EDITORIAL

European Integration Through International Law? The Strange Story of the Global Tax Project

Day after day, the project to reform the current worldwide accepted system of corporate taxation is taking shape, commonly referred to as the global tax project.

At the beginning of March, a deal to back this project was reached within the G7. This informal agreement was upheld by the G7 Finance Ministers meeting on June 5, 2021, in London. In the first days of July, a working Statement drafted within the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting was signed by 139 countries, representing more than 90 percent of the world GDP (Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy – 1 July 2021, www.oecd.org). The Statement sets out that this reform is designed to address the tax challenges arising from the digitalisation of the economy and to ensure a fair distribution of taxing rights among countries concerning the largest multinational enterprises (MNEs), including digital companies. The project is based on two principles. Pillar 1 partly shifts taxation from the country where enterprises are based to the countries where they do business. Pillar 2 establishes a minimum threshold of corporate taxation, provisionally set at 15 percent. According to an Agenda set within the G20, this triumphal march should be finalized in the Fall through an agreement specifying the details of the project.

The innovative character of this prospective reform is uncontroversial and as such was it presented by the world press. The immense wealth and power concentrated in the hands of some MNEs by the opportunities offered by the digital economy upset the historical link between public authority and private individuals and enterprises. More and more, States vie to grant tax advantages to MNEs to lure them within their jurisdiction and, by so doing, enjoy some benefit deriving from the armature produced by their presence on the territory at the cost of renouncing to conspicuous tax revenues and, symbolically more importantly, of creating huge inequalities and humiliating the role of public powers.

In the minds of its proponents, the prospective global tax may put a limit to the race to the bottom, which is featuring the tax competition among countries, which produces a huge transfer of wealth from the States, deprived of ever larger shares of revenues to finance their public policies, to the private MNEs, which further increase their prosperity and power (see the Special Section 'Regulatory Competition in the EU: Foundations, Tools and Implications' edited by Francesco Costamagna (2019) European Papers 123

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and, in particular, P van Cleynenbreugel, 'Regulating Tax Competition in the Internal Market: Is the European Commission Finally Changing Course?' therein).

Looking from the prism of *realpolitik*, the principle of taxation in the country where MNEs do business and earn a profit is primarily aimed at re-shifting the balance of power between States and MNEs. This explains why, paradoxically, this project is advocated by the traditionally most powerful States and not so much by the poor States, which, at least theoretically, should be the main beneficiaries of the redistribution of wealth it may produce.

From a legal viewpoint, this endeavour, noble or not, will not be easily realized. Absent a global authority having the competence to legislate in fiscal matters, the enduring claim to absolute sovereignty by States entails that the global tax project will see the light of the day through its incorporation in a voluntary agreement, which, to be efficient, should gather a universal or quasi universal consent.

All in all, the road to institute a global tax through international, though paved with good intentions, is presumably longer than expected. However, despite these difficulties, it is worth going along it. That road symbolically depicts the overwhelming need to govern the new social and economic dynamics triggered by the new technologies and the difficulties to do it through a decentralised approach. It remains to be seen whether this project will be as revolutionary as it promises and if it will inaugurate a new course in the international economic relations based on a common and fair approach to collective issues.

In spite of the laudable intentions of the Commission and the Parliament, the European Union did not have a prominent place in promoting this project.

The obvious reason for these difficulties is that the competence of the Union in taxation is quite weak and, in particular, does not cover direct taxation. The lack of a solid ground may explain why the feeble attempts by the Commission to promote analogous initiatives in the more integrated European context failed. In the Communication COM(2020) 313 final from the Commission to the European Parliament and the Council of 15 July 2020 on Tax Good Governance in the EU and beyond, the Commission unsuccessfully proposed to anticipate on the European scene the introduction of a minimum corporate tax.

The difficulties are even increasing with the regard to the participation of the Union in the global tax project. In its Communication COM(2021) 251 final of 18 May 2021 to the European Parliament and the Council on Business Taxation for the 21st Century, the Commission, after reaffirmed that "the EU needs a robust, efficient and fair tax framework that meets public financing needs, while also supporting the recovery and the green and digital transition by creating an environment conducive to fair, sustainable and job-rich growth and investment", did not unveil how it can be realized. The Communication proposes to implement a possible agreement on a new corporate global tax through two directives. Pillar 1 of the project should be implemented by a new directive, whose legal basis is not unveiled by the Communication. Pillar 2, the most spectacular innovation concerning the minimum global rate, should be implemented through "the pending proposal for recasting the Interest and Royalties Directive (IRD), which has been in the Council since 2011". In the view of the Commission, the new proposal, lodged in 2020, should be recast to "make the benefits of the Directive (which eliminates withholding tax obstacles to cross-border interest and royalty payments within a group of companies) conditional on the interest being subject to tax in the destination state".

After pointing out that "some Member State held the view that the IRD should go further and set a minimum level of tax in the destination state as a condition for benefiting from the absence of withholding tax", the Commission, optimistically, added that "agreement on Pillar 2 will resolve this issue".

This last passage is crucial to identify the difficulties of the Union in shaping tax policies having a redistributive effect (see the Communication COM(2021) 251 final cit. point 2.2.). Although implicitly, the Commission admitted that international law can attain worldwide a goal hardly attainable by the EU in the restricted European space. At first sight, this appears to be a living paradox. How is it possible that an international agreement may attain, at the global level, a goal unattainable within the limited and by far more integrated European context?

The reason is easily explained by a combination of two factors: the segmentation of the competence assigned to the EU and the complexity and cumbersomeness of its decision-making procedure.

First, the Union cannot use the powers of action bestowed upon it by the Member States to pursue indifferently any objective assigned to it. Expressly, art. 5(2) TEU, laying down the principle of conferral, namely the "Alpha and the Omega" of the integration project, states that "the Union shall act only within the limits of the competences conferred upon it by the Member States in the Treaties to attain the objectives set out therein". This provision has been constantly interpreted in the sense that each competence of the Union has two components: the powers of action and the objectives assigned to it. This bijective relation makes it illegal for the Union to use a means of action to pursue an objective assigned to another competence. The application of that principle to the case at hand entails that, to fight tax competition and to prevent corporate tax rulings, the EU Institutions must use its competence in fiscal matters.

Unfortunately, no provision of the Treaties confers to the Union competence to that effect. Tax competition consists in the exploitation of the disparities of Member States fiscal legislation to grant advantages to private undertakings. The Union does possess the competence to prevent States' actions distorting the competition under art. 107 TFEU, and the competence to harmonise Member States fiscal legislation under art. 115 TFEU. However, these two competences can be hardly combined.

Attempts to qualify tax rulings as State aid hitherto failed to pass the test of the selective advantages, as evidenced by joint cases T-778/16 and T-892/16, where the General Court annulled a decision of the Commission which had qualified two Irish tax rulings as State aid in favour of two Irish subsidiaries of Apple Incorp. (see *Apple Sales International and Apple Operations Europe v Commission* ECLI:EU:T:2020:338).

Nor more successful has been the attempt to harmonize diverging Member States' legislation on direct taxation. Under art. 115 TFEU, the power of the Union is conditional to the demonstration that the disparities among Member States legislation directly affect the establishment or functioning of the internal market. However, for decades, competition between jurisdictions fuelled by diverging Member States' regulations was considered as a magnification of the internal market philosophy, aimed to streamline the resources and create an efficient balance between demand and supply, even at the cost of lowering the standard of protection for collective interests.

But there is a further difficulty of procedural nature. Art. 115 TFEU provision requires unanimity in Council. The fact is that the requirement of unanimity within the Council is, paradoxically, more complex and cumbersome than the requirement of the consent of the parties to an international agreement. Whereas under international law, unanimous consent is required only from the States which intend to become a party to the agreement, under European Law the consent is required by all the States of the Union. This additional requirement confers to each State member of the Union the power to vetoing a further process of integration by the remaining States. To overcome this veto power, recourse ought to be had to an even more cumbersome procedure, namely the enhanced cooperation, which, in practice, never took root in the EU legal system.

Tax competition is a clear example of the perverse effect produced by the requirement of unanimity in an integrated system. Whereas under general international law, every State is free to assess its interest and to opt-out from a new legal regime but it cannot impede others from setting it up, this is precisely the effect of a negative vote in the European system.

The difference is not only theoretical but has far-reached practical consequences. By nature, normative consensual regimes do have a subtle capacity to attract the consent of outsiders. This is likely the intent of the supporters of the global tax project. To properly function, such a project ought to be universal in nature: an objective that will be hardly achieved in the short run. However, the fact that it will be set up, that it will enter into force and produce advantages for its parties, that it will meet the expectations of the international community as a whole, that – last but not least – it is supported by the economic superpowers, could win the resistance of the objectors and trigger a race to join it.

If international law can be used – and it regularly is used – as a factor of disintegration of the European legal space, sometimes it can be used in the reverse sense, namely as a powerful element of integration.

This may be precisely the destiny of the global tax project. Despite their efforts, the EU supranational Institutions are encountering insurmountable obstacles to harmonize the National systems of corporate taxation to reduce, at least partly, the tax competition which thrives across Europe. The conclusion of an international agreement aimed to harmonize tax legislations worldwide could break the deadlock and prompt a corresponding development at the European level.

From a political viewpoint, it could be more convenient for the recalcitrant MS to accept the European Union as the sole actor at the negotiating table, than to run the risk to remain outside a new system supported and participated by all the main global stakeholders. This "international moment" could be even more momentous from a legal viewpoint. In its Communication COM(2021) 251 final cit., at para. 2.2., the Commission maintained that the agreement on the global tax, whose contents are still uncertain, should be implemented through Union's acts. If the Union had the competence to implement that agreement, according to reverse logic, it should have the competence to conclude it. The obvious assumption is that, in the view of the Commission, that competence should be based on the ERTA doctrine, namely on the affectation that the agreement will likely produce on pre-existing EU common rules: presumably, the Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market, and on the Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States, both based on art. 115 TFEU. The equally obvious objection is that very likely none of the two Directives will cover the presumable scope of the agreement, with the consequence that the agreement should be concluded in mixed form.

There is, however, a further possibility. The case at hand illustrates a process of inverse harmonization, whereby the harmonization proceeds from the general to the particular, namely from the global arena to the regional European arena. But, of course, to harmonize a wider or even universal space than Europe, the use of an international instrument such as an agreement is necessary. Indeed, through EU acts, the Union can only harmonize the internal, not the external market. Is it too audacious to contend that the Union alone has the power to conclude the agreement of the global tax on the basis of art. 216 TFEU, which confers to the Union the power to conclude an agreement if "necessary in order to achieve, within the framework of the Union's policies, one of the objectives referred to in the Treaties"?

It is well known that the existence of this implied power was first ascertained by Opinion 1/76 (*Draft Agreement establishing a European laying-up fund for inland waterway vessels* ECLI:EU:C:1977:63) where the Court of justice ruled that "the power to bind the Community vis-a-vis third countries [...] flows by implication from the provisions of the Treaty creating the internal power and in so far as the participation of the Community in the international agreement is, as here, necessary for the attainment of one of the objectives of the (Union)" (para 4). The doctrine was tailored on the factual situation of the case, where an internal regulation not binding for third States would have been manifestly inappropriate to attain its purposes, namely to regulate the navigation on the river Rhine. Yet, the harmonization of corporate taxation shows us a similar factual situation. An internal harmonization preventing the tax competition between Member States by no means could prevent tax competition by third States. It follows that a global agreement may prove to be necessary to regulate an issue that is global in nature.

But is the regulation of tax competition one of the objectives of the Treaties? How can the Union claim to be empowered to participate in an agreement having the objective to harmonize corporate taxation worldwide if it proved hitherto unable to harmonize corporate taxation internally?

A positive answer could be formulated on the basis of the new set of objectives and values of the Union guiding its external action. In Opinion 2/15 (*Free Trade Agreement between the European Union and the Republic of Singapore* ECLI:EU:C:2017:376), after holding that "Article 3(5) TEU obliges the European Union to contribute, in its relations with the wider world, to 'free and fair' trade", the Court went on by adding that "it follows that the objective of sustainable development henceforth forms an integral part of the common commercial policy" (paras 146-147). In Opinion 1/17 (*Comprehensive Economic and Trade Agreement between Canada, of the one part, and the European Union and its Member States, of the other part (CETA*) ECLI:EU:C:2019:341:341) the Court made a further step by qualifying free and fair trade as one of the objectives of the Union (paras 84, 200 and 213). The Court used the objective of free and fair trade to enlarge the scope of the Common commercial policy, namely a policy having a specific objective to be pursued. *A fortiori* it could be used in a situation where the agreement is the indispensable tool to attain that objective "within the framework of the Union's policies", under the very terms of art. 216.

The story of the global tax may thus resurrect the doctrine 1/76, infrequently invoked and even more infrequently used in the international practice of the Union; it can invert the ordinary relation between internal rules and external powers and create a situation where the Union uses its external competence to attain objectives unattainable through domestic measures; it can give a tangible sign that the external action of the Union will be guided by its ethical values and not, or not only, by selfish interests. It can contribute to a new and fairer approach to the global governance of the economy which, after all, is one of the objectives and values of the Union.

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