decreased over the years. This is a reflection of the convergence of the underlying tax base, meaning that the effective rate is increasingly determined by the nominal rate.

Table 1. Corporate income tax rates in the EU and US (%)

Country	1980	1985	1990	1994	1997	1998	1999	2001
Belgium	48	45	43	40.17	41.17	40.17	39	39
Danemark	37	50	40	34	34	34	32	30
Germany	61-44	61-44	50-36	45-30	45-30	45-30	40	25
Spain	33	33	35	35	35	35-30	35	35
Greece	49	49	46	40	40	40-35	40	37.5
France	50	50	37-42	33	36-41	36-41	33.33	33.33
Ireland	45	50-10	43-10	40-10	36-10	32-10	10	10
Italy	36.3	47.8	47.8	52.2	53.2	31-41	37	36
Luxembourg	45.5	45.5	39.4	33.3	32	32	30	30
Netherland	46	42	35	35	35	35	35	35
Austria	61-38	61-38	61-38	34	34	34	34	34
Portugal	51-44	51-44	39.6	39.6	39.6	37.4	34	32
Finland	50	50	40	25	28	28	28	29
Sweden	40	52	52	28	28	28	28	28
UK	52	40	35	33	31	31	30	30
US	–	–	–	–	–	–	35	35

Source: (2, p.3)

Table 2. Effective average tax rates (EATR) and corporate income tax rates (CITR) in the EU (1999-2001)

Country	EATR (1999)	CITR (1999)	CITR – EATR	EATR (2001)	CITR (2001)	CITR – EATR
Belgium	34.5	39	4.5	34.5	39	4.5
Danemark	28.8	32	3.2	27.3	30	2.7
Germany	39.1	40	0.9	34.9	25	-9.9
Spain	31	35	4	31	35	4
Greece	29.6	40	10.4	28	37.5	9.5
France	37.5	33.3	-4.2	34.7	33.3	-1.4
Ireland	10.5	10	-0.5	10.5	10	-0.5
Italy	29.8	37	7.2	27.6	36	8.4
Luxembourg	32.2	30	-2.2	32.2	30	-2.2
Netherland	31	35	4	31	35	4
Austria	29.8	34	4.2	27.9	34	6.1
Portugal	32.6	34	1.4	30.7	32	1.3
Finland	25.5	28	2.5	26.6	29	2.4
Sweden	22.9	28	5.1	22.9	28	5.1
UK	28.2	30	1.8	28.3	30	1.7
EU average	29.5	32.4	2.8	28.5	30.9	2.4

Source: European Commission/Eurostat (2001).

In sum, while nominal tax rates have decreased, EU governments have widened the tax base. In other words, the discrepancy between taxable profits and real economic profits has decreased (3). The latest example of this general trend is Germany, which in 2000 decided to fundamentally change its corporate tax system. Namely, German tax rates (split rates) went down from over 40% to a single rate of 25%. The base is broadened by tightening the criteria for accelerated depreciation, increasing the time of amortisation of assets and reducing the depreciation of business buildings (3 &4). While the overall effect on the effective tax burden has been limited, national tax systems have tended to become more transparent, less distorting and less costly to comply with.

CONSEQUENCES OF THE CURRENT SITUATION

The diverse tax picture may be attractive to for those who favour subsidiarity and national sovereignty. In the EU there is indeed a relatively broad political consensus that tax policy falls within the competence of member states, not the Community. As economic integration has deepened and widened, it, however, has become increasingly clear that national tax rules create obstacles to achieving a true Single Market. This section evaluates the effects of this discrepancy between national tax rules and economic integration. It focuses on the question whether national tax policies will lead to a race to the bottom, whether they may lead to a shift in the tax burden, whether they may create economic distortions and what kinds and levels of costs it imposes on society.

States compete among themselves to attract economic activity. One of the instruments by which they compete is taxes. Tax competition could lead to a "race to the bottom" in tax rates or revenues. The claim that tax competition may be harmful is contentious, however. Many economists tend to regard tax competition as beneficial. Empirical evidence of a race to the bottom is limited. As has been depicted above, there has indeed been a general decrease in the nominal and effective corporate tax rates, but this has not affected tax revenues. As can be seen from the figure 1, EU member states' total tax revenues as a percentage of GDP increased until the mid-1980s and have since remained stable at around 40%.

If the problem is not one of a collapse in revenues, then it might be a shift in the distribution of the tax burden. While corporate tax revenues as part of total tax revenues have remained stable over time, it is often claimed that labour has come to carry more of the tax burden. Apart from any equity argument that the tax burden should be more evenly borne by labour and capital, the increased taxation of labour would hamper employment creation as it increases the cost of labour. This argument need, however, to be qualified. As can be seen from the figures 2 and 3, labour yields substantially more tax revenues than corporations.

However, the difference, which increased markedly until 1975, has since remained stable, or even decreased. This would imply a refutation of the argument of a wide shift of the tax burden towards labour. However, if one looks at another measure of taxation, a different picture emerges. The effective tax burden on *capital* has decreased from 45 to 35% between 1981 and 1996. During the same time, the effective tax burden on labour has increased from 35 to 42%.

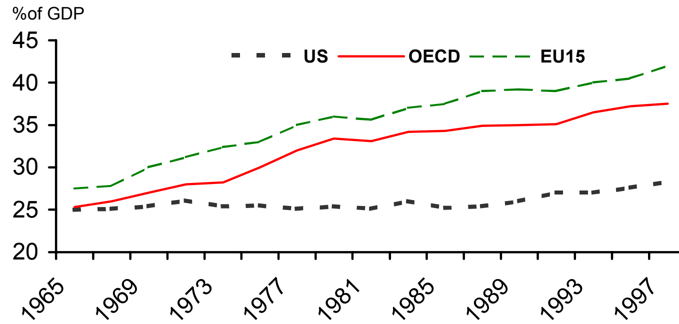

Fig. 1. Total tax revenues as a percentage of GDP, 1965-1997 (4)

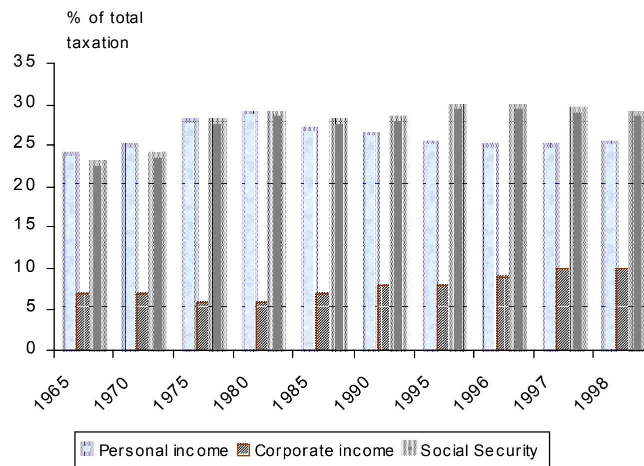

Fig. 2. Different taxes as a share of total taxation in the EU (4)

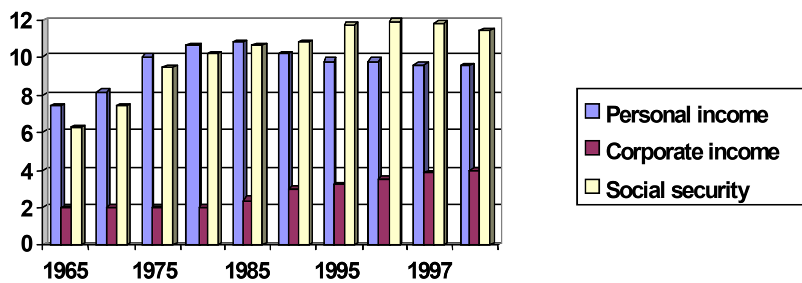

Fig. 3. Different taxes as a share of GDP in the EU (4)

There are various possible explanations of the increasing gap between personal and corporate income taxation in the 1970s. Since the statistics are based on tax revenues, it is likely that the rise in personal income taxation was caused by the rapid inflation of the

1970s (i.e. revenues in nominal numbers increased). At the same time, corporate income taxes remained constant in nominal terms, and decreased in real terms, as stagflation in the wake of the oil price shocks depressed corporate profits. It may also be a pro-active and perfectly rational choice by governments in open economies to tax mobile factors less and immobile factors more.

The ambition for the EU's Single Market is that national borders should play no role in the decision of where to invest. As long as corporate taxes remain national, however, divergences in the effective tax levels remain large. Therefore, the investment decisions of companies remain affected by tax considerations: the effective tax burden depends on the home country of the parent company and the location of foreign affiliates. The result may be that investments become more and more tax driven, i.e. they take place in the lowest tax jurisdiction, not the lowest cost jurisdiction.

The current situation, characterised by 15 different tax systems in the EU, offers corporations plenty of opportunities to "shop around" for the best effective tax rate. The extent of tax arbitrage depends on the mobility of corporate investment. Although it is often claimed that all factors of production are entirely mobile in today's globalised world, there are reasons not to overstate the argument. Mobility is increasing but there are still several factors that continue to hamper it. Physical installations such as factories are not that easy to move, for example. In addition, there are reasons other than taxes why companies tend to favour a particular location, e.g. proximity to the market, well-adapted regulations, stable and predictable political climate, etc.Nevertheless, it has become increasingly easy to move financial capital. There are already policy measures that are supposed to prevent tax arbitrage: there are rules governing how companies should count the value of transfers between the different entities of a company group *(transfer pricing* rules). In principle these transactions should be priced on an *arms-length* basis, i.e. the value a company attributes to an internal transaction should reflect the current market value of a similar transaction between two independent companies. Nation states have also developed a vast number of bilateral double taxation treaties, intended to eliminate double taxation, but also to counter international tax planning and avoidance.

Even though the continued existence of 15 different tax systems offers opportunities to companies to minimise their taxes, tax planning comes at a cost, being time-consuming and complicated. It also risks diverting the attention of companies from profitability to tax minimisation (3). The time spent by senior management on tax issues instead of other issues directly related to the operating of the company represents a huge hidden cost. The activity of tax planning is unproductive and economically inefficient. Assessments of compliance costs are difficult to make. For the UK it has been measured that compliance costs amount to 2.2% of a company's income tax revenues (5). In the Netherlands, compliance costs have been found to make up 4% of total tax revenues (ibid.). The Ruding Report (6) also assessed compliance costs. More than 85% of the companies participating in the report's survey estimated that compliance costs represented 3% of their company's total income.

With the launch of the euro, yet another obstacle to cross-border activity has been removed and this is likely to propel more European companies to enter European markets other than their home country. Thus, more and more companies will suffer from the remaining aspects of fragmentation, such as tax.

CHANGES IN EU TAX POLICY

Harmonisation of direct taxation has been one of the least successful parts of the Single Market programme. To date, only two harmonising measures, the parent/subsidiary and the merger directives, and a Tax Arbitration Convention, have been agreed, whereas other proposals have been stalled or were withdrawn. The adoption of the tax policy package by the December 1997 EU Council of Finance Ministers (Ecofin) signalled a change of track: namely, the EU would focus on tax coordination, rather than harmonisation, and it would link the ifferent elements in a tax package: savings taxation, harmful tax measures and a revised interest and royalties directive.

a) The Single Market programme

The 1992 programme in the area of direct taxation produced two directives and a tax Arbitration Convention, while several other proposals had to be abandoned. The two directives deal with the abolition of double taxation of enterprises operating on a cross-border basis in the EU. The parent/subsidiary directive (90/435/EEC) exempts dividends paid between associated companies from taxation; the merger directive (90/434/EEC) eases cross-border company restructuring operations from a fiscal perspective. While both directives have proven useful, they are fairly narrow, and earlier attempts by the European Commission in 1993 to expand their scope failed. Moreover, implementation by the member states has been problematic.

Another significant element in the earlier attempts to proceed with tax harmonisation was the 1992 *Ruding Committee Repor*t. This Committee, set up by the European Commission to give a new impetus to tax harmonisation, concluded that differences in corporate taxation distorted the functioning of the internal market. It argued for a minimum corporate tax rate of 30% in the EU, coupled with a series of measures in three phases designed to produce significant convergence in company tax systems. Member states showed no desire, however, to take these steps or even to continue discussion on corporate tax measures.

b) The Monti package

The definite initiative to relaunch the EU tax policy debate was taken by Commissioner Monti at the informal Ecofin Council (EU finance ministers) in Verona in April 1996. The Commissioner started from the overall assessment that taxation on income from labour was becoming too heavy as a result of a downward spiral in capital taxation created by unfair tax competition between the member states to attract investment. This was considered harmful since it led to a loss of tax revenue, distorted the Single Market and undermined employment. The Ecofin agreement includes four elements:

1. The first is a voluntary Code of Conduct in business taxation
2. The second component of the deal is the commitment to ensure a minimum level of effective taxation of savings within the EU.
3. The third element is the decision to take a closer look at special tax regimes from the point of view of the Commission's powers in the area of state aid.

4. Finally, the fourth element of the ECOFIN deal is the decision to resume proposals for a corporate tax directive on interest and royalty payments between enterprises operating on a cross-border basis.

The new approach led to important progress in the area of direct taxation. The combination of soft law (codes of conduct), hard legislation and the use of existing Community powers in the area of state aids have brought more progress than reliance on directives alone, which have to be adopted unanimously by the member states. The new approach has three important drawbacks, however. First, the basic premise underlying the whole package, i.e. that tax competition is harmful, is weak. Secondly, the package approach always requires balanced progress. Thirdly, there is the heterogeneity of the package. In general terms, tax competition is seen as beneficial as it forces policy-makers to adjust (7, p. 16-26). While corporate tax *rates* have come down, the overall level of corporate tax revenues as a percentage of GDP has slightly increased over time in the EU. This reflects the fact that tax reforms in EU countries, and in OECD countries in general, have combined cuts in tax rates with measures to broaden the corporate profit base. As can be seen from Table 1, the statutory tax rates have fallen in all EU member states except one, Spain. As shown in Figure 3, corporate tax as a percentage of GDP in the industrialised countries has experienced a slight upward trend, rising from 2.5 to 3.5%. The package approach has probably been a clever way to achieve consensus in tax decisions at EU level.

A second element in the drive towards more integrated tax systems is the Lisbon process. The Lisbon European Council (March 2000) set an ambitious strategic goal for the EU, namely "… to become the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion". The reforms contemplated in the context of the Monti package are, however, certainly insufficient to provide for this more long-term ambition. Rather they have managed to get member states back around the table, and solved some short-term problems. But they are not the basis for a greater convergence of national tax systems, which would be more in conformity with the strategic goal set in Lisbon.

c) The European Company Statute

In the meantime, the agreement on other important elements of the Single Market programme, 1) the European Company Statute (ECS) and 2) the move to the application of International Accounting Standards (IAS) for listed companies, gives a further reason to come up with a long-term strategy. Both elements will largely facilitate the environment for doing business in the EU. After more than 30 years of negotiation, the member states of the EU finally endorsed the European Company Statute on 8 October 2001. The ECS will allow companies operating in two or more member states of the Union to work within the framework of a single European incorporated entity. The final version of the regulation is less complicated and may lead European business to consider re-incorporating as a European company. It should simplify the organisational structure of European multinational enterprises and thus lead to substantial cost savings and efficiency gains. It will, for example, allow large corporations to rethink their organisational structure, and to re-organise themselves along specific lines of activity, rather than having to incorporate on a country-by-country basis. The legal structure could in this sense coincide much better with the effective business configuration.

The EU regulation will allow four different forms of creating an SE. An SE can be established:

- as a holding company promoted by public or private limited companies from at least two different member states;
- as a joint subsidiary of companies from at least two different member states;
- through the merger of two or more existing public or private limited companies located in at least two member states; or
- by transformation of a national company that has operated in two (or more) member states for at least two years, without the need to dissolve the company.

A major problem is the frequent referrals to national law. The SE is a framework regulation, in the sense that only some core elements are harmonised at European level. Issues such as securities law, bankruptcy law and taxation are not covered and left to national law.

The second element highlighting the need for progress on the tax side is the move to International Accounting Standards (IAS). Under a proposed regulation, published in February 2001, all listed EU companies will be required to prepare consolidated accounts in accordance with International Accounting Standards (IAS), rather than having to comply with their home accounting standard, and an international standard. This requirement should enter into force no later than 2005. Member states will have the option to extend this requirement to unlisted companies and to the production of individual company accounts. The regulation will help eliminate barriers to cross-border trading in securities by ensuring that company accounts throughout the EU are more transparent and can be more easily compared. This would in turn increase market efficiency and reduce the cost of raising capital for companies, since one accounting standard should be acceptable for the whole of the EU.

CONCLUSION

Tax issues have been difficult to address at an EU level for a number of reasons. If nothing is done in terms of decision-making, enlargement will further add to these difficulties. The enlarged Union will be more heterogeneous in terms of their members' national interests. The new members are different in their economic structure. Their tax systems are shaped in accordance with their stage of economic development, thus using taxes as a means to stimulate investments and to penalise the repatriation of profits. Tax breaks and special regimes are also widespread.

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POREZ NA DOBIT PREDUZEĆA U ZEMLJAMA EU KOMPARATIVNA ANALIZA

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Direktni porezi u svim savremenim državama predstavljaju jedan od najizdašnijih izvora prihoda državnog budžeta. Najznačajniji direktni porezi su porez na dohodak fizičkih lica (gradjana) i porez na dohodak pravnih lica (porez na dobit preduzeća).

Sve zemlje članice EU i većina drugih zemalja u svetu oporezuje profit preduzeća. Kritičari poreza na dobit preduzeća ističu da oporezivanje profita nije u skladu sa bazičnim stavom svake nacionalne ekonomije: da preduzeća imaju odlučujuću ulogu u ostvarivanju privrednog razvoja. Naime, plaćanje poreza na dobit preduzeća znači ili povećanje cena (prevaljivanje unapred) ili smanjenje izdataka za radnu snagu i kapital (prevaljivanje unazad).

Medjutim, oni koji opravdavaju oporezivanje dobiti preduzeća, ističu da su to u stvari plaćanja za javne usluge koje preduzeća koriste, kao što je infrastruktura. S druge strane, ovaj poreski oblik znači "obezbedjenje plaćanja poreza na dohodak fizičkih lica", jer da isti ne postoji fizička lica bi u cilju izbegavanja plaćanja poreza na dohodak sve svoje viškove prihoda transferisale u preduzeća.

U radu je učinjen osvrt na postojeću situaciju poreza na dobit preduzeća u EU, gde se jasno vidi da sve zemlje EU imaju različite sisteme poreza na dobit preduzeća (diferencirane poreske osnovice i poreske stope), kao i na posledice ovakvog stanja na nivo i distribuciju poreskog opterećenja preduzeća, na pojavu poreske arbitraže i prilično visokih troškova žalbi preduzeća. U drugom delu rada akcenat je stavljen na razvoj poreske politike u EU (program jedinstvenog tržišta, Montijev paket i statut evropskih kompanija).