POLSKI INSTYTUT SPRAW MIĘDZYNARODOWYCH
THE POLISH INSTITUTE OF INTERNATIONAL AFFAIRS

BULLETIN

No. 53 (993), 30 May 2017 © PISM

An EU Tax Haven List: Prospects and Limitations

Patryk Toporowski

The European Union is pursuing the creation of a blacklist of tax havens. It would be an element of the wider strategy to counter tax avoidance. The list, however, may prove an ineffective tool to limit profit-shifting outside the EU. Poland may lose as much as €10 billion euros in corporate income tax and may join a group of countries actively seeking closer cooperation on fighting tax evasion.

The EU wants to establish an official blacklist of "non-cooperative external tax jurisdictions"—tax havens—states or territories that in effect allow corporations to avoid taxation on money that would be taxed in another country. Companies that conduct cross-national business in their accounting might assign a significant share of the overall profits they generate to a company incorporated in a tax haven because it has less stringent legislation, saving it money. Of course, the majority of the income comes from actual sales in stricter tax jurisdictions.[1]

Profit-shifting outside the EU is estimated to reduce total budgetary revenue to Member States by up to €70 billion a year (equal to more than half of the EU's annual budget). In addition, while aggressive "tax optimisation" mechanisms are lawful, tax havens facilitate money laundering because of the opacity of their regulatory systems, according to the European Commission. Despite these reasons, the EU plan of action on tax havens has developed slowly. The main obstacle to formulating a coherent bloc-wide strategy is the high differentiation of the Member State tax systems. Some allow profit-shifting outside the EU in return for investment. This leads to diverging interests between EU members. As a consequence, EU legislation specifically designed to combat tax evasion (such as Council Directive 2014/107/EU on the exchange of information in taxation, or Council Directive 2016/1164 on counteracting tax avoidance) is too general and ineffective.

Listing Process. The registry would be part of the EU's "External Strategy for Effective Taxation," launched in January 2016. The strategy foresees the promotion of best tax practices by targeting non-EU actors with development aid or other tools. The strategy is in response to scandals such as LuxLeaks or the Panama Papers related to wealth-hiding and profit-shifting by the wealthiest Europeans and transnational corporations. The responsibility for preparing the list rested with The Code of Conduct Group, composed of national experts and set up in 1998 by the ECOFIN Council. The actual composition of the group, how it operates, and its decisions are confidential.

According to unofficial information, the provisional list developed by the group includes 92 jurisdictions (i.e., states and territories). These places were informed about the start of a review of their tax systems and they will be assessed on three criteria (based on OECD recommendations) proposed by the group and the EC and then—after modifications—adopted by the ECOFIN Council. The first criterion is transparency of the tax system, understood as compliance with information-exchange standards. The second is "fair taxation,"

[1] J. Foks, "'Raj podatkowy' jako zagraniczny czynnik w systemie podatkowym," *Biuletyn PISM*, no. 5 (5), 10 February 2001.

i.e., a tax system that does not introduce unfair competition with the EU. The third is the OECD's proposed minimum standards to prevent the improper transfer of profits.

The EU's register is expected to take shape at the end of 2017 after discussions with these tax havens' authorities. If the listed jurisdictions meet the criteria or commit to meeting them, they will be excluded from the final blacklist.

Diverging Opinions in the EU. The biggest opponents of tax havens are Germany, France and Italy, which in 2014 jointly demanded the establishment of an EU law limiting so-called aggressive tax planning (including profit-shifting outside the EU). In 2016, together with Spain and the United Kingdom, they proposed establishing a joint blacklist with the G20 (which is also developing its own list).

In Germany, the fight against tax havens is supported by all the main political parties. After the disclosure of the Panama Papers, Germany created a transparency register of corporations. Finance Minister Wolfgang Schäuble encouraged other Member States to work together to combat profit-shifting. The leader of the Social Democrats, Martin Schulz, made the fight against tax avoidance one of the main economic issues in the campaign before the September Bundestag elections.

According to Oxfam, which also examines tax-avoidance issues, in the banking sector alone in 2015, France lost about €5 billion euros to tax havens (of which €2 billion euros went to Luxembourg). Italy, on the other hand, claims it suffers more than €100 billion in losses each year due to its leaky tax system, with almost 15% being CIT transferred to tax havens. The country's public debt crisis—more than 130% of GDP—together with an ongoing budget deficit of around 2.5% of GDP limit its economic growth and proved an incentive for the socialist government to join the fight against tax havens.

The opponents of increasing the fight against profit-shifting are states considered by experts to be tax havens or whose taxation system facilitates profit-shifting outside the EU, often in exchange for a small tax paid in their jurisdiction or for investments. This group includes Luxembourg (LuxLeaks), the Netherlands, Ireland, and Malta. The United Kingdom, although one of the initiators of the fight against tax havens at the G20 level, has also weakened EU efforts in this area. This is because it has protected the looser tax laws in its dependencies (Jersey, Guernsey) and overseas territories (Cayman Islands, British Virgin Islands).

As a result of the tension between these interest groups, the criteria adopted by the Council are weaker than initially proposed. Because the EU Council requires consensus, the "delayers" have negotiated transition periods and softened the second criterion ("fair taxation"). While initially describing a zero, next-to-zero or no CIT rate a breach of the criterion, the ECOFIN Council agreed in the end that these characteristics of a tax system alone would not necessarily mean a listed jurisdiction will be declared a tax haven.

Perspective for Poland. For any blacklist as a tax avoidance tool to be effective, it should be supplemented with sanctioning mechanisms. Decisions on what instruments, including restrictions on access to resources from the European Bank for Reconstruction and Development for corporations found to be using tax havens, are to be made by the end of 2017. However, there are limitations on its effectiveness independent of these instruments. First, it is not clear which jurisdictions are on the initial list. In addition, with the Council easing the criteria, the final register may be short.

The key to effective EU action in this field is harmonisation of Member State tax systems, which may lead to a convergence of interests among the countries in fiscal matters. This process gradually takes place in selected areas, for example, through EU tax regulations for the largest corporations. This is done through the common consolidated corporate tax base (CCCTB) or the automatic exchange of information about individual tax rulings.

According to European Parliament estimates, Poland loses up to €10 billion euros a year in corporate tax avoidance, so a third less than Italy, a much economy, loses. It amounts 12% of Poland's budget revenue and 75% of its deficit in 2016. Poland could use the Weimar Triangle formula to accelerate the EU-wide fight against tax havens. This issue enjoys widespread support in Germany. The fight against tax havens was part of new French President Emmanuel Macron's campaign programme. The Weimar Triangle could then eventually become the backbone of a coalition of EU Member States seeking to limit profit-shifting.