THE IMPACT OF TAX COMPETITION AND HARMONISATION IN THE EU IN RELATION TO FISCAL OPTIMISATION

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Abstract: *Fiscal competition and harmonisation are topical issues and the controversy generated by preferences for one or the other is due to the effects they generate in the economies of the EU member states. The practice of tax competition to a smaller or larger extent by some of the Member States is often identified with tax optimisation practices. Thus, in the economies of developed or emerging countries, the effects are both on the labour market, in the collection of indirect taxes (VAT or excise duties), but also in the transfer of profits versus transfer prices. The European fora are working hard for the uniformity of European legislation, but also to determine the governments of the Member States to apply the legislation adopted at European level in their national legislation. The European Commission's legislative perspectives are included in the EU's fiscal policy strategy, which is explained in the Commission's Communication entitled "Taxation Policy within the European Union – Priorities for Future Years", focus on the main priorities of the EU's fiscal policy, as follows: removing tax barriers that hamper cross-border economic activity, the fight against harmful tax competition and tax evasion, wider promotion of collaboration between financial administrations, in order to control and combat fraud. In line with the established objectives, it is suggested that greater fiscal policy coordination would ensure the support of wider EU policy objectives through fiscal policies of the Member States as set out in the Europe 2020 Strategy for smart, sustainable and inclusive growth and in the single market act.*

Keywords: *tax competition; fiscal harmonisation; tax optimization.*

JEL Classification: *F65; E62; H21; H26.*

1. Introduction- General Framework

Over the last few years, we have witnessed increasingly consistent efforts to harmonise the economic and political systems of the Member States of the European Union. However, economic globalisation and increased capital mobility have created a framework conducive to the emergence of fiscal competition between Member States.

The absence now of an EU-wide integrated tax system at EU level marks the way in which the same tax policy decision is transmitted and perceived at each Member State level. In the absence of an integrated European tax system, there is currently only a connection of different national tax systems. Such plurality has made possible the tax competition generated by national tax systems.

In the literature, debates and opinions on harmonisation and tax competition at the European Union level have been visible, especially since the 1990s, when

economists, politicians and authors of various scientific works have pronounced themselves differently on the architecture of a common fiscal policy, oscillating between a centralised fiscal policy as a result of a tax standardisation, including tax rates (total harmonisation) or of compatibility of varieties, as a result of a simple coordination of national tax systems.
According to Ungureanu (2018) the general fiscal policy framework of the European Union is reflected in the law and actions of the Community authorities to regulate taxes unitarily in the EU. In a narrow sense, the financial and fiscal policy aims at the way to obtain and spend the money resources in the budget and the multi-criteria foundation of each country's contributions to the EU budget.
In a comprehensive sense, financial and fiscal policy aims at actions jointly undertaken by member states through strict adherence to unanimity, reducing their asperities in order to achieve, over time, the goals and functionality of the Single Market.
The EU's fiscal policy strategy, as explained in the Commission's Communication "Taxation Policy within the European Union - Priorities for Future Years", focuses on the main priorities of the EU's fiscal policy as follows: removing tax barriers that hamper cross-border economic activity, the fight against harmful tax competition and tax evasion, greater promotion of collaboration between financial administrations, in order to control and combat fraud.
In line with the established objectives, it is suggested that greater fiscal policy coordination would ensure the support of wider EU policy objectives through fiscal policies of the Member States as set out in the Europe 2020 Strategy for smart, sustainable and inclusive growth and in the Single Market Act.
At the same time, according to the same strategy, the fiscal powers belong to the Member States, with the EU having competences limited only at European level. Each Member State is a decision-maker in choosing its own tax system that it considers the most appropriate, provided it complies with EU rules.
The most recent EU policy priority has been to combat tax evasion and tax avoidance practices. As the EU fiscal policy aims at the smooth functioning of the single market, the harmonisation of indirect taxation rules has been dealt with before the direct one.
The way the EU countries' economy is currently functioning due to the complexity of the mechanisms and implications of the integration process and the need for alignment to the Constitutional Treaties of the European Union, the operation and objectives of the tax system at a Member State level, demonstrate that fiscal policy cannot be addressed individually, at a Member State level, since in many cases interaction with other states has negative externalities, in particular on the good functioning of the European single market. Tax measures should therefore be unanimously adopted by the Member States.
Specialised publications bring many arguments for or against the process of tax harmonisation, in terms of the degree and limits this process should be continued, by resorting to the option of total harmonisation or harmonisation based on fiscal coordination, which also implies the acceptance of some elements of tax competition.
Thus, some form of tax harmonisation becomes inevitable, and a number of issues can be argued for tax harmonisation, such as: eliminating the risk of double taxation which is not beneficial for those who earn income in a country other than their State of residence, nor for the States concerned (the source and the home State), eliminating discrimination, preventing tax evasion, particularly in intra-Community

transactions. preventing revenue losses associated with tax competition and fragile revenue, in particular by migrating national tax bases between Member States in search of a more favourable tax regime, reducing the compliance costs of non-residents' employment under the various tax systems, the non-use by some Member States against others of the benefits of a single market, but also from the point of view of the international distribution of tax revenues, the distortion of the constitution and implicitly the equitable allocation of budgetary resources, with negative consequences on the level of financing of the public expenditures.
Harmonisation of fiscal policies is delayed and, as an effect, we are witnessing the emergence of more dynamic and competitive economies on the market, while EU countries are in a position to apply certain aspects of tax competition.
As a general definition currently applicable at EU level, tax competition is the reduction by a Member State of tax rates and taxes, with the main consequence that certain categories of direct or indirect taxpayers, both natural and legal persons, opt for locating wealth or income sources in that State, that tax residence that best meets the best combination between a reduced tax pressure and/or public goods received. Thus, the governments of EU Member States applying tax competition have various purposes such as:
- generating jobs, a goal achievable by attracting foreign direct investments;
- attracting mobile financial capital, which is useful for financing investments, for stability of financial markets and for obtaining comparative advantages in the provision of financial services;
- attracting internal financial flows from multinationals that can be directed to their own tax jurisdiction by attracting those corporate functions used for the international transfer of profits;
- generating interest on the niche of skilled labour force generating added value
- attracting potential buyers in cross-border areas and not only, in particular, for products on which indirect taxes, such as VAT or excise duties apply, where there are significant differences between them.
Keen (2008) defines fiscal competition as a “strategic fiscal context, within the wider framework of non-cooperation between tax jurisdictions (countries, states or regions of a federation), where each establishes some parameters of the tax system according to the taxes practiced by others.”
In order to achieve a higher return on income, direct or indirect taxpayers operating on the market will be clearly attracted by EU tax competition. This can be seen as a competition between the tax jurisdictions of the Member States where everyone wants to become more attractive from the tax point of view. This must be seen from the perspective of qualitative and quantitative parameters such as:
- acceptability of tax rates by setting lower rates than others in other tax jurisdictions;
- granting facilities (discounts, deductions, exemptions) in establishing tax bases;
- flexibility and transparency of regulations and methods for calculating taxes;
- infrastructure and functionality of the local and central fiscal management and administration system;
- providing facilities related to environmental problems, or in providing the infrastructure required to attract foreign investment.
One of the most discussed and controversial issues also by the finance ministers of the EU member states is the harmonisation of the tax rates of European companies' profits. There is a difference between fiscal policy, such as the one-off tax rate, of some governments that aim to increase the competitiveness of national economies

and fiscal policy preferred by other governments that rely on a high tax rate in order to provide the resources needed for funding state. Also, the emotional factor is likely to greatly influence the harmonisation trends, and a number of Member States consider that joining a Community-wide harmonised tax system is waiving an important component of national sovereignty.
However, by harmonising, it should not be understood that all Member States shall have the same tax rate on profits but that the same types of resources shall be imposed so that such harmonisation does not affect the independence of the national fiscal policies of the States that will accept such a measure.

2. Harmonisation or tax competition in the field of direct taxes and indirect taxes

The European Parliament has highlighted the immediate need for the European Union to combat as effectively as possible tax evasion and aggressive fiscal planning and to act swiftly, particularly in the direction of improving cooperation and transparency, in particular by ensuring that direct taxes are paid by the taxpayer where the value has been created, respectively in the case of indirect ones where the goods are consumed.
In order to adopt the most beneficial measures aimed at combating fraud and tax evasion, as well as the widespread phenomenon of money laundering, an EU-level initiative has been generated materialised on a VAT Action Plan 2016 which includes: the principles of a future European single VAT system, anti-fraud measures in the field of VAT, an update of the framework for the establishment of VAT rates, simplifying and modernizing VAT rules for e-commerce, a package of VAT measures that comes with real support for SMEs.
As a consequence, one of the niches of the European Union's tax system is the common system of generalized VAT application, which involves harmonisation by uniformity of the tax base, the obligation to fit the rate between minimum and maximum thresholds, the abolition of tax frontiers for the intra-community movement of goods and services, generalization of the destination principle, actions to reduce fraud and evasion in the field, in accordance with Directive IV and later.
Currently, there are harmonised VAT rules in the EU, but their application may be different from one country to another.
In principle, VAT must be paid for all goods and services, including when sold to the final consumer. Value-added tax is charged at each stage of the production process (purchase of components, assembling, transport etc.).
Thus, the VAT rates currently applicable in the EU member states, both standard and reduced. In this respect, an overview of VAT rates in each of the EU Member States would be edifying in order to be able to compare and see where each of the Member States fits.
As shown in Table 1, the highest VAT rate between EU Member States is practiced by Hungary, respectively 27%, and the lowest in Luxembourg is 10% here the percentage is ten percent lower, 17% respectively.

Table 1. List of VAT rates currently applied in Member States

Member State	Country Code	Standard Rate	Reduced Quota	Very Low Share	„Parking" Rate Share
Austria	AT	20	10 / 13	-	13
Belgium	BE	21	6 / 12	-	12
Bulgaria	BG	20	9	-	-
Cyprus	CY	19	5 / 9	-	-
Czech Republic	CZ	21	10 / 15	-	-
Germany	DE	19	7	-	-
Denmark	DK	25	-	-	-
Estonia	EE	20	9	-	-
Greece	EL	24	6 / 13	-	-
Spain	ES	21	10	4	-
Finland	FI	24	10 / 14	-	-
France	FR	20	5.5 / 10	2,1	-
Croatia	HR	25	5 / 13	-	-
Hungary	HU	27	5 / 18	-	-
Ireland	IE	23	9 / 13,5	4,8	13,5
Italy	IT	22	5 / 10	4	-
Lithuania	LT	21	5 / 9	-	-
Luxembourg	LU	17	8	3	14
Latvia	LV	21	12	-	-
Malta	MT	18	5 / 7	-	-
Netherlands	NL	21	6	-	-
Poland	PL	23	5 / 8	-	-
Portugal	PT	23	6 / 13	-	13
Romania	RO	19	5 / 9	-	-
Sweden	SE	25	6 / 12	-	-
Slovenia	SI	22	9,5	-	-
Slovakia	SK	20	10	-	-
United Kingdom	UK	20	5	-	-

Source: https://europa.eu/youreurope/business/taxation/vat/vat-rules-rates/index_ro.htm

From Figure 1, one may see a tendency to harmonise the VAT rate in the last three years for four of the five countries in the previous example, namely Germany, France (EU founding countries), and apply a VAT rate of 19% and 20% respectively (including Austria), a threshold to which Romania has been aligned since 2016 with a 20% share, which has fallen from 2017 to 19 percent. Of all five, Denmark

maintains “moms”, at a high rate over the past 7 years, with a 25% VAT rate being applied, this being the highest in the EU, well above the average applied in the EU, as notes in Figure 2, and slightly below Hungary's highest rate.

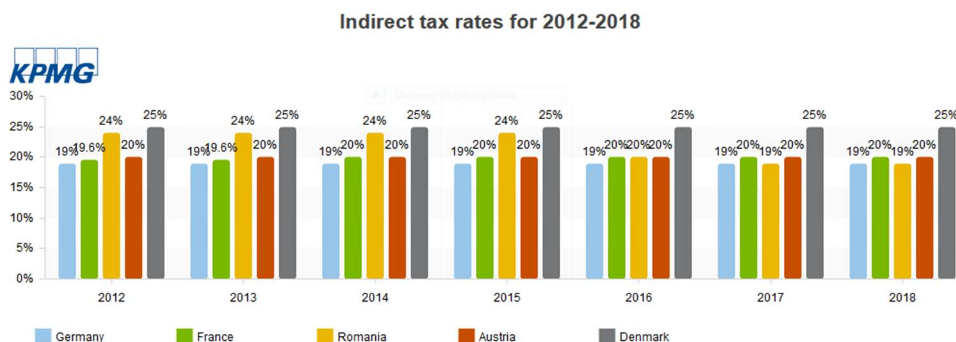

Figure 1: Indirect tax rates for 2012-2018 Germany, France, Romania, Austria, and Denmark
Source: own processing on the basis of the data provided by
https://home.kpmg.com/xx/en/home/services/tax/tax-tools-and-resources/tax-rates-online.html

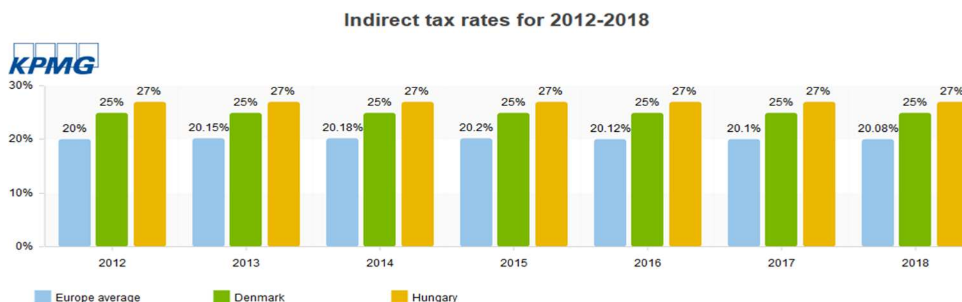

Figure 2: Indirect tax rates for 2012-2018 Europe average, Denmark and Hungary
Source: own processing on the basis of the data provided by
https://home.kpmg.com/xx/en/home/services/tax/tax-tools-and-resources/tax-rates-online.html

A single-rate VAT system is more efficient and its administration costs are lower, a VAT system with several quotas, offers some protection to low-income consumers.
Efforts to harmonise the system consisting of the application of VAT by all Member States focused on two main aspects, namely the uniformity of tax base stemming from the obligation of all Member States to contribute to the Union budget and also the harmonization of tax rates in order to counteract the distortions that high rate differences can induce in the structure of intra-community trade.
Given the failure to harmonise the VAT rates applied in the EU Member States or to bring them between minimum and maximum thresholds without significant differences, fiscal competition is inevitable, its effects being negative and will result, for example, in deviation from the general rule that VAT due or paid to return to the Member State in which the final consumption of the asset takes place.

Thus, a taxpayer in a Member State with a significant tax will prefer to acquire goods from another Member State where the VAT rate is reduced compared to the base Member State. S/He will pay VAT in the Member State with a reduced VAT rate, increasing the tax base of that state, so that then the consumption of goods shall be produced in the Member State with the higher VAT rate. Paradoxically, a Member State that has a high tax rate through a high volume of sales comes to collect less.
In order to combat tax fraud and tax evasion and to reduce VAT collection distortions at Member State level in the action plan proposed by the European Commission (2016), the examination of the way in which intra-Community supplies of goods are dealt with in legislation, the definitive VAT system for intra-Community transactions of goods to taxable persons is an integral part.
Under the new system, cross-border commodity trade shall be treated as a “unique” taxable transaction, which will ensure the taxation of goods in the Member State of goods destination. Thus, the supplier shall levy VAT on the share in the Member State where the goods are delivered.
At the same time, the European Commission also proposes setting up an online portal (“One Stop Shop”) where to have access to all intra-Community economic operators in order to avoid their registration in each Member State. This portal shall also be accessible to non-EU economic agents that want to sell to other entities within the EU and that would then be required to register for VAT purposes in each EU Member State. They will only have the obligation to appoint an intermediary in the EU that shall have the task to manage their VAT obligations for them.
In this context, the only exception is when VAT is payable by the taxable person to whom the goods are delivered, but this depends on the extent to which the company is a “certified taxable person” and the goods are supplied by a taxable person that is not established in the Member State where VAT is due. The initiative on this concept of “certified taxable person” was presented in the Commission's proposal of 4 October 2017.
These new rules will enter into force on 1 July, 2022, with Member States of the European Union being obliged to transpose the amendments to the VAT Directive into national law no later than 30 June 2022.

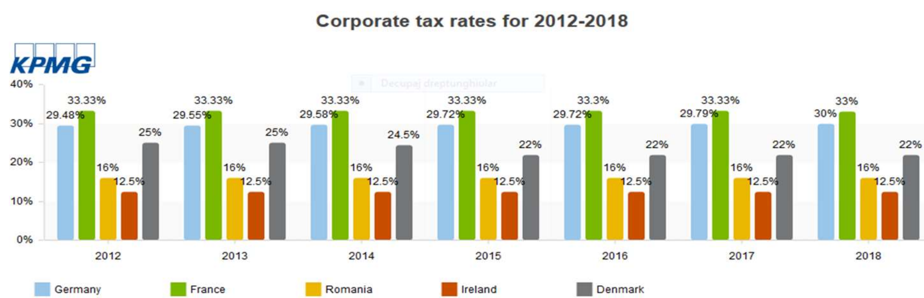

Figure 3: Corporate tax rates in Europe for 2012-2018
Source: own processing on the basis of the data provided by
https://home.kpmg.com/xx/en/home/services/tax/tax-tools-and-resources/tax-rates-online.html

As far as direct taxes are concerned, they are currently set by each Member State. In countries considered the pillars of the EU construction, Germany and France,

“corporate” tax is maintained over the period 2012-2018 at 30% and 34%, respectively. These particularly high - and damaging to the economic growth process - are seriously threatened by relaxed tax arrangements such as Ireland whose direct tax rate does not exceed 12.5% over the past 7 years.
In Latvia and Lithuania corporate taxes are at 15%. Even Austria has reduced corporate tax rates from 34% to 25% in an attempt to make the internal economy favourable to business development but also in attempting to halt the exodus of multinationals and corporations to eastern states. Hungary also reduced the tax rate in a considerable percentage from 19% to 9%, as it can be seen in Figure 4, for the same reasons of fiscal policy.

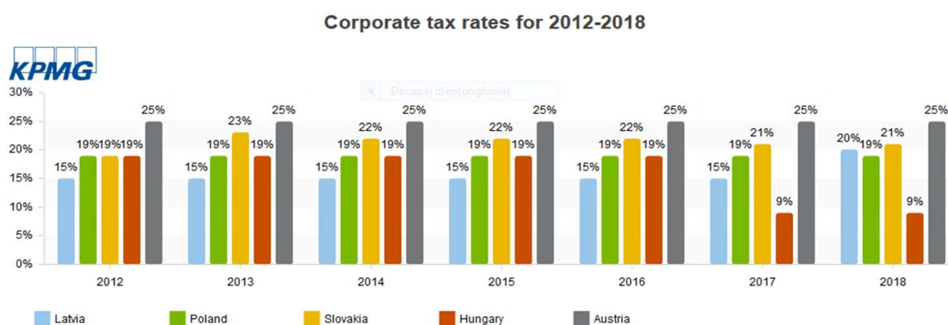

Figure 4: Corporate tax rates for 2012-2018 – different UE members
Source: own processing on the basis of the data provided by
https://home.kpmg.com/xx/en/home/services/tax/tax-tools-and-resources/tax-rates-online.html

Transfer pricing is an economic and tax area under the consideration of control authorities around the world, interested in taxing profits in their jurisdictions. Tax adjustments generated by transfer pricing are among the most important values.
In order to justify the market value of transfer pricing in intra-group transactions, the companies need to prepare a specific documentation, namely the “transfer pricing file” as required by the Order of the President of A.N.A.F. no. 442/2016. Often, pricing between affiliated persons, both in domestic transactions and in cross-border transactions, deviates from the market value principle. Using such prices offers companies the ability to “reallocate their profits or losses in different jurisdictions according to the objectives pursued at central level, with a direct impact on each country's tax position” in which they operate. Tax authorities are interested in taxing real profits earned by companies in transactions with their affiliated persons; where intra-group transactions do not comply with the market value principle, they may make adjustments to revenue and expenditure, adjustments that may lead to double taxation, specific to transfer prices.
Romania follows the approach of the control authorities in the European states. The local transfer pricing legislation included in the Fiscal Code since 2004 contains rules and principles and is complemented by the OECD Transfer Pricing Guide published on 10 July 2017. In 2017 Romania joined as a partner at the BEPS Project Implementation Forum (Base Erosion and Profit Shifting). The new EU directives give the national authorities more freedom to track affiliate transactions and, implicitly, transfer prices, mainly through global information exchanges.

With the entry into force of GEO no. 42/2017 in Romania “automatic exchange of information” between tax authorities became operational. “Country reports” introduced through this order make possible for tax authorities to monitor multinational groups in each country where they operate. The information obtained from the reports will be used by the control authorities for analysing transfer pricing and tax verification of companies that are part of multinational groups.
Transfer pricing affects not only tax companies, but also key performance indicators, cash flow and business strategy. These are the reasons why group companies must argue (in the transfer pricing file) that intra-group transaction prices are in line with the market value principle in order to avoid adjustments proposed by control authorities.
Tax inspections in the field of transfer pricing are carried out for taxpayers for whom there is “a fiscal risk associated with transfer pricing”. The selection of taxpayers subject to verifications of transfer pricing is made, as provided by ANAF in April 2018, taking into account certain criteria: identifying the existence of affiliated parties, the existence of significant transactions with affiliated parties, frequency of their performance, analyzing the taxpayer's profitability, especially if it records losses, taxpayer behaviour, analysis of the taxpayer's economic domain (based on its main CAEN code).
Taxpayers conducting transactions with affiliated persons, irrespective of the significance thresholds mentioned in the Order of the President of A.N.A.F. no. 442/2016, have the obligation, within a fiscal inspection, to prove the compliance with the market value principle, according to the general rules provided by the financial, accounting and fiscal regulations in force.
Romania has a relatively short experience of transfer pricing compared to other countries, being an area where both companies, control authorities and courts have much to refine.

3. Labour Factor between Competition and Tax Harmonisation in the EU

The main problem faced by European economies is labour. Protecting the right to engage in tax competition must be one of the objectives of policy makers, especially those interested in economic development in developing countries.
In the European Union, tax revenue obtained from labour taxation, often withheld at source, is the predominant source for the state budget in most member countries. Labour taxes contribute in proportion of 50% to the formation of tax revenues.
The migration of labor from Romania to other EU member states has created a major shortage of human resources, especially qualified, skilled labour force. This increasingly stronger phenomenon was in the first phase beneficial to the Romanian economy, both by diminishing the unemployment and the social constraints generated by it, and by infusing money into the Romanian market (money earned in the EU member states and consumed in country of origin for investment, maintenance, family.)
There came then the negative effect produced by labour migration from Romania when part of those who left, decided to definitively settle in the countries of adoption, their income not returning to the country of origin, hitting the country's economy already affected by the lack of workforce.
An example of tax competition with questions about legality and morality in the field is the cross-border posting/ delegation of labour force, a phenomenon identified in

Member States with low taxation on labour force or with a low minimum wage, to member countries with a high minimum income level.
This is the case with Germany, which adopted the well-known MiLoG law on 1 January 2015, so the German authorities implemented the legislation on the minimum wage in Germany. This transposes European directives into German law, of course, with the application of national interpretations. Simultaneously with the MiLoG Law (the Minimum Wage Law), the Law on the Posting of Employees (AentG) was adopted, the provisions of which refer to foreign employers who post workers in Germany. According to this law, the former must provide information on the date of commencement and termination of the secondment of each person, the empowered person and the address where the proof of payment of the minimum wage is kept. The provisions adopted by the German state in 2015 aim at removing as far as possible unfair practices of posting employees in Germany. The field where the German law on minimum wages is most applicable is perhaps transport, it having the particularity that the provisions are applicable to it even in situations where the transactions do not concern the German market, being only in transit. Thus, if a driver of a foreign firm enters Germany, he is entitled to receive the minimum wage of EUR 8.84 per hour (a value valid from 1 January 2017, previously being EUR 8.5 per hour) for the period worked in this country. The minimum wage is due for the period worked in Germany and this does not include legal breaks.
At the same time, starting 1 January 2017, employers based abroad should register online their posted employees in Germany using the minimum wage entry registration portal.

4. Conclusions

Establishing a clear and firm legal framework, bringing about a common denominator of regulations on indirect taxes and labor taxation, as well as stepping up the fight against taxing real profits made by companies in dealings with their affiliated persons are major points of interest for decision-makers of the European Union. The concern of international fora to harmonize Member States' tax systems was determined by the practice of tax competition. Applying fiscal solutions as evenly as possible aims to diminish the migration of taxable bases, although perfect and unadulterated uniformity of tax and tax rates is virtually impossible to achieve.
The major impact of successful tax harmonisation at the union level would diminish the tendency for taxpayers to apply tax strategies, not having the possibility to plan their activities by using all the acceptable alternatives within the law in order to reduce their tax costs.
Taxation is of great importance in the construction of the social model, since accepting the idea of needing redistribution in order to reduce inequality, requires that the tax model be approached in such a way as to ensure a maximum of budgetary revenues on one hand, and on the other hand to be equitable respectively not to introduce inequalities in the personal income of taxpayers.
The European Commission is determined to win its struggle to integrate Member States' economies into a single market mechanism.
According to Trovato (2007), the European Union should have the power to set and levy taxes and not just make recommendations to Member States on fiscal policy measures.

The European Union market will not be competitive if certain aspects of national fiscal policies are not harmonised (both by aligning the tax base and the tax rates), so new and new decisions need to be made in this direction; each country must have a functioning market economy and, on the other hand, must face the competitive pressures and market forces within the Union.

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Bio-note

The authors Ioan Cosmin Pițu, Bianca Cristina Ciocanea, Mihaela Luca are students from Department of Doctoral Studies, Faculty of Economic Sciences, "Lucian Blaga" University of Sibiu, Romania.

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