For a fair taxation system in Europe

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Version 3

Introduction

Ladies and gentlemen

I'm very honoured to be with you today. I especially want to thank the Rector of the University, Gianmario Verona. And above all, your President, Mario Monti. Mario is someone whose achievements are well known, here in Italy and all over Europe. But for me, he is first and foremost an illustrious predecessor, who has shown the way for so much of what we do in competition enforcement today.

Grazie mille, Presidente. Grazie mille, Magnifico Rettore.

I'm afraid that's as far as my Italian goes.

I thought about continuing this talk in Danish. But that seemed a bit unfair. Because Danish can seem a bit of a strange language. Let me give you an example.

For a Dane, the word "skat" means something like "darling" or "dearest". You might use it when you talk to your spouse or your children. But the word "skat" in Danish also means "tax".

That makes sense, when you think that the word literally means "treasure" – a little bit like "tesoro" in Italian.

But it might still make the Danes the only nation in the world who talk about tax with a term of endearment.

Fair taxation and the social contract

Because let's be honest. Paying tax is no one's idea of fun.

But of course, we still understand why paying tax is important. We still know that our taxes pay for the things that make a decent society. Our roads and our railways. Schools for our children, and care for the elderly. The welfare systems that protect us from the uncertainties of life.

So paying tax depends on a sort of unspoken agreement – a social contract, if you like. We pay our taxes. But in return, we expect a fair deal.

We expect that everyone will make a fair contribution. So our governments can provide the services we expect. And so they don't have to come back and ask to pay more, just because others aren't paying their share.

I think that's why all the stories that we've heard in recent years – from LuxLeaks and SwissLeaks, the Panama Papers, and now the Paradise Papers – have produced so much anger throughout Europe.

Because people have just been through a decade of crisis. They've seen their governments raise taxes and cut back on services.

And now they see that some of the people and businesses who can most afford to pay have been using loopholes in our tax systems to escape from paying tax. They see that among the rich, and the powerful, there are some who don't seem to believe that the social contract applies to them.

Fixing Europe's tax rules

So it's no surprise that Europeans want to see change. And the European Commission has a responsibility to help deliver that change.

For the last three years, under the leadership of the Commission's President Jean-Claude Juncker, my colleague, Pierre Moscovici, has been leading our work to close loopholes in Europe's tax laws.

We made our first proposal only four months into our term of office. That proposal dealt with a subject that was at the centre of the LuxLeaks publication – tax rulings.

A tax ruling isn't a bad thing in itself. Corporate tax can be complex. So it helps when companies can get certainty in advance, by asking a tax authority for a decision on how the rules will be applied. The problem is that sometimes, those decisions approve a way of applying the rules that helps a company avoid tax.

So that first proposal – which has been in force since January this year – provides for EU tax authorities to exchange information on tax rulings automatically. So they know what arrangements a company has made in other countries.

Since then, a whole series of rules have become law. Large multinationals now have to tell the tax authorities about the tax they pay in each country and their activity in that country. So authorities can spot companies that may not be paying tax where they make profits.

And from 2019, a new Anti-Tax Avoidance Directive will close a series of loopholes that companies use to avoid tax. So EU tax authorities can collect some of the 50 billion euros they lose to tax avoidance each year.

Tax and competition

But the effect on national budgets isn't the only issue with tax avoidance. Because special tax benefits can also harm competition.

When governments hand out subsidies to a few favoured companies, then competition doesn't work the way it should. It becomes hard for other businesses to compete on equal terms – even if their products might serve people better. It means that businesses battle, not to meet consumers' needs, but to get a bigger subsidy. It can even build monopolies, when the companies that don't get a subsidy have to leave the market, because they just can't compete.

All of that ends up hurting consumers. They lose out on the benefits that competition brings – the lower prices, the wider choice, the more innovative products. And it makes no difference whether that subsidy is a handout in cash, or special tax treatment that means a company pays less tax than its rivals.

It's no secret that special tax treatment can harm competition. Certainly not to Mario Monti. He was Competition Commissioner in 2001, when the Commission investigated more than a dozen tax schemes all over Europe. And it found that several of them were harming competition. Because they gave multinationals special ways to work out the tax they had to pay – ways that benefited them, and weren't available to their rivals.

So everyone knew that this sort of arrangement could be illegal.

What we didn't know until some years ago was that it still going on. Not openly this time, but quietly, in the form of tax rulings.

The Commission’s state aid investigations

And then in 2013, the secret started to come out. The US Senate looked into Apple’s tax affairs. The British Parliament studied Starbucks and Amazon. And the Commission decided it was time to look again.

Since then, we’ve asked every EU country to explain how it uses tax rulings. We’ve looked in detail at rulings from the 23 countries that use them. We’ve followed up information from the LuxLeaks publication – and we’re looking at whether we need to do the same with the Paradise Papers. Altogether, we’ve looked at more than a thousand tax rulings.

And we’ve found that most of them don't give special benefits. But in a few cases, they have been used to hand out a preferred tax treatment to selected companies.

Transfer pricing

Some of those cases have involved transfer prices – the prices for transactions within a group of companies.

When you run a standalone company, the price of what you buy and sell depends on competition in the market. And your profit is just based on those market prices.

But for a group of companies, it isn't so simple. Goods move from one company to another within the group. Intellectual property that’s owned by one company could be used by many others in the same group. And of course, none of those transactions is done in the market. So to work out the company’s profits, you need to put a price – a transfer price – on each transaction within the group.

Deciding on those transfer prices can be complex. So it can make sense to get a tax ruling, to confirm that you’ve done it right.

But that complexity also means there's room to manipulate those prices. And to use prices that don't match the economic reality to shift profits around the world.

So a decade ago, the European Court confirmed that when it comes to tax, transfer prices should be in line with the price in a market with free competition. So they reflect the economic reality of the situation.

And in cases like the ones involving Starbucks and Amazon, we've taken action against transfer prices that didn't match economic reality.

Financing companies

We've also looked closely at tax rulings that give special benefits to financing companies.

Those companies make loans to other parts of a group. The company that borrows the money can deduct the interest from its profits. But that's OK, because the financing company pays tax on that interest.

In 2002, it turned out that Luxembourg had agreed to tax these companies on just a tiny, fixed part of the loans they made. That margin was just over 0.1%. It was far less than any bank would accept as profit on a loan, and way out of line with economic reality. So the Commission – again, in Mario Monti's time – decided that was illegal state aid.

But when we looked at tax rulings, more than a decade later, we found that this issue hadn't gone away. Some countries were giving tax rulings that accepted very low profits. So we've explained to EU governments that tax rulings approving those tiny profits for financing companies could give them state aid.

We're also concerned about rules in the UK that give financing companies an exemption from rules against tax avoidance. That is why, last month, we opened an investigation into those rules in the UK.

The way forward

In the last few years, we've taken action in a series of cases. We've found that Apple and Amazon, Fiat and Starbucks, and some 35 multinationals in Belgium, have all been given illegal state aid. So they will have to pay back those taxes – some 14 billion euros in all.

And our work isn't over yet.

As well as our investigation into financing companies in the UK, we're still looking at whether Luxembourg gave illegal state aid to McDonald's and Engie.

And we will open investigations whenever there are indications that State aid has been granted.

And there's still work to do on our legislative work, to close the loopholes in our tax laws.

Intermediaries like accountants, law firms and banks can be deeply involved in setting up arrangements that can be used to avoid tax. We've seen that role very clearly from the Panama Papers, and the Paradise Papers. So in June, we proposed new rules that would make intermediaries tell the tax authorities about those arrangements.

And we've also relaunched a project called the Common Consolidated Corporate Tax Base. That project will close loopholes between tax systems in the EU, by providing a standard way to calculate taxable profits throughout Europe.

The responsibility of Member States

But in the end, what we need is not just new laws. We need a new culture. One where tax authorities take responsibility for making sure everyone pays their fair share of tax. Where powerful businesses don't get special deals. Where there's no reason for any company to put money and time into coming up with clever ways to get round the rules.

That change of culture won't happen just because we gave new rules. It needs national governments to face up to their responsibilities. And the good news is that things do seem to be starting to change.

Many countries are getting more careful about the way they deal with tax rulings. Every new corporate tax ruling in Luxembourg now has to go to a Tax Rulings Committee before it can be granted. We've heard that Ireland is looking at all the tax rulings that were granted to companies before 2012.

And in the Netherlands, when it turned out that a ruling found in the Paradise Papers was given without following the proper procedures, the government responded at once. It's now checking whether more than 4,000 cross-border tax rulings were given in line with the rules.

Some governments are also improving the way they deal with financing companies.

In January, Luxembourg made changes to its rules, to tax those companies on profits that more closely match economic reality. In July, Cyprus made similar changes to its own rules. And I'm very glad that both countries took the initiative to fix those issues, and worked closely with us to find a solution.

Strengthening the tax base

And that's not all. Many governments are going back to first principles, asking whether they've really been taxing the profits that companies make in their countries.

Here in Italy, the tax authorities have been looking at whether Apple and Google have paid all the taxes they should. That's led to the government reclaiming more than 300 million euros from each of them.

Italy has also joined France, Spain and Germany in asking whether digital companies are paying their share of tax.

Because our tax systems aren't set up to deal with digital businesses properly. A system that looks at a company's physical assets to decide where it should be taxed is bound to face problems in an age when you can easily do business in a country without a physical presence.

Commissioner Moscovici and his team have done a lot of work on ways to deal with this issue. It's an issue that affects governments all round the world, so I hope that we'll be able to find an international solution. That's just what the OECD is trying to do right now. But if it doesn't happen by the spring of next year, then the Commission will propose new rules for the EU.

Conclusion

Because we need to act now. This is our opportunity to make taxation fair.

It's our opportunity to make sure that national budgets can cope with the challenges that they'll face in the future, as our populations age and the way we work changes.

It's our opportunity to make competition in Europe fairer. So our markets work for everyone, not just the companies that get the biggest subsidies.

And most importantly, it's our opportunity to restore people's trust. Their confidence that everyone in their society is making a contribution. That some of the rich and the powerful, who should know better, are not playing them for fools.

Closing the loopholes in our tax systems will help. But people also need proof that our tax systems are fair.

In spring last year, we proposed to introduce public country-by-country reporting. Meaning multinationals would have to publish information on the tax they pay in each EU country, and the activities they have there. So the public can see for themselves if those companies are paying tax where they make profits.

And I hope national governments will work quickly in the Council to make this proposal law.

Because we've come a long way in the last three years. The culture is changing, in tax authorities and businesses.

Now we need to show that, in ways that the public can see. Not so people start to love paying tax - that's never going to happen. But so that every time they do pay, they know that they're part of a community where everyone – without any exceptions – makes their contribution.

Thank you.