Ladies and Gentlemen,
Honourable Members of the FISC Subcommittee of the European Parliament

I would like to thank the Chair, Mr Tridico, for the invitation to this public hearing.

EU Economy and Competitiveness

The role of tax policy in enhancing the EU's economic competitiveness is closely linked to the current economic conditions we are experiencing today. The EU has emerged from two consecutive crises in the past 15 years – a deep economic crisis and a global pandemic. Geopolitical instability in the region has significantly affected energy costs and price stability, with negative consequences particularly for low-income households and small and medium enterprises. Slow economic growth, as a result of stagnating productivity and slow technological innovation uptake, has become a chronic problem for Member States, thereby impeding the region's economic dynamism. Public finance sustainability in Member States has improved but faces headwinds. Ageing, climate change, and digital transformation pose major challenges for the future of the EU, which will require increased cooperation between countries and a coherent response from all to address them.

A benchmark for Europe's economic trajectory has often been the growth and dynamism of the US economy. The Draghi report has documented a shortfall in competitiveness, especially in the high-tech sector. The compounding effect of higher economic growth in the US compared to the EU has caused a divergence in the two regions' GDP, such that the total GDP of the US economy will be roughly double that of the EU in a few years.

If one can summarise the recipe offered to EU policymakers and country officials in the Draghi report, this will take the form of (a) more support for European innovative companies in a more harmonised single market, (b) improvement in competitiveness through lower energy costs and decarbonisation, and (c) massive additional public investment to achieve these objectives (at least €750 billion annually).

The Role of Taxation in Supporting Competitiveness

Against this backdrop, the most important role taxation can play is by providing part of the additional funds that Europe will require to achieve the competitiveness objectives. A way that this can take place is by expanding the tax base, especially by improving the functioning of the single market, enhancing the taxation of multinational companies, and by increasing the tax progressivity at the very top of the income distribution.

Between 1995 and 2021, the EU average statutory corporate tax rate fell from 35% to 21%. Some EU Member States have particularly low corporate tax rates and offer special regimes that facilitate tax base erosion. A common rate, for instance at the EU average, without exceptions and loopholes, would have simplified the functioning of firms in the single market. Tax base harmonisation, through BEFIT for instance, and digitalisation policies, such as in the

VAT, are low-hanging fruit for EU countries, which are made difficult by the unanimity rule and by country-specific objectives. Closing corporate loopholes and providing a common rate and tax base at the EU level would improve the simplification of procedures, increase competitiveness in the single market, and at the same time provide additional funds to support the EU's competitiveness agenda.

Regarding personal income taxation, recent evidence we have presented in the EU Tax Observatory's Global Tax Evasion Report 2024 shows that the effective tax rates at the very top of the income distribution are significantly lower (about half or more) than those of the general taxpayer population in a country. For EU countries, this is a particularly worrying pattern due to the high labour tax wedge. Based on the evidence we have; it is paramount to improve progressivity at the top 1% of the income distribution. This can take place through wealth taxes and higher corporate income taxes, since wealth and corporations are the main source of income for the highest percentile. To effectively monitor this measure, tax administration coordination should be enhanced by expanding the automatic exchange of information to other asset classes, such as real estate. Additional tax revenue can be hypothecated for growth-enhancing measures, thus shifting economic resources from unproductive to productive activities.

Compromising Anti-Avoidance Regulations: A Dangerous Precedent

Over the past months, competitiveness and simplification have become the main policy objectives of the new European Commission. Some political and interest-group voices were quick in advocating for a link between important objectives set in the Draghi report (which sketched the need for a harmonised publicly funded industrial policy) with those of tax simplification and tax competitiveness. Namely, that competitiveness in the EU will be achieved with lower corporate tax rates and with a more simplified tax regulation for companies. These voices have called for lower rates, a revision of the Anti-Tax Avoidance Directive (ATAD) with higher applicability rules, relaxation of Controlled Foreign Company (CFC) rules, and an increase in the interest limit (from €3 to €5 million).

Based on recent findings in the economic literature, we should all err on the side of caution regarding calls for revision. Firstly, we have no solid economic evidence that lower corporate tax rates spur investment and innovation. On the contrary, we might be risking unwanted side effects such as increasing inequalities since corporate ownership is highly concentrated at the very top of the income distribution. In addition, lower tax rates would mean that we ignore the lessons of the past 40 years that have led countries to a race to the bottom; thus, we would undermine the efforts of the past 10 years in enhancing multilateral tax coordination to reverse this trend. Evidently, these efforts have borne fruit by ending financial secrecy and by introducing a minimum global tax for multinational companies. The current momentum in multilateral taxation favours an expansion of the "pillars" to the taxation of high-net-worth individuals, where a global minimum tax on billionaires will widen the tax base with minimal effect on global economic growth.

Secondly, we do not have sufficient economic evidence to support revisions in the Anti-Tax Avoidance Directive. The Directive has been in place for a few years, and time should be allowed for empirical assessments. Some evidence exists regarding CFC rules, and these indicate that they play a crucial role in deterring the tax avoidance practices of multinational corporations and in preventing companies from shifting profits to low-tax jurisdictions. No sufficient evidence exist that relaxing any of these rules will lead to an increase in investment and innovation.

Thirdly, the overlap of some ATAD rules with Pillar 2 obligations has called for reporting simplifications, a process termed “decluttering”. Caution is needed to correctly identify any double reporting. This can take the form of harmonising the reporting obligations for multinationals without, however, relaxing anti-tax avoidance rules or changing the scope or applicability of the directive.

Closing

All in all, it is essential to approach any calls for tax simplification with caution, particularly regarding lower corporate tax rates, the revision of ATAD, and CFC rules. More time is needed for a proper assessment of the effects of these policies, while there is currently no evidence to suggest that simplification could spur innovation.

The past 10 years have seen an unprecedented evolution of cooperation in multilateral taxation, and this is where our efforts should focus. We should enhance our tax framework to support fair competition across companies regardless of their size and across individuals regardless of their wealth. A well-structured, comprehensive, and progressive taxation system is vital for generating the funds needed to support innovation and public investment, which are critical for the EU's competitiveness objectives. Increasing public funds to support innovation is the most important role taxation can play in improving the competitiveness of the EU's economy.

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