

CONTROVERSIES CONCERNING THE FISCAL COMPETITION AND FISCAL HARMONIZATION WITHIN EUROPEAN UNION COUNTRIES

Irina Ștefana Cibotariu¹, N. Bobițan², Camelia Cătălina Mihalciuc¹

¹Universitatea Ștefan cel Mare, Suceava, Romania

²Universitatea de Vest, Timișoara, Romania

e-mail: irinac@seap.usv.ro

Abstract

The traditional aim of the public authorities, towards creating a fiscal system, is represented by the maximization of the public revenues, depending upon the minimization of distortions over the investments size and positioning. The taxation of corporations' revenues has generated real challenges to governments in the last years, if one might consider the significance of stimulating the entrepreneurship activities, and especially of the corporations' activities on one hand, and the achievement of necessary financial resources so as to comply with the joint interest, on the other hand. The activities of corporations have proved to be an essential factor, specific to the economies of all states, due to the economic and social effects generated by corporations: creating of new employment opportunities, increasing the work productivity, increasing the competitiveness of products or developing the revenues sources, so as to increase the budgetary revenues. Taking into account the conditions of the economic globalization, the multinational companies have had the possibility of reaching the best manufacturing locations, depending upon the conditions available at certain moments on the market. In this way, one might emphasize that these conditions of fiscal nature have influenced the decisions making, concerning the positioning of foreign investments and capital flows, so that each state policy related to taxation of corporations' revenues has to establish the topic of cardinal analysis.

Key words: fiscal competition, fiscal harmonization and corporatist taxation

INTRODUCTION

Issuing the fiscal policy of a state represents an especial and complex decision action, which has to focus mainly upon the efficiency regulation. In this way, reducing the fluctuations, the economic unsteadiness, protecting the revenues and stimulating of economic are taken into account. The taxes and other drawings related to state budget are modifying the initial distribution of revenues, thus influencing the economic activity, the investments and the consumption. One might say that policy within taxation is essential for the state members, and the activities of a country specific to fiscal/financial field might have an impact not only to that country, but also to the neighbor countries.

The multinational companies have the possibility of "delocate the benefits" through financial or commercial transactions, within the group in order to reduce the total fiscal

obligations. A simple method of transferring the profit from countries of high taxation towards the countries with reduced taxation is represented by the lending of loans between branches, knowing that usually the payments carried out by a company are free of tax, while incomings are taxable. Another possibility is represented by the manipulation of prices to products changed between branches: if a branch of a country with high level of taxation produces intermediary products used by branches placed in countries of low taxation, the price at which these assets are transferred between branches can be established at a very low level, thus generating the decreasing of profit in countries of high taxation. These instruments of avoiding the taxation are more easy to use as concerns the European Union, due to the level of liberalization of markets.

As result, the taxation of revenues in corporations within European Union has been partly influenced by the decisions of placing the foreign direct investments (FDI), thus generating a series of distortions on both economical and also social types, at the level of national economies and unique market.

Within this frame, the fiscal competition occurs, where fiscal authorities will try to attract the taxpayers to their own jurisdictions, thus offering the combination of taxes – public assets, due to them.

The total (of both taxation quotas and fiscal basis) or partial (not only of fiscal basis) harmonization represents nowadays the means of solving the existing situation towards taxation of corporations' revenues, being emphasized in tough debates of economists and politicians. Taking into consideration the complex involvements that harmonization of taxes towards corporations' revenues would generate upon the level of all European countries, carrying out a study concerning the progress tendencies of this process was considered to be useful within the present paper.

MATERIAL AND METHOD

Theories concerning the fiscal competition

The fiscal policy has represented for EU one of the instruments that government can use so as to influence the national economies. By means of Treaty of Steadiness and Growth, the fiscal policy has been somehow constrained, since this treaty established that member countries are obliged to ensure the growth of coherency between the fiscal policy requirements on mean term and the challenges of steadiness on long term specific to public finances, so as to limit the excessive deficits. Respecting the rules of discipline within fiscal and budgetary field will determine the general attenuation of public finances quality and will allow to member states to issue the budgetary resources necessary to encourage the investments, the education and to create new labor positions.

The concept of "fiscal competition" was first introduced by Charles Tiebout (1956) and starts with the idea of existence, towards the

public assets, of the equivalent specific to private assets markets. The taxpayers should choose those residences that offer an optimal combination of public assets and taxes. On their turn, the fiscal authorities will try to attract the taxpayer to their own jurisdictions, thus offering a combination of taxes – public assets aimed by these, until an optimal dimension of the taxation basis is reached; in this way, this will allow the minimization of costs specific to public assets which were provided.

The fiscal competition can be defined as a competition between various final jurisdictions, so as to encourage the physical and judicial persons to establish the residency within their area. Considering another approach, the fiscal competition represents the phenomenon by which mobile fiscal bases are attracted by jurisdictions of low taxation. In this way, the fiscal competition might be assimilated to a certain "trespass", when a country applying some types of fiscal stimulants would determine the transfer of some taxation bases of abroad to its own jurisdiction.

The idea of competition is extremely known nowadays. As concerns the fiscal field, the controversies regarding the competition concept are tough. As Grau and Herrera mentioned, the fiscal competition might be considered as a real competition, since finding a parallel between this and the competition of market exchanges is not possible. While the competition on the market of exchanges is submitted to rules determined by the confrontation of supply and demand, the fiscal competition is the result of economic and political interests. Since the fiscal competition is put into effect by the reducing of taxation level to which the capital is assessed, this reducing will be often compensated by rulers in means of increasing the taxation over the work labor. As result, the fiscal competition might be seen as "a game" whose result "the winners" are the owners of mobile factors (as capitals), and the "defeated" are the owners of immobile factors (as the work labor). Ruy V. și Rahn W. mentioned that the result of

competition on the market of exchanges is represented by the growth of economic efficiency, while the fiscal competition has as result the increasing of using the budgetary resources. Reducing the taxation quotas of corporations' revenues to various countries members of European Union, as result of fiscal competition, represents an alignment action to a tendency manifested on international level, being less the result of actions intended to be carried out by rulers. In this way, the fiscal competition will determine a spontaneous convergence of quotas of taxation practiced within different jurisdictions.

The attempts of proving that there is competition between member states of the European Union on attracting the mobile fiscal bases (the capitals) resulted in many analysis within the progress of levels to taxation quota specific to corporations' revenues, the progress of incomings level form the taxation on corporations' revenues and of measuring the fiscal task to which the corporations are submitted to.

As concerns these analysis, two approaches related to fiscal competition can be identified within the specialty literature:

- that according to whom the fiscal competition represents a phenomenon which naturally occurs within globalization conditions, not being necessary nor opportune on fighting against it; in this way, most of times, offering attractive fiscal regimes might be a possibility of counterattack the exogenous disadvantages (as the reduced level of developing new member states within European Union) and of determine an uniform allotment of resources within an area;
- That under assessment that fiscal competition within European Union might determine the occurrence of some harmful tax competition.

Baldwin and Krugman appreciated that until the end of 1990, significant reducing related to taxation quota of companies revenues did not really exist to EU member states, despite an important growth of capital's mobility. Moreover, within the

mentioned time, the incomings on taxes related to corporations revenues increased both as percentage of gross domestic product (GDP) and also as percentage of total revenues. This progress was assigned to phenomenon called "forces agglomeration", according to whom the localization of industrial enterprises is no indifferent towards the economic environment, where the investors preferred the regions where the level of economic development was high. Therefore, a mobile production factor might become half-fixed, whose mobility is influenced in a less percentage over the taxation level. Baldwin and Krugman published a theoretical model of industrial agglomeration, where the fiscal policy, even in conditions of capital's mobility did not determine competitive taxation quota. As result, an excessive competition of the taxation quota could not exist between the "centre" (the old EU member states) and periphery (the new member states), but "a severe competition" between the last two was not excluded either.

The competition within taxation might determine sometimes a reducing of taxes incomings, which might question the possibility of authorities on satisfying the demand of services and public assets. Introducing new overstate rules, by which the minimal level of taxation rates was established, would ensure the provision of public services and assets in good conditions. This idea might be observed to Zodrow G. R. si Mieszkowski P., which stated concisely the necessity of some rules of taxation, common to all member states; by these rules, the collecting of enough fiscal revenues assured, so as to ensure the continuity of providing public services and assets.

The corporations have proven the possibility of using aggressive strategies on avoiding the taxation, which might involve the mechanism of transfer prices, the thin capitalization, the using of organizational structures, lacked of any significant economic activity, in order to operate abroad, and so on. The ability of organizations on using these strategies has offered them an important fiscal advantage towards the national competitors,

so that fiscal competition will bring benefit to high size companies, carrying out activities on national level. Also, the companies disposing of the experience within using the strategies of avoiding the taxation will be in advantage towards the companies being newly established, since to developing countries most of companies newly established might be noticed; making an extrapolation of this thinking, one might say that by fiscal competition, the business of multinational companies of developed countries are encouraged in contradistinction with competitors of developing countries.

In the situation where governments are obliged to accomplish reductions of taxes quota, to offer deductions, fiscal credits and exceptions so as to attract the capitals of previously meet their movement towards more advantageous fiscal jurisdictions, the fiscal competition might generate the wrong allotment of resources within world's economy. In this way, the production activities might be directed towards countries where the cost of production factors is high, but the taxation is reduced. The fiscal competition generates phenomena of spatial focusing of activities and cumulative strengthening of inequalities over the fiscal potential.

According to economists Edwards Ch. and Rugey V., the fiscal competition is harmful, since it determines the reducing of taxation bases to neighbor countries and makes a distortion over the effective allotment of capital and services on international level. To countries where reducing the nominal quota of taxation is aimed to (especially to developing countries), the incomings of assets, services, capitals, qualified labor force will increase, while the neighbor countries will face a reducing of economic increasing. The advantages of which developing countries benefit as result of fiscal competition have though controversial character, according to the opinions mentioned by Avi-Yonah R.

Regarding the point of view of other studies, the fiscal competition has generated the so-called "competition towards reducing of taxes" (or "race to the bottom"), which

might finally lead toward the disappearance of any form of taxation specific to companies' revenues.

Though, there are some opinions according to who the fiscal competition and the fiscal harmonization would not be in a conflict of objectives. In this way, the fiscal competition would encourage the governments to adopt measures of fiscal policy, similar to those promoted in countries that manage to attract capitals by practicing some favorable fiscal regimes. In time, these practices might bring the standardization of fiscal systems to some areas.

Doctrinaire approaches concerning the harmonization of corporatist taxation

The existence of fiscal heavens has generated at the beginning of millennium III new challenges related to taxation. The offshore companies managed to evade from taxation a part of benefit, by means of establishing of branches in countries where taxation is reduced or even not existing and of organizing artificial relationships with them (only on records). Within European Union, the number of fiscal heavens was increased, a situation that represents a potential danger towards the future of European Community. In order to eliminate this danger, various measures were taken: making more severe the rules of establishing the fiscal residence, severe checking of double residence to taxpayers, reviewing the assistance provisions as concerns the recovering of mutual debts, etc.; though, the results of eliminatory actions to harmful fiscal practices have yet remained uncertain.

Concerning the countries of European Union, the fiscal policy has remained one of the instruments which the government might use so as to influence the national economies. Carrying out different national fiscal systems might though represent the origin of many problems:

- influencing (distortion) of resources allotment, with negative consequences so as to capitalize the advantages of a real unique market, but also taking into consideration the point of view on

international distribution of revenues resulted from taxes, fact which might put into disadvantage some member states towards other member states;

- making fragile the budget incomings, by losses form revenues associated to fiscal competition;
- limitation of fiscal sovereignty, including the limitation of possibilities to fight against tax evasion;
- the tendency of increasing the inequality of fiscal systems, by the privileged treatment of mobile bases on imposing;
- the risk of double taxation.

Many specialists and politicians have pronounced for accomplishing a coherent and centralized policy at the level of European Union, so as to solve problems mentioned above. The keyword used by those considering that all member states should align their own fiscal systems towards the executive's provisions of Bruxelles is named "harmonization". One of the most used argues is that Union should have the power of establishing and laying taxes, and not just saying to member states how to do it.

Within specialty literature, many definitions of fiscal harmonization are met. Mainly, these definitions can be grouped in two main categories. On one hand, the fiscal harmonization is associated to the agreements by which the level of a country's fiscal system takes into account the fiscal system of other countries, as well as in situations of avoiding the double taxation or bilateral reducing of customs taxes. On the other hand, the fiscal harmonization is regarded as a complete standardization of the type of taxes, of fiscal bases and taxes quotas. Dossier D. restricted the concept of fiscal harmonization to the fiscal coordination between nations within the process of integration to customs or economic union. Rounds O. said that fiscal harmonization means the reducing of taxes afferent to assets, services or capitals that circulate between some national economies, and Prest A. suggested that harmonization might be seen as a process of organizing the fiscal systems to different countries according to a similar model. Considering the

point of view of Musgrave P., the fiscal harmonization might be seen as a process of adjusting the national fiscal systems, according to a set of common economic rules.

RESULTS AND DISCUSSIONS

The points of view expressed by specialists as regards the fiscal harmonization have been different. The main objections refer to:

- the cancellation of stimulants which result from fiscal competition;
- the restraining of possibilities to public authorities of using the fiscal instruments so as to reach some economical-social objectives.

A neutral fiscal system, generated by the fiscal harmonization within European Union might offer the advantage of eliminating the distortions on taking economic decisions and would allow the correct allotment of resources within unique market. In situation where assets produced by any member state were under taxation identically, the producers would allow to manufacture those assets, so as the costs and production factors to be the lowest. As matter of fact, the fiscal harmonization would favor the competition, thus facilitating the movement between jurisdictions of companies and owners of labor force.

CONCLUSIONS

As general conclusions, one might emphasize that at the level of European Union, the fiscal taxation represents an essential factor on determining the process of placing the investments, and their sensitivity towards the installments of tax is continuously increasing.

In my opinion, the fiscal competition represents a real problem by which the economies of European Union member states are facing with, because of major distortions that this phenomenon might generate. Reducing the level of taxation of companies' revenues, so as to attract foreign capitals, is a measure intended to generate favorable effects to a European country's economy, but only on short term; the competitive advantage

determined by fiscal conditions will be reduced awhile, by adopting certain similar measures by the neighbor states. For instance, at the beginning of 2000, Hungary managed to be placed on top of destinations preferred by foreign investors, by practicing the least quota of taxation on corporations' revenues of European Union. (19,6%). The fiscal practice of authorities in Hungary was fast copied by other neighbor countries: Lithuania reduced in 2002 the quota of taxes on corporations' revenues to 15%, Slovakia in 2004 to 19%, Bulgaria 2005 to 15%, and in 2007 to 10%, Romania in 2005 to 16%. The signals of fiscal nature have been represented an essential factor (together with other factors of economic, social and political nature) of directing the foreign investors (searching for some locations for their capitals) towards those economies. The migration of capitals in their search so as to find the most advantageous fiscal jurisdictions can affect the structural equilibrium of economies specific to their origin countries, but do not generate stimulant effects on long term to economies of host-countries.

Taking into account the financial unsteadiness more and more emphasized, which world economy is facing with, some measures are imposed, by which the fiscal regime should gain efficiency, transparency and simplicity. An uncontrolled fiscal competition within an area characterized by the mobility of production factors (as to European Union) might determine the reducing of budget revenues and might harm the redistributive role of the public finances.

Considering this point of view, the harmonization of corporatist taxation represents a solution for avoiding some disordering over public finances system, but also for ensuring a good operation of the unique market. Certainly, an economic union and a unique market require for a harmonized fiscal system. Therewith, the allotment of resources on this market is preferred that to be accomplished depending upon the competitive economic advantages of countries that carry out on this market, rather than depending upon the reduced level of taxation.

REFERENCES

- [1] Avi-Yonah, R., Globalization and Tax Competition: Implications for Developing Countries, 2003;
- [2] Baldwin, R., Krugman, P., Agglomeration, Integration and Tax Harmonization, CEPR Discussion, Paper No. 2630, Nov. 2000;
- [3] Cibotariu, I.Ș., Nedelea, A., Morariu, A., Cosma I., The Fiscal Effects Resulted from the Appliace of IAS/IFRS on the Companies in the Agricultural Domain, Bulletin of University of Agricultural Sciences and Veterinary Medicine, Cluj-Napoca, p.99-105;
- [4] Garret, G., Mitchell, D., Globalization. Government Spending and Taxation in OECD, European Journal of Political Research, 2001;
- [5] Negrescu, D., Tendințe de armonizare fiscală la nivelul Uniunii Europene. Provocări pentru România, 2008;
- [6] Rugsy, V., Rahn, W., Threats to Financial Privacy and Tax Competition, Policy Analysis no.491, Cato Institute, 2003;