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TALKING TAX: Harmonization of direct taxation: future or fiction?

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Currently the field of direct taxation in the EU is not harmonized. Compared with the sphere of indirect taxation, few directives exist. In those cases where the directives do not apply, member states are free to determine tax rates and other factors that bring taxpayers within their powers of taxation. As a consequence, tax rates in member states differ, and the existence of these disparities between systems may distort investment, employment and decisions by companies and self-employed individuals.

The lack of harmonization, however, does not mean that member states possess unlimited taxation powers. The European Court of Justice and the commission are “on their guard.” Still, the ECJ’s extensive and sometimes very controversial case-law shows that even after more than 20 years the court’s attempts to reconcile the freedoms guaranteed by the EC Treaty with nations’ direct tax systems still languish. The same can be said about the commission’s attempts to harmonize this field by submitting different proposals for directives, which in most cases are subsequently withdrawn for one or another reason.

Nevertheless, the ECJ and the commission have not given up their attempts to make member states respect Treaty freedoms whenever they exercise their taxation powers. The commission has started an ambitious strategy to eliminate tax obstacles such as: high compliance costs for cross-border operations, existing transfer pricing problems, complicated exemption approaches to international taxation and the lack of cross-border loss carry-over.
According to the commission, these goals can be achieved by introducing the Common Consolidated Corporate Tax Base within the EU. But it seems that member states are not in a hurry to decline their rights to collect direct taxes as they consider appropriate and therefore look at the CCCTB with considerable disfavor.
According to a position adopted on June 4, 2007, Latvia considers introducing the CCCTB unnecessary, as the vast majority of enterprises operate within national borders. In Latvia’s view, the fact that small and medium-sized companies are treated more heavily than large enterprises in respect to compliance costs is not yet a reason to change the tax law.

However, it is hardly believable that this odd argumentation may be the real reason why Latvia, like other member states, does not want to allow introduction of the CCCTB within the EU. With a high degree of credibility it can be argued that the real reason is the fear of being “forced” to harmonize tax rates as to remain competitive.
Consequently, even if harmonization of rules in the field of direct taxation is the inevitable future for member states, it is hardly believable that this future will materialize soon, and the commission’s intention to introduce the CCCTB in 2008 will remain a dream about a shiny future without direct taxation as an obstacle for the internal market.

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