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Germany

European Tax Harmonization Top Goal For German Finance Minister

By Jabeen Bhatti

Newly appointed German Minister of Finance Olaf Scholz broadly laid out the government's tax and financial proposals for the next legislative period in his first address to Parliament March 22, highlighting plans to gradually dismantle decades-old tax treatments and invest in social and infrastructural programs.

For all of Social Democrat Scholz's talk of dynamism and change, however, attorneys told Bloomberg Tax that such policies signal a continuation of the fiscal ethos of his predecessor, Christian Democrat Wolfgang Schäuble, known for his strict adherence to a balanced budget, conservative tax treatments, and low-cost government spending measures.

Snapshot

- Countries feeling pressure after U.S. cut corporate tax to 21 percent from 35 percent
- Practitioners doubt comments signal sea change

But Scholz's more congenial tone in supporting German-Franco-led European tax harmonization measures, and calls to bolster German investments in the European Union, are an indication that Germany is moving away from unilateral action in favor of European-wide tax policy to keep it competitive, attorneys said. This comes amid pushes in countries like the U.S. and China to offer the most pro-business tax regimes.

“What we saw today was that the general attitude toward finance that started with Schäuble is going to continue—nobody's deviating strongly from what Mr. Schäuble created,” Thomas Busching, a partner with Squire Patton Boggs law firm in Frankfurt, told Bloomberg Tax March 22. “But I'm starting to see more signals that we're moving away from unilateral, country-by-country initiatives.”

If major players within the bloc can manage to round up smaller countries to get in line to harmonize corporate tax rates and accounting procedures, “it would be a huge benefit and relief” for business and tax professionals, he added.

Domestic Treatments More the Same

Beginning with domestic tax treatments, Scholz stressed the new government's plans to gradually dismantle the country's decades-old solidary surcharge—a 5.5 percent levy on income tax, capital gains and corporate tax—to the benefit of middle and low-income earners. The tax was instituted after German reunification and brought in 17.45 billion euros in 2017, according the German Ministry of Finance.

The German government is convinced, given the success of German reunification and the fiscal health of the nation, to put an end to the tax: “We must now find the path out of the solidarity surcharge and the taxes that are connected to it,” Scholz said. “We'll accomplish that in this legislative period.”

According to the government's coalition agreement, it will begin gradually rolling back the surcharge in 2018, with 90 percent of taxpayers free from paying the levy by 2021—a tax savings amounting to 10 billion euros for middle and low earners, with the top 10 percent still required to pay.

While pegged as a cost saving measure to consumers and industry, Oliver von Schweinitz, a partner with GGV law firm in Hamburg, told Bloomberg Tax March 22 that the gradual phase out is a way to still benefit from the groundswell of money from wealthy citizens and businesses for as long as possible—essentially continuing the status quo.

“With the gradual phase out, they have the chance to phase it out for consumers first and businesses going last,” he said. “It creates a strange phenomenon that wealthy people and businesses may eventually face a much higher tax rate just by falling into the bracket subject to the surcharge—eventually there's a cliff.”

Moreover, the 46 billion euros ($56.6 billion) listed in the coalition agreement for government investments into digital infrastructure, school programs and social welfare projects is merely a drop in the bucket for an economy like Germany, Von Schweinitz added. Thus, the investments don't necessarily deviate from former Minister of Finance Wolfgang Schäuble's fiscal conservatism.

“For an economy like Germany, 46 billion isn't that much,” he said. “The government has always been weak at implementing investments—it's just a continuation.”

European Optimism

In his speech, Scholz pledged bolstered spending in the EU, especially as the U.K. prepares to depart the bloc, and indicated that fiscal harmony is crucial to its success. The U.K. will leave the EU in March 2019.

“We have a very crucial national interest and that's that Europe is able to function and that this European Union has a future,” Scholz said. “The politicians active today in Germany and in other countries within the European Union have to guarantee that the necessary steps will be taken.”

Ralph Brinkhaus, a lawmaker in the Bundestag, the lower house of the German Parliament, with Chancellor Angela Merkel's Christian Democratic Union, backed up Scholz's calls for harmonization and heightened investments, saying it's the path to keeping Europe competitive.

“Our tax claim is to make corporate tax law competitive,” he said. “We are ready to invest in Europe to make Europe future-proof—we will not be able to live well in Germany if our neighbors do not also live well.”

But while such calls from France and Germany look good on its face, there hasn't been much momentum on harmonizing the corporate tax base across Europe, Von Schweinitz said.

Now that the corporate tax rate stands at 21 percent in the U.S., and 13.125 percent for a corporation's foreign-derived intangible income, European leaders need to come together to decide if that's the lowest base acceptable —a tough sell to other, business-friendly regimes, like Ireland, with its 12.5 percent corporate tax.

“I don't think Germany and France have sufficient political clout to force the other members to get in line unless they reach a consensus about what the minimum corporate tax rate would be,” he said.

By Jabeen Bhatti

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