LEGAL MECHANISM OF AVOIDING DOUBLE TAXATION IN THE EUROPEAN UNION

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Annotation. The article titled "Legal Mechanism of Avoiding Double Taxation in the European Union" provides a comprehensive examination of the intricate legal framework established within the European Union (EU) to tackle the pervasive issue of double taxation.

The contemporary landscape of the European Union is characterized by a dynamic and interconnected economic environment, fostering a thriving cross-border business ecosystem. However, this vitality often encounters significant impediments in the form of double taxation, where individuals or entities are subject to taxation in multiple EU member states for the same income or transaction. Double taxation not only creates administrative burdens but also undermines the seamless operation of the EU's internal market.

The article provides a comprehensive understanding of double taxation, delineating its various forms. It highlights the potential consequences of double taxation on businesses and individuals, such as reduced competitiveness, disincentives for foreign investment, and impediments to economic growth within the EU etc.

Against this backdrop, the article delves into the central theme of the legal mechanisms implemented by the European Union to combat double taxation. It recognizes that while taxation is primarily within the purview of individual member states, the EU has intervened with a series of directives, treaties, and judicial rulings to harmonize and streamline tax practices

The article "Legal Mechanism of Avoiding Double Taxation in the European Union" explores the complex and crucial issue of double taxation within the EU. It delves into the various legal instruments, directives, and tax treaties that have been established to prevent or mitigate double taxation, which can arise when individuals or businesses are subject to taxation in multiple EU member states. The article provides insights into key EU directives, bilateral tax treaties, European Court of Justice practice etc.

Key words: double taxation, European Union, economy, business, directives, bilateral tax treaties.

1. Introduction.

In the complex world of international finance and trade, double taxation has long been a challenge that businesses and individuals face when operating across borders. The European Union, with its 27 member states and interconnected economies, has made significant strides in addressing this issue. The avoidance of double taxation within the EU is crucial for promoting economic integration, encouraging cross-border investment, and ensuring a level playing field for all market participants.

2. Analysis of scientific publications.

The issue of the Legal Mechanism of Avoiding Double Taxation was considered in the scientific works of Shmygol N.M, Khodzytska V.V, Morozov S.M., Levytska E.Y., Kovalchuk K.V., Petrova L.V and others.

3. The aim of the work.

The aim of the article "Legal Mechanism of Avoiding Double Taxation in the European Union" is to provide a comprehensive understanding of the legal frameworks and mechanisms established within the European Union to prevent and mitigate double taxation issues.

4. Presenting main material.

The most important determining factor in the development of the world economy today is the globalization of the world economy. It manifests itself in the expansion of international cooperation, the movement of capital, goods and other services, which, in turn, creates double taxation. Double taxation creates such a situation when it occurs the imposition of some taxes on others, and this is inevitably accompanied by negative economic consequences [1, p. 98].

European Union (EU) tax policy consists of two components: direct taxation, which remains the exclusive responsibility of member states, and indirect taxation, which affects the free movement of goods and the freedom to provide services in a single market. There are also rules of administrative cooperation that ensure the proper functioning of the tax system.

In the conditions of the strengthening of globalization processes in the world economic space, the role of interstate coordination of tax policy has grown significantly, because the internationalization of transnational corporations significantly complicated management and ensuring the efficiency and fairness of taxation systems [2, p. 80].

Double taxation occurs when a taxpayer is subjected to taxation on the same income or capital in two or more countries. In the context of the European Union, this situation can arise due to the diversity of national tax laws, which may result in overlapping tax claims on cross-border transactions, dividends, interest, royalties, or other forms of income.

External double taxation, unlike internal, can be eliminated by states both independently and by combining their efforts, that is, by concluding international treaties. The latter is considered the main way to prevent cases of external (international) double taxation.

We must agree that relations regulated by tax and legal norms are always variable, conflicting, arise and develop depending on the goals of the stakeholders. The general and formal nature of tax relations determines several options for realizing the interests of the subjects of tax relations [3, p. 238]

Double taxation has several negative consequences for businesses and individuals operating within the EU as reduced Competitiveness (double taxation can increase the overall tax burden on cross-border economic activities, making them less attractive and reducing the competitiveness of EU businesses in the global marketplace), compliance costs (compliance with multiple tax systems, reporting requirements, and varying tax rates can be administratively burdensome and costly for taxpayers), investment barriers (double taxation can discourage foreign direct investment within the EU, impeding the free movement of capital and stifling economic growth) and uncertainty (taxpayers may face legal uncertainty, as different interpretations of national tax laws can lead to disputes between taxpayers and tax authorities).

Also double taxation causes a decrease in the flow of investments and economic activity of enterprises, which leads to an increase in prices for goods and services and reduction of revenues to the budget of countries. That is why in elimination of double taxation is of interest to both taxpayers and government. The result of inaction in the problem of elimination of the double taxation can be a big tax burden, because of which any economic activity in the country and outside its borders will be economically impractical [4, p. 256].

Within the European Union, a region characterized by a vibrant internal market and free movement of capital, goods, and people, the prevention of double taxation is a crucial element of its economic integration and growth. EU member states have recognized the need for a harmonized approach to address this issue, resulting in a framework of directives, agreements, and mechanisms designed to mitigate the negative impact of double taxation. The prevention of double taxation in the European Union is primarily governed by a combination of EU directives and bilateral tax treaties between EU member states.

Some of the key directives related to double taxation in the European Union include the Parent-Subsidiary Directive, the Interest and Royalties Directive, the Merger and Division Directives etc.

The Parent-Subsidiary Directive (Directive 2011/96/EU) is an important component of the European Union's efforts to promote economic integration and eliminate double taxation within its member states. This directive is designed to facilitate the distribution of profits and dividends between parent and subsidiary companies located in different EU member states.

The directive allows for the tax-free distribution of profits (dividends) from a subsidiary to its parent company, provided certain conditions are met. This exemption helps prevent double taxation of corporate profits within the EU.

To benefit from the directive, both the parent and subsidiary companies must meet specific eligibility criteria, including minimum ownership requirements and a minimum holding period.

The directive also includes provisions to prevent abusive practices and ensure that it is not used for tax evasion or avoidance purposes.

By eliminating barriers to profit distribution within corporate groups across EU borders, the Parent-Subsidiary Directive encourages cross-border investments and the efficient allocation of capital [5].

Overall, the directive plays a crucial role in harmonizing tax rules and fostering economic cooperation among EU member states by ensuring that profits distributed within corporate groups are not subjected to multiple layers of taxation.

The Interest and Royalties Directive (Directive 2003/49/EC) is also an important instrument within the European Union aimed at preventing double taxation and promoting cross-border investments and intellectual property transfers among member states.

The directive ensures that interest and royalty payments made between associated companies in different EU member states are exempt from withholding tax. This exemption encourages the free flow of funds and knowledge across borders within the European Union.

To benefit from the directive, specific conditions must be met, including the requirement that the payer and recipient of interest and royalties are associated companies.

Like other EU tax directives, this directive includes anti-abuse provisions to prevent inappropriate use for tax avoidance or evasion purposes. By facilitating the transfer of intellectual property and the sharing of knowledge within the EU, the Interest and Royalties Directive promotes innovation and encourages investment in research and development.

The Interest and Royalties Directive plays a significant role in harmonizing tax rules within the EU, reducing barriers to the cross-border movement of capital, and creating a favorable environment for businesses and innovators engaged in intellectual property transactions across EU member states [6].

Quite an important place take the Merger and Division Directives. These are two essential directives within the European Union aimed at facilitating corporate restructuring and business mobility while preventing tax obstacles.

The Merger Directive (Directive 2009/133/EC) established a framework for tax-neutral cross-border mergers of companies within the EU. Its primary objective is to simplify corporate restructuring and business mobility by ensuring that such mergers do not trigger immediate taxation of capital gains or other tax liabilities.

The directive allows companies to merge across European Union borders without adverse tax consequences, provided they meet specific eligibility criteria, including the preservation of economic activities. It promotes the free movement of capital and investments within the EU by eliminating tax-related obstacles associated with cross-border mergers [7].

The Division Directive (Directive 90/434/EEC) governs the tax treatment of cross-border divisions of companies within the EU.

Similar to the Merger Directive, it aims to provide a tax-neutral framework for corporate restructuring, ensuring that divisions do not lead to immediate taxation of capital gains or other tax liabilities.

Companies can engage in cross-border divisions without facing adverse tax consequences, subject to certain eligibility criteria and the preservation of economic activities. The directive simplifies administrative procedures and reduces tax-related barriers to corporate restructuring across EU member states [8].

Both directives, the Merger Directive and the Division Directive, contribute to the EU's broader goals of economic integration, harmonization of tax rules, and promotion of business mobility within the single market. They create an environment where companies can restructure and adapt to changing business needs across borders without facing undue tax burdens.

In situations where member states are unable to reach an agreement to eliminate double taxation, the Arbitration Convention provides a mechanism for dispute resolution through arbitration. It ensures that taxpayers have a means of redress when double taxation issues cannot be resolved through traditional channels.

The Arbitration Convention, established by Council Directive 90/436/EEC, is a mechanism within the European Union designed to provide a means for resolving disputes related to the interpretation or application of double taxation treaties between EU member states.

The Arbitration Convention aims to address situations where double taxation disputes arise between two or more European Union member states concerning the interpretation or application of bilateral tax treaties.

Under this convention, an independent arbitration panel is established to help resolve such disputes. The panel typically consists of three impartial arbitrators, including one appointed by each of the conflicting member states and a third, independent arbitrator agreed upon by the two member states involved.

The decisions of the arbitration panel are binding on the member states involved in the dispute. This means that the member states are obligated to implement the panel's decision and resolve the double taxation issue accordingly.

The Arbitration Convention emphasizes a swift resolution process. Member states are required to reach an agreement on the appointment of the arbitration panel within specific timeframes to ensure that disputes are resolved promptly.

The convention typically includes provisions on maintaining the confidentiality of the arbitration proceedings and decisions to protect sensitive taxpayer information.

By providing a mechanism for resolving double taxation disputes in a fair and impartial manner, the Arbitration Convention enhances investor confidence and encourages cross-border investments within the EU [9].

The EU directives that control double taxation are essential tools for fostering economic integration and growth within the European Union. By harmonizing tax rules, facilitating cross-border transactions, and promoting fairness, these directives not only benefit businesses and individuals but also contribute to the overall stability and prosperity of the EU's single market.

As the EU continues to evolve and refine its tax framework, the prevention of double taxation remains a top priority. Businesses operating within the EU should stay informed about these directives, as they play a crucial role in shaping the tax landscape and ensuring a level playing field for all participants in the European market.

Elimination of double taxation through unilateral settlement may lead to unjustified losses of the budget, as well as to various kinds of machinations from the side unscrupulous taxpayers. Also, in this case, the country of permanent residence acts as a donor of the country where it is a citizen (or enterprise) carry out economic activity. At the same time, unilateral avoidance of double taxation does not solve the problem the problem is also because each state faces a task and how ensure a sufficient level of tax revenues to the budget, and how create optimal conditions for economic development. As a result, a lot countries refuse this way of eliminating double taxation [10, p. 266].

Bilateral tax treaties in the European Union, also referred to as double tax treaties or DTTs, are agreements made between two EU member states to regulate the taxation of income and assets in situations where double taxation could otherwise occur. These treaties aim to provide clarity and avoid overlapping taxation by specifying which country has the primary right to tax specific types of income or capital. Bilateral tax treaties promote economic cooperation and the free flow of capital, goods, and services within the EU while allowing individual member states to maintain certain tax sovereignty and tailor agreements to specific economic relationships. These treaties are an essential part of the EU's broader framework for preventing double taxation and promoting fair tax practices.

These treaties often include provisions for the exchange of tax information between the contracting states. This helps prevent tax evasion and ensures that taxpayers comply with the tax laws of both countries.

Also to avoid abuse of the treaty, most agreements contain provisions to prevent taxpayers from claiming benefits twice, either within the same treaty or by using similar agreements with other countries.

European Union member states may also enter into bilateral tax treaties with each other to prevent double taxation. These treaties establish rules for the allocation of taxing rights between the countries involved, and they often incorporate principles of the Organization for Economic Co-operation and Development (OECD) Model Tax Convention.

The Multilateral Convention to Implement Tax Treaty-Related Measures to Prevent Base Erosion and Profit Shifting (MLI) is another mechanism that can impact double taxation. It allows countries, including EU member states, to modify their existing bilateral tax treaties to implement measures aimed at preventing tax avoidance and treaty abuse.

MLI is a significant international treaty developed by the Organization for Economic Co-operation and Development and the G20 countries. It is designed to address issues related to tax avoidance and profit shifting by multinational enterprises.

The primary objective of the MLI is to modify existing bilateral tax treaties between participating countries to prevent base erosion and profit shifting. It is part of a broader effort to combat tax avoidance practices and ensure that multinational companies pay their fair share of taxes.

The Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) is a tool for countries to collectively address tax avoidance issues by modifying their existing bilateral tax treaties. It is part of a global effort to create fairer and more effective tax systems in an era of increasing cross-border economic activity [11].

Also, the European Court of Justice (ECJ) plays a significant role in resolving disputes related to double taxation within the European Union. ECJ decisions concerning double taxation typically revolve around interpreting and applying EU law to ensure uniformity and fairness in cross-border tax matters among EU member states.

Its decisions contribute to the harmonization of tax practices, the promotion of free movement, and the protection of taxpayers' rights in the context of cross-border transactions. ECJ rulings are pivotal in ensuring a fair and unified approach to taxation across European Union member states [12].

It is important to note the presence of a unique project as the Common Consolidated Corporate Tax Base (CCCTB). It is a proposed framework for corporate taxation within the European Union. While it has not yet been fully implemented, it represents a significant step toward harmonizing tax rules and preventing double taxation within the EU.

Its aim is to establish a harmonized set of rules for calculating the taxable profits of multinational corporations operating within the EU. This harmonization is designed to reduce complexity and inconsistencies in tax regulations among member states.

Under the Common Consolidated Corporate Tax Base, companies would apply a single set of rules for determining their taxable income, rather than adhering to different national tax regimes. This simplifies compliance and reduces administrative burdens for businesses operating in multiple EU countries.

One of the central features of the CCCTB is the option for companies to consolidate the profits and losses of their EU subsidiaries and parent companies. This consolidation approach helps eliminate mismatches and offsets profits and losses, ultimately reducing the overall tax liability.

The Common Consolidated Corporate Tax Base introduces an apportionment formula to distribute taxable income among EU member states where a multinational corporation has a presence. This formula considers factors like sales, assets, and labor, aiming to allocate profits to countries where genuine economic activity occurs.

While the CCCTB establishes a common set of rules, it does not introduce a single EU-wide corporate tax rate. Instead, it allows member states to apply their own tax rates to the apportioned profits, respecting their national sovereignty in setting tax rates.

It also includes provisions to prevent tax avoidance and profit shifting, ensuring that companies pay their fair share of taxes within the EU.

The Common Consolidated Corporate Tax Base represents a significant effort by the EU to create a more consistent, transparent, and business-friendly tax environment across its member states. While its implementation has faced challenges and remains a topic of discussion, it holds the potential to enhance the single market, promote cross-border investment, and reduce tax-related obstacles for businesses operating within the EU [13].

While the EU has made significant progress in the prevention of double taxation, challenges remain, including the need for ongoing adaptation to evolving economic realities and the importance of addressing issues related to tax evasion and avoidance. Nevertheless, the EU's commitment to fair tax practices and economic cooperation remains steadfast.

As the European Union continues to evolve and strengthen its economic integration, the prevention of double taxation will remain a central theme in shaping the tax landscape. The EU's dedication to finding equitable and efficient solutions to these challenges underscores its commitment to fostering prosperity and stability in the region and beyond. In the globalized world of today, effective prevention of double taxation is not just a matter of economic efficiency; it is a cornerstone of international collaboration and shared prosperity.

The prevention of double taxation within the European Union is a multifaceted endeavor that reflects the EU's commitment to fostering economic integration, promoting fair tax practices, and facilitating cross-border activities. Through a carefully crafted framework of directives, bilateral tax treaties, and cooperation mechanisms, the EU has taken significant steps to alleviate the burden of double taxation on businesses and individuals alike.

It's important to note that while these documents and mechanisms aim to prevent double taxation within the European Union, the specific rules and procedures may vary from one member state to another. As tax laws and regulations can change, it is essential to consult with tax experts or authorities for the most up-to-date information and guidance on double taxation issues within the European Union.

5. Conclusions.

In conclusion, the legal mechanisms for avoiding double taxation within the European Union represent a significant milestone in the development of a harmonized and efficient tax system across member states. The EU has recognized the challenges posed by double taxation and has implemented a comprehensive framework to address these issues.

Through a combination of EU directives, bilateral tax treaties, and the jurisprudence of the European Court of Justice, the EU has strived to create a fair and balanced environment for individuals and businesses engaged in cross-border activities. These mechanisms promote economic growth, investment, and the free movement of capital, ultimately strengthening the EU's internal market.

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