Tax Competitiveness – Different Approaches Across Europe

— BY —
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At the beginning of its sovereign debt crisis, Greece undoubtedly had a more competitive corporate tax system than it has today. While other countries used the crisis as the perfect opportunity to develop into tax friendly and tax stable jurisdictions, Greece opted to shoot itself in the foot and become instead a high-tax jurisdiction.

Indicatively, in 2011, the Greek statutory corporate income tax rate was 20%, the eighth lowest among the 36 OECD economies and tenth lowest among the 28 EU member states. In 2018, this tax was increased to 29%, being the eighth and sixth highest in the OECD and EU respectively. The tax on dividends also increased from 10% (in 2014) to 15% (in 2017). At the same time, the average Greek employee is paying more than 50% of his gross annual income in taxes and social security contributions.

The justification for this trend was that tax increases were a natural antidote to Greece's fiscal deficit. In essence, it was the inability and/or unwillingness of the Greek political system to accept what international experience has already proven: that overtaxation kills the economy.

HAS GREECE LOST THE GAME OF INTERNATIONAL TAX COMPETITION?

Two of the other three EU member states that experienced a bailout, Ireland and Cyprus, treated their low corporate income tax rates as sacrosanct and kept them untouched. According to Eurostat, Ireland's GDP growth rate for 2017 was 7,2%, while Cyprus's was 4,2% (Greece's was 1,5%), and unlike Greece, both countries have low unemployment rates. Of course, corporate income tax rates are not the only reason for their recovery; however, they are an indication of how a growth-oriented crisis-stricken economy can face recession. And it is not only Ireland and Cyprus that set an example. Other EU member states—including Bulgaria, Romania, Hungary, Malta, and Cyprus—have adopted a policy of low tax rates, which is reflected in their high GDP growth rates (between 3,8% and 7% for 2017) and low unemployment rates (between 3,7% and 8,5% for 2018). Those jurisdictions have promoted tax incentives that attract foreign direct investments, high-skilled workers, or high-net-worth individuals.

Going in the opposite direction, Greece focused on increasing its tax revenues beyond the abilities of the local economy, while maintaining the anti-competitive features of its tax systems. For example, Greece remains a hostile jurisdiction for holding companies from a tax and financial perspective; this is evident in the fact that three of the companies listed in ATHEX's large cap index have changed (or attempted to change) their seat during the last few years. Instead of watching holding companies migrate or the ownership of local companies kept under newly established foreign holding companies, Greece could have copied holding-friendly measures, such as a participation exemption for capital gains, net interest deduction for equity financing, a less complex system for debt financing, or incentives for repatriated high-skilled employees and managers.

Has Greece lost the game of international tax competition? Statistics and empirical evidence suggest that most likely it has. Can this situation be reversed? International experience also suggests that it is possible, but would require long-term commitment and dedication to a stable, business-friendly tax regime with an equivalent adjustment of public expenditure. Business-friendly fiscal policies lead to growth, while excessive taxation only raises obstacles to business development and competitiveness.