Fiscal Lessons of the Crisis: Beggar-Thy-Neighbour Tax Policies Could Destroy the EU

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EU: The Myth of Unity in Crisis

• ‘Within a single market and major trading bloc like the EU, it makes good sense to coordinate national economic policies. This enables the EU to act rapidly and coherently when faced with economic challenges such as the current economic and financial crises’

• (European Commission: Webpage for Economic and Monetary Affairs)

1. Coordinated Crisis Management?

• October & November 2008 dominated by separate national initiatives to salvage banks (UK, Germany, France, Austria, Netherlands, Spain)

• Some coordination in parallel actions of ECB, BoE and other central banks

• Disappointing G7 meeting in October

• Only 10/11 December produced so-called European Recovery Programme
Consistency?

- The ERP ‘provides a common framework for the efforts made by Member States and by the European Union, with a view to ensuring consistency and maximising effectiveness’
- (European Council Meeting statement 10/11 December)
- What evidence of consistency? Very little

Divergent Imperatives 2008-9

- EU15 Collection of disparate counter-cyclical stimulus packages, sanctioned by Commission; toleration of excessive deficits
- EU10 Imposition of strict pro-cyclical conditions for rapid restoration of PSBR to below 3% (Hungary, Latvia, Estonia, Bulgaria, Lithuania, Romania)

PSBR in the EU27 (2009)

Dominance of Deflationary Imperative (German preferences)

- ‘Even in the midst of the crisis, the Stability and Growth Pact remained the cornerstone for the EU budgetary framework, because it was sufficiently flexible to implement the anti-crisis measures but still provided a framework for the consolidation strategies for the future’.
  (General Report on the Activities of the European Union 2009, p.12)
- Perversely accurate assessment: spirit of EU policy (and non-decisions) continued to reflect obsessive preoccupation with SGP
Divergent effects of Deflationary Imperative in 2009

- **EU15**
  - Delay of stimulus (Germany) and associated coordination
  - Extensive bank salvage measures (26% of EU27 GDP); modest fiscal stimuli but some effect: GDP contraction: -4.4%

- **EU10**: reductions in state expenditure in Bulgaria, Estonia, Latvia, Lithuania, Hungary GDP contraction: -8%

Tax Divergence Pre-programmed EU10 Fiscal Vulnerability

- **EU15 Tax Ratio (2008):** 39.6% of GDP (Greece: 32.6%; Ireland: 29.6%)
- **EU 10 Tax Ratio (2008):** 32.9% of GDP (Latvia: 28.9)

Financing sovereign debt weakened by lack of critical mass of revenue; compounded by current account deficits and exchange rate weaknesses

Source: Taxation Trends 2010

Erosion of Progressivity in Taxation in Europe

- Never an explicit commitment to progressive systems of taxation in the accumulated acquis communautaire;
- Existing systems of PT in all of the EU15 member states were taken as implicit parts of fiscal culture;
- No discussion of flat taxes in any EU15 state before the turn of the century (> German CDU 2005; rapidly rejected)
- Even worse among W Balkan applicants

Higher reliance of EU10 on Indirect Taxes (as % of total revenue)

<table>
<thead>
<tr>
<th>Region</th>
<th>Tax Share (%)</th>
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<tbody>
<tr>
<td>EU10 (CEECs) Average</td>
<td>40.3</td>
</tr>
<tr>
<td>EU27 Average</td>
<td>37.7</td>
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<tr>
<td>EU15</td>
<td>34.8</td>
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EU: Asymmetrical Tax Harmonisation before Global Crisis

• 1990s: opportunity/need for standardisation and harmonisation BUT
• VAT floor-rate of 15% in 1992
• Negative fiscal harmonisation of Maastricht Convergence Criteria (1992) and SGP (1997)
• Indifference to flat tax regimes in Baltic States (1994-5)
• No reference to progressive income tax or direct tax rate minima in Copenhagen Criteria (1997)

Tax Changes after Outbreak of Crisis: Indirect Taxes

• VAT reductions in UK (temporary) & Ireland
• Portugal 2010: From 20% to 21% to 20%!
• VAT increases in nine other member states (six CEECs & 3 EU15 (Sp, Fi, Gre)
• Rise in average EU27 VAT rate to 21%
• Widespread increases in excise duties

Crisis Tax Measures: Direct

• Eleven of the EU15 states reduce direct tax burdens of PIT and CT
• 5 CEE countries provide tax concessions on PIT & CT (Hu, Lith, Pol, Sk, Slo); in three cases (Hu, Lith, Slo) stimulus neutralised by increases in indirect taxes
• Highest PIT/CT stimuli in Denmark (1.6% of GDP); France (1.5%); Germany (1.4%); Austria (1.25%); Sweden (1.1%)

Interim Conclusions on Post-Crisis Tax Measures and Distribution

• Regressive effect, compounding the effects of European tax competition before crisis
• Changes will increase the over-dependence of CEECs on indirect taxation
• PIT/CT concessions concentrated in EU15
• Changes will widen disparities between EU member states and increase inequalities within them
Why taxation?

Dominance of Neo-Conservative prejudices

- Tibor Machan: ‘Liberty is incompatible with taxation … it boils down to extortion’
- Mark Skousen: ‘Taxation is the price we pay for failing to build a civilized society’
- These reactionary prejudices need to be challenged by states and civil society developing a positive discourse of taxation as primary vehicle for lubricating and civilizing capitalism (O.W. Holmes: ‘taxes: with them I buy civilization’)

Functions of taxation

1. Pays for public goods
2. Compensates (partly) for structural market failure: inequalities of capitalist modes of accumulation (as public ‘bad’)
3. Compensates (partly) for cyclical market failure
4. Counteracts self-destructive dynamic of capital logic
   Post-2008 crisis management has addressed 4 but is currently failing to address 1-3

Major contradictions of current GPE in field of taxation

- Internationally mobile corporations and financial services
- National tax sovereignty – deliberately enshrined in EU law
- Low tax jurisdictions – deliberately designed to promote tax avoidance by foreign corporations and ‘high net worth individuals’ (HNWI)
- Relative fiscal impoverishment of states with both high and low tax ratios through ‘tax competition’ – implications for development
- Democratic answerability of states v
- Shareholder answerability of corporations

Tax Avoidance ‘Industry’

- ‘Offshore tax-savings structures with on-shore benefits’ (offshoreconsultants.co.uk)
- ‘Big Four’ (Deloitte, Ernst & Young, PWC, KPMG) and most major banks have large ‘offshore’ departments:
  HSBC (offshore.hsbc.com)
  Barclays (offshore-barclays.com)
  Deutsche Bank (doffshore.com)
  BNP Paribas (securities.bnpparibas.com)
Institutional Capture?

- KPMG Professorship of Taxation Law
- PWC Chair in Financial Accounting
- Ernst & Young Chair in Governance and Compliance (sic!)
- Deutsche Bank Chair of Banking and Financial Services
- BNP Paribas Chair in Quantitative Finance

Political Protection/ Toleration

- Eighteen tax havens are ‘crown dependencies’ of the United Kingdom
- Offshore-companies.co.uk: Choose your tax haven
- EU contains nine states that regularly appear on lists of tax havens
- Three EU states (Austria, Luxembourg, Belgium) have not even signed up to OECD’s Internationally Agreed Tax Standard
- Protection through relativisation: OECD three lists: white, grey, black

Function (not list-status) critical

- Transparency (central to OECD analysis) critical for pursuing tax evasion BUT
- Significant disparities in tax rates/ tax bases/ tax administration are more important as these >
- Drive corrosive tax competition AND
- Reinforce the power of tax avoidance agencies > daily threats to relocate

Crisis as Opportunity (Missed?)

- Partial awareness (EU, UK, Ger, Fra, Italy, US)
- New Focus on Tax Avoidance and Tax Compliance (e.g. Greece)
- BUT both EU and OECD still differentiate between good and bad tax competition
- The EU is guilty of culpable neglect in not establishing minimum standards in PIT/ CT & Failing to coordinate action of tax avoidance
New Austerity as Threat: 1) to Tax Justice

- Austerity weakens state’s power to redress market distribution of income
- Reductions in public goods will affect all, but particularly poor
- Shift to indirect taxation reduces further what remains of progressivity
- Sovereign debt servicing involves redistribution from taxpayers to creditors (incl. Financial corporations)

Austerity: Threat to Recovery

- Crowding-in assumptions are wrong
- Speed of ‘consolidation’ plans are wrong
- Danger of L-shaped depression is high
- Danger of negative growth considerable
- Threat to competitiveness of whole region
- Threat to welfare capitalist model of EU states

Crisis + Austerity Threat to Democracy

- Unequal burden-sharing
- Disproportionate effect on young people:

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<th></th>
<th>EU15</th>
<th>EU27</th>
<th>EU10</th>
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<tr>
<td>Adult unemployment</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2008</td>
<td>6.3</td>
<td>7.0</td>
<td>6.3</td>
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<tr>
<td>2009</td>
<td>8.3</td>
<td>8.9</td>
<td>10.1</td>
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<tr>
<td>Youth unemployment</td>
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<tr>
<td>2008</td>
<td>15.6</td>
<td>14.9</td>
<td>14.6</td>
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<tr>
<td>2009</td>
<td>19.9</td>
<td>20.7</td>
<td>23.1</td>
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Threat to European Union

- Convergence of 1990s is being reversed
- Convergence of EU15 and EU10 has been halted
- Crisis reveals critical fiscal divergence
- Barroso’s fear of fragmentation is totally justified by beggar-thy-neighbour tax policies
- A common EU-tax (Barroso/ Lewandowski) not enough
- Taxation/ regulatory arbitrage could be fatal
Recommendations

- Minimum tax standards for PIT & CT as condition of continuing EU membership
- Strengthening progressivity
- Multilateral blockade of tax ‘havens’
- Concerted legislative programme to outlaw tax avoidance (mobilising support of European taxpayers)

**Don’t waste a good crisis:**
Overwhelming public support for pursuit of destructive and parasitic financial services